

## Economy

### RAISING PRODUCTIVITY IN SMALL TRADITIONAL ENTERPRISES

- ▶ Mexico has the widest labour productivity gap between small and medium-sized enterprises (SMEs) and large firms across OECD countries, with the productivity gap between small enterprises of up to 50 employees and large firms particularly big.
- ▶ Increasing productivity levels in small enterprises holds the potential to revive productivity growth and reduce income inequalities.
- ▶ Mexico is taking measures to support productivity growth in small enterprises, including a new fiscal regime aimed at fostering the formalisation of informal entrepreneurs and innovative programmes that combine the upgrading of managerial skills with ICT adoption.
- ▶ Institutional arrangements have also improved. The National Productivity Committee was created in 2013, contributing to the administration's productivity programme, which includes the government's strategy for raising productivity in an inclusive fashion.
- ▶ However, additional structural reforms to reduce regulatory burdens on business are important. Moreover, new programmes fostering productivity growth at the firm level could be developed that target groups of companies (rather than individual firms) and/or prioritise industrial modernisation.

#### What is the issue?

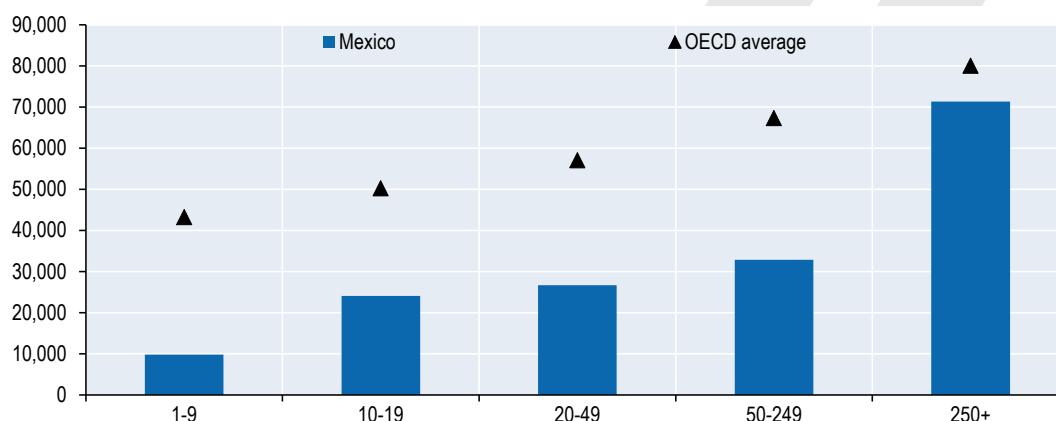
Like many OECD countries, Mexico is experiencing a slowdown in productivity growth. A particular concern for Mexico is the very low productivity level of SMEs. In fact, Mexico has the lowest labour productivity levels across all SME size classes within the OECD area (see Figure) and the widest productivity gaps between SMEs and large firms, in part due to the relatively high productivity of its large business sector. Labour productivity in Mexican micro-enterprises with 1-9 employees is only 14% of that in large companies of more than 250 employees (OECD average of 55%). For very small

enterprises (10-19 employees) the proportion is 34% (OECD average of 64%), for small enterprises (20-49 employees) it is 37% (OECD average of 73%) and for medium-sized enterprises (50-249 employees) it is 46% (OECD average of 85%). These figures do not include workers in informal employment relationships, which accounted for 57% of the Mexican labour force in 2016.

Mexico recognises the importance of strengthening productivity growth to revive economic growth and bridge income inequalities. In 2013, the government launched a

#### Labour productivity levels in Mexican SMEs lag far behind the OECD average

Labour productivity levels (value added per person employed) by firm size (number of employees), 2013, PPP USD



Note: Data refer to the whole business economy (industry, construction and market services), excluding financial services activities.  
 Source: Calculations based on OECD (2016), *Entrepreneurship at a Glance*, OECD Publishing.

strategy to “democratise” productivity and established the National Productivity Commission to provide advice on productivity-related policies. Under this framework, the 2013 fiscal regime for incorporation (Régimen de Incorporación Fiscal) offers discounted rates, over a 10-year period, on the personal income tax rate of small business owners whose annual revenues do not exceed MXN 2 million. Likewise, the 2016 Financial Inclusion Action Plan stresses the importance of access to finance for small businesses.

The federal government also manages specific programmes targeted to micro and small enterprises, such as business incubators for “basic enterprises” (empresas básicas), a programme on micro-franchising, and one which encourages the upgrading of managerial skills and ICT adoption in micro-enterprises. The latter, launched in 2015, takes an innovative approach whereby micro-enterprise owners receive six hours of basic management training and an electronic tablet which includes a business administration software programme and a point-of-sale terminal to accept credit card payments. Over 2015-16, more than 70,000 companies were expected to participate in this programme budgeted with MXN 660 billion (about USD 34 million) thanks to low per-enterprise implementation costs.

Despite these efforts, a number of challenges persist. Informality is still extensive, with the share of workers in informal employment relationships amounting to 57% in 2016 (down from 60% in 2012). The informal sector plays an important role in providing jobs, but is a drag on productivity growth and social inclusion in the long term. Moreover, productivity levels in small and large companies continued to diverge over the 2000s, with labour productivity growing by 5.8% per year in large firms, but falling by 6.5% per year in micro-enterprises. Evidence suggests that there is no “silver bullet” to combat informality, yet a package of policies can help promote formalisation, including enhancing workers’ skills, encouraging investment in productive areas, improving the tax system and labour regulation, and deterring corruption.

At the same time, with 3.2 million small enterprises in Mexico, new programmes to support productivity growth at the firm level could be tested where groups of firms, rather than individual firms, are targeted. This would allow for economies of scale in programme implementation and knowledge spillovers among participating firms. An example is Chile’s PROFO (Proyectos Asociativos de Fomento), which supports groups of companies that jointly wish to improve management practices or find solutions to common production challenges. Similarly, access to finance for small businesses remains a challenge, especially in rural areas, which calls for scaling up well-performing initiatives such as the federal loan guarantee programme.

## Why is this important for Mexico?

Much of the recent SME policy debate in Mexico, as in other countries, has focused on the impact of high-growth firms and start-ups on economic growth and job creation. While the economic relevance of these companies is clear, they constitute only 10-15% of the entire population of firms in any given country. It is therefore important to give due attention to the bulk of established small enterprises, which account for 51% of total employment in Mexico. Given the large number of people employed in these firms, boosting their productivity levels will lead to stronger productivity growth and social inclusion, two objectives at the core of the government strategy to “democratise” productivity.

## What should policy makers do?

- ▶ Encourage worker and managerial skills upgrading, ICT adoption and industrial modernisation (i.e. the acquisition of new machinery and equipment) by small companies.
- ▶ Make the business environment more conducive to business growth, including by easing local administrative and regulatory burdens.
- ▶ Consider introducing a new programme which targets groups of firms rather than individual firms.
- ▶ Increase the outreach of the federal loan guarantee programme as an effective tool for advancing the financial inclusion of small companies.
- ▶ Evaluate the impact of existing targeted programmes for small enterprises on productivity growth at the firm level with a view to scaling up successful programmes and phasing out or adjusting those that have not performed well.
- ▶ Co-ordinate the collection of income taxes and social security contributions and strengthen enforcement of these obligations on large formal firms employing informal workers.
- ▶ Strengthen awareness of in-work subsidies for formal workers.



## Further reading

OECD (2017), *Financing SMEs and Entrepreneurs 2017: An OECD Scoreboard*, OECD Publishing, forthcoming.

OECD (2016), *Increasing Productivity in Small Traditional Enterprises: Programmes for Upgrading Management Skills and Practices*, paper available on OLIS, CFE/SME(2016)6.

OECD (2014), *A Strategic Framework for Entrepreneurship and SME Policy Development in Mexico*, OECD report prepared for the federal government of Mexico.

OECD (2013), *OECD Studies on SMEs and Entrepreneurship – Mexico: Key Issues and Policies*, OECD Publishing. <http://dx.doi.org/10.1787/9789264187030-en>