



# **The Determinants of Private Sector Performance in Mozambique: A Case Study of Small and Medium Scale Tourism Firms**

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ICBE-RF Research Report No. 18/11

Investment Climate and Business Environment Research Fund  
(ICBE-RF)  
[www.trustafrica.org/icbe](http://www.trustafrica.org/icbe)

Dakar, November 2011

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This research study was supported by a grant from the Investment Climate and Business Environment Research Fund, jointly funded by TrustAfrica and IDRC. However, the findings and recommendations are those of the author(s), and do not necessarily reflect the views of the ICBE-RF secretariat, TrustAfrica or IDRC

## **Executive Summary:**

Mozambique has been one of the fastest growing economies in Africa, since the mid 1990s. One of the major contributors for this growth is the tourism sector, thanks to its natural comparative advantage: a long coast with yet unexploited natural assets. In fact since the end of the civil war, the sector has improved markedly in line with the general trend of the rest of the economy. From 1995 to 2007 the total investment in the sector amounted to 1.8 billion US\$, almost 14% of the same period authorized projects. Just in 2006 alone close US\$ 200 million was invested and the physical hotel capacity is reported to have grown by more than 50% in the last 8 years.

To take advantage of the reported new trend, in her current strategic plan, the government expects to put in place measures to transform Mozambique into what she calls a “vibrant, dynamic and exotic destination in Africa” by the year 2020. Achieving this objective however, will require massive government and private sector investment in both hard and soft skills for structural transformation of the indigenous private sector operators. In the absence of such transformation, the SMEs involved in hospitality subsector of the tourism sector in Mozambique will at best be marginal contributors to envisioned future. Currently, they are poorly managed, lacking in social capital skills against a background of harsh market conditions for input. Reflecting the severity of the three reported problems, labour productivity is in general low and decreases when one move from micro to medium scale firms.

The introduction of measures to increase competition for supply of input may help in reducing prices, increasing the availability of goods and indirectly improve the working conditions of local firms. Second, from government perspective it pays off to invest in creating management skills as well as tourism sector related skills. Both skills have a potential to change the current state of the relatively large firms, which is now disappointing. More reforms are required from the managers. Managers should invest in building social capital development, particularly, with clients and workers as the pay off for this is positive.

## Contents

Executive Summary: .....	ii
Contents.....	iii
1. Introduction .....	4
2. Problem Statement.....	5
3. Objectives.....	6
4. Significance of the Study.....	6
5. Methodology .....	7
6. Description of tourism sector trends.....	9
6.1 General Business Environment .....	9
6.2 Tourism Trends in Maputo, Sofala and Nampula .....	11
7. The State of the Small and Medium Scale Tourism firms in Mozambique .....	13
8. The Determinants of firm Performance.....	16
8.1 Human Capital and Firm Performance.....	16
8.2 Social Capital .....	18
8.3 Management Practices and Firm Performance.....	19
8.4 Regression Analysis .....	22
9. Conclusions and Recommendations.....	25
References .....	27
Appendix:.....	28

## **1. Introduction**

Like many other African countries, Mozambique has been implementing political and economic reforms since the 1980s. These reforms were intended to reverse the deterioration of economic conditions, promote economic growth and strengthen democratic institutions under a market-based economy. In 1990 the authorities introduced a new constitution in favor of the private sector, market forces, and a multiparty democracy. Following three years of negotiations, the government sealed a peace agreement with the opposition movement in 1992, and the country held the first multiparty elections in 1994.

These political changes happened besides rapid economic reforms. From 1987 to 2000, the government removed controls over most prices of goods and services and privatized more than 1200 state companies (Anderson and Boo Sjøo, 2002). It further lifted controls of interest and exchange rate in 1994 and 1996, respectively. In order to improve the performance of the private sector it introduced several measures, including: (i) Setting up industrial free zones, (ii) adopting tax incentives, (iii) importing and exporting tariff reforms; (iv) establishing special credit lines for small and medium enterprises. More recently, the government launched a nation-wide public sector reform strategy with a view to improve its efficiency.

By Sub-Saharan Africa standards, the results achieved are impressive and various reports consider the country one of the most successful reformer in the continent. From 69%, the incidence of poverty declined to 54% in 2005. GDP growth rate averaged 8.5% per annum from 2000 to 2005 and the private investment growth rate responded increasing from negative 8% in 1996, to 4.4% in 2003 (IMF, 2005, INE, 2008). In the last five years private investment as a percentage of GDP is reported to be close to 18% in 2007 (INE, 2008).

Researchers studying the underlying causes for this improvement have been unanimous on pointing out to increased macro and political stability, liberalization and privatization (Banco de Moçambique, 2009, IMF, 2005). While they also agree regarding the need for further public sector reforms, they do not clarify several puzzles of the Mozambican

economy. First, and unfortunately, privatization has had mixed results. While some firms managed to go through internal reforms and became competitive, others simply failed, output declined and labor unrest and dissatisfaction increased. Apart from the traditional public sector constraints widely discussed in the literature, this calls for the examination of social and management dimensions of those companies that were underperforming. What features in terms of social, physical as well as human capital and organizational culture do they share? Can these features explain better their performance rather than the company external factors?

Using descriptive statistics and regression analysis based on a data set collected from 174 small and medium scale tourism firms in Mozambique, this paper presents and discusses the results that can help in responding to the above questions. The starting hypothesis is that internal factors related to lack of appropriate management practices, poor social capital and human capital constraints constitute the most important binding barriers for the global development of Mozambique`s small and medium scale tourism firms in particular and the private sector in general.

The rest of the paper is organized as follows. Section two resumes the problem statement. The objectives and the relevance are presented in section three and four. Then, follows the methodology in section five. Section six presents the description of tourism sector trends. In the last two sections, the main development in the small and medium scale tourism firms are discussed and the paper closes with the conclusion.

## **2. Problem Statement**

Privatization has had mixed results in Mozambique. While some firms managed to undergo internal reforms and became competitive, others simply failed. Using a sample of small and medium scale tourism firms, this paper proposes to explain the human, social and management dimensions of those companies that were underperforming. What features in terms of human, social capital and management indicators do they share? Can these features be related to their performance?

### **3. Objectives**

This paper proposes to investigate the determinants of firm performance. Using a sample of 174 small and medium scale tourism firms in Mozambique, it specifically intends to:

- (i) Investigate the relationship between the various indicators of human capital, social capital and firm performance
- (ii) Investigate the relationship between various indicators of management practices, , and firm performance
- (iii) Discuss the private sector response to government and market failures
- (iv) Draw policy recommendations for targeted policy interventions

### **4. Significance of the Study**

The proposed research is crucial for the current debate on the private sector development in Mozambique. The available literature insist on pointing out to government constraints to growth, under the assumption that once these constraints are removed the private sector will respond accordingly and the country will definitely enter into a virtuous circle of growth and development. While this may be true in other nations, for Mozambique and probably for some other African countries it may not be and the available evidence seems to support this position.

In the last 20 years Mozambique has been implementing structural reforms for fostering a private sector led growth. Since the peace agreement of 1994, growth has indeed been happening and the public sector and foreign resources have been driving it. Although private investment from locals is reported to be expanding, foreign direct investment comprises a significant share of total flows.

Furthermore, privatization of small and medium firms has had mixed results and globally seems to have been detrimental to employees. In a recent report, Webstar et al (2005) present a dismal picture of management practices in most Mozambican firms. The necessary prerequisites for productive labor relations were frequently ignored. Workers on the shop floor had no organizational structures in most companies visited and management practices followed top down approaches with rampant violations of workers' rights, lack of incentives and firm level institutionalized dialogue spaces.

Taken together, these arguments call for the simultaneous search of both internal and external constraints for private sector performance, if the objective is to create an enabling environment for sustainable development. By opening the issue of social and human capital management practices in the tourism industry, the study may help in explaining why enterprises subject to the same policy environment along with factor and product market conditions perform differently.

Within the private sector, the tourism industry has been expanding at faster rates and the sector is seen as promising for poverty reduction. Given the country's comparative advantages, together with agriculture, the tourism sector takes the lead in the country's development agenda, implying that the results of the proposed research will also be of great relevance for improving the quality of economic dialogue between the private sector and the authorities. By raising issues related to social networks and the response of the tourism private sector to market, policy and institutional failures, the proposed research will definitely shade some light about the social cost within firms with respect to delayed reforms in one of the most important sectors in the country's development.

## **5. Methodology**

The research proposed was conducted using a sample of 174 small and medium tourism firms out 1080 that that existed on the National Institute of Statistics data set. These firms were defined as those entities specialized in providing various services including accommodation, meals and entertainment.

The survey covered three main geographic areas: Maputo, Sofala and Nampula. The distribution of firms surveyed was : 60 for the Maputo, 52 for Nampula and 62 for Sofala. The number of firms were defined taking into account the distribution of firms in the three provinces, using data from previous survey conducted by the National Institute of Statistics (INE) on SMEs in Mozambique.

Both the study area and the tourism firms were chosen because they offered a fair base for responding to the study objectives, within the time span defined for the project. .As reported in the last section, the tourism sector is one of the fastest growing sectors in the

economy. Despite that, unfortunately one finds a diversity of firms operating below their optimal capacity with increased labour dissatisfaction and poor performance.

The literature offers a diversity of perspectives of the concept of social capital and how it is related to firm performance and development. For example, Putman (1995) defines social capital as elements of social organization such as networks, norms, and social trust that ensure cooperation for mutual development. Similar definition is given by the World Bank (2000a) , which defines social capital as norms and social relations prevalent in social structures whose prime role is to facilitate people coordination and achievement of shared objectives.

While these two definitions shade some light on the dimensions of social capital, they are not consensual as it is difficult to capture their global dimension. Like Anne (2004) This paper follow Fukuyama and define social capital as being linked to other persons. It is a way to avoid moral hazard in any adverse context. As derived from an administered questionnaire, the presence of social capital is captured using the following indicators: positive interaction with suppliers; costumers and employees.

The paper adopted a general definition of management practices to discuss their impact on sales. It is taken as a set of institutionalized procedures within a firm summarized under the human resource management practices. In this way, it was proxied by the following indicators: (i) the presence of planning; (ii) skills training; (iii) communications procedures; and (iv) the presence of quality control mechanism.

To investigate the impact on firm performance proxied by the revenue per labour ratio of the above mentioned variables, we followed two approaches. First we grouped the firms by size and quintile of the revenue per labor ratio and tried to understand their profile in terms of management practices indicators as well as human and social capital variables. Second, a regression equation was fitted following the information obtained when discussing the profile of firms by size and revenue quintiles. The equation fitted is:

$$Y_i = \beta_0 + \beta_1 S_i + \beta_2 C_i + \mu_t \dots \dots \dots (1)$$

Where S stands for the above mentioned indicators of social capital and management practices variables for each firm and C represents a set of control variables, including operating cost labor ratio. The variable  $\beta_1$  and  $\beta_2$  represent a vector of parameters associated with each indicator of social capital, management practices indicators and control variables.

The data from the three sites was aggregated in unique sample, using location specific dummies to control for regional specific characteristics. The study also looked for the impact of social capital, and management practices indicators on with and without the operating costs per labor ratio and the number of workers.

## **6. Description of tourism sector trends**

### **6.1 General Business Environment**

Mozambique has enjoyed significant improvement on her major macroeconomic indicators. From a level as high as 70% in 1994, inflation declined to below 6% in 2007 (Banco de Moçambique, 1995, 2008). With the implementation of new ventures including natural resource based megaprojects, the country's export base doubled. In line with that performance in the last 10 years, the economic growth on average was 7%, making the country one of the fastest growing economy in sub-Saharan Africa.

The table below presents the structure of the country GDP between 2006-2007. The main drivers of growth were agriculture, livestock and forestry with 23%. The manufacturing sector, commerce, transport and communication made more than 30% of GDP. The contribution of the tourism sector, as measured by the share of accommodation, restaurants and similar, on GDP remained constant in the last two years (1.6%) between 2006 and 2007.

**Table 1: Mozambique GDP Structure at constant price (2006 and 2007)**

	<b>2006</b>	<b>2007</b>
<b>Description</b>		<b>National</b>
<b>Gross Domestic Product</b>	<b>100.0</b>	<b>100.0</b>
Agriculture, livestock and forestry	22.9	22.9
Fishery, Aquaculture, and related services	1.6	1.6
Minerals	1.0	1.3
Manufacturing	14.0	13.3
Electricity and Water	5.5	5.6
Construction	3.2	3.2
Commerce	11.0	10.9
Repairing services	0.4	0.3
<b>Accommodation, Restaurant and Similar</b>	<b>1.5</b>	<b>1.6</b>
Transport and communication	9.7	10.0
Financial services	5.1	5.6
Housing and services to firms	8.1	7.7
Public administration, Defense and Social security	3.6	3.6
Education	3.5	3.7
Health	1.2	1.3
Other services	1.8	1.7

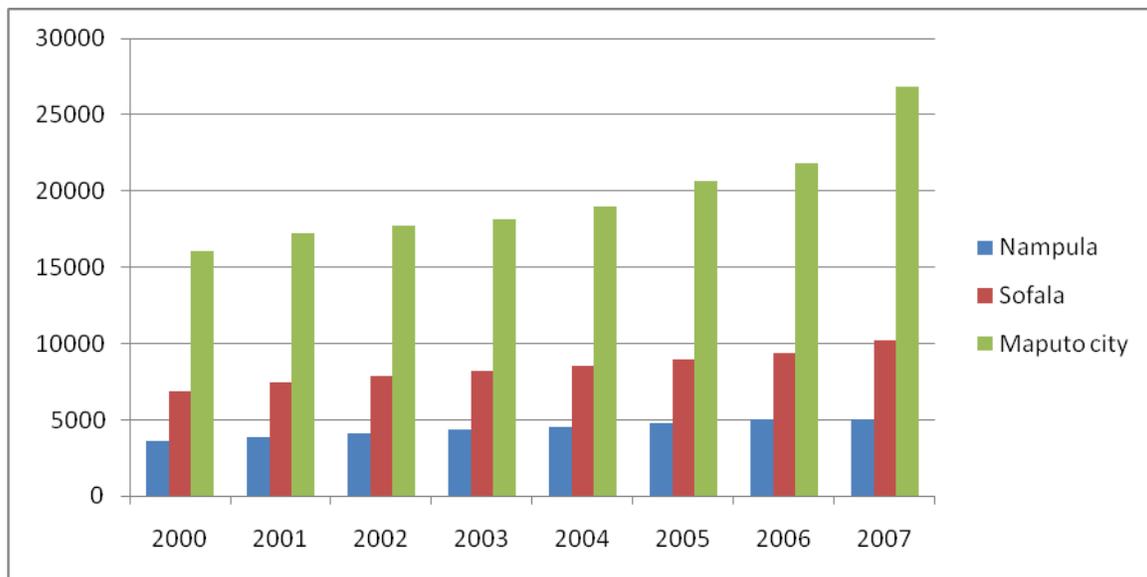
*Source: INE (2008)*

Thanks to its long cost and unexploited natural assets, the tourism sector is considered strategic for economic development. As it is reported on the government master plan for the sector, by the year 2020, the government expects to put in place measures to transform Mozambique into vibrant, dynamic and exotic destination in Africa, with the ability to mobilize and host over four million visitors per year. Though difficult as the country is still lagging behind peers in the region, the stated target does not seem unachievable. In fact since the end of civil war, the sector has improved markedly in line with the general trend of the rest of the economy. From 1995 to 2007 the total cost of tourism sector investment amounted to 1.8 billion US\$, almost 14% of the same period authorized projects. Just in 2006 alone close US\$ 200 million was invested and the physical hotel capacity is reported to have grown by more than 50% in the last 8 years.

## 6.2 Tourism Trends in Maputo, Sofala and Nampula

Maputo is the Capital city of Mozambique and it is the country's most developed area. The region per capita income has been growing from 16026 Metical in 2000 to 26799 Meticais in 2007. This is almost three times the country's per capita GDP and more than five times that of three provinces from the north (figure, 1).

**Figure1: Percapita Income distribution for Maputo, Sofala, Nampula**



Source: INE

The tourism industry value chain is relatively well developed in Maputo. It is comprised of a number of modern and relatively developed firms from travel agencies to five star hotels targeting foreign tourists, and small and medium scale firms, including restaurants and take- aways. The extreme feature of tourism sector operators is represented by family informal business selling diverse items from local craftwork to foodstuff along beaches.

The table 2 below summarize the sector situation in 2004 and 2005 for the Maputo city, the neighbouring province of Maputo , Maputo city , Sofala, and Nampula. In the period of reference, national and foreign visitors increased in both provinces as well as for the country. Though consistent estimates were not found at the time of drafting this report, this trend seems to have persisted in the following three years (2006 and 2007).

**Table 2: Origin of Visitors by Nationality**

	Visitors				total Nr of Visitors	
	National		foreigners			
	2004	2005	2004	2005	2004	2005
Total	157901	167495	164497	171558	322398	339053
Maputo P	6914	7194	8046	4193	14960	11387
Maputo c	55016	60215	99475	112882	154491	173097
Sofala	12982	12594	7167	7642	20149	19761
Nampula	8138	9741	2207	2793	10345	12534

Source: INE

It is important to note the expansion of domestic tourism in the last five years. The number of Mozambicans demanding tourism services has been expanding in Maputo, Sofala and Nampula. For Maputo city alone the number of Mozambicans demanding accommodation from the tourism industry increased from 110568 in 2004 to 228254 in 2005 (Table 3). This is a consequence of per capita income increases and seems to reflect the emergence and empowerment of Mozambique's middle class, following over ten years of sustained economic growth.

**Table 3: Number of Tourists demanding accommodation services**

	Nationals		Foreigners		Total	
	2004	2005	2004	2005	2004	2005
Maputo Province	8496	7728	21068	15431	29564	23159
Maputo City.	110568	118154	263328	240040	373897	358194
Sofala	25492	27591	14964	14556	40456	42147
Nampula	18016	21300	4240	4924	22256	26224
Mozambique	286702	316789	407806	389454	694508	706242

Source: INE

Following the described context, the sector future prospect is promising. The country and the three regions economic outlook is expected to keep its development trend. With strong support from donors and international agencies, the government will be able to sustain macroeconomic stability and economic growth. Several issues however still remain unsolved, including: (i) poor human capital base associated to high illiteracy rate; (ii) less friendly market conditions and legislation; (iii) poor performance of the justice system compromising the rule of law; (iv) low level of savings and investment against a

background of high cost of accessing credit, particularly for small and medium enterprises.

### 7. The State of the Small and Medium Scale Tourism firms in Mozambique

It is against the background described above that small and medium scale tourism firms compete for success. Table 4 and 5 below summarizes descriptive statistics of the 174 interviewed firms in Maputo, Sofala and Nampula.

Firm scale is defined in terms of the number of employees. Revenue/Labour ratio is the amount of reported revenue over labour force. It measures how much each unit of labour generated in the last six months before the interview. It is considered a measure of firm productivity. Getting to the appropriate numbers of revenue from the firm books was difficult because of reluctance from the firm owners/managers. Hence the reported numbers must be taken as proxy to the true values.

The small scale firms make about 60% of the surveyed firms, while less than 20% may be considered of medium scale (Table 4). This picture characterizes the underlying structure of economic activities in Mozambique. The most recent survey of firms in Mozambique classified 98% of firms as small and medium scale firms in Mozambique, using the number of worker as a reference point (INE, 2004).

**Table 4: Selected Firm Characteristics**

Firm Scale	Nr of Firms	%	Core Business	Average OperatCost/Labour	Average Revenue/Labor
1-5	52	29.89	Take Away	10409.86	13367.69
6-10	52	29.89	Restaurant&Bar	8226.905	9468.608
11-20	43	24.71	Restaurant&Bar	5475.274	6788.429
21-51	27	15.52	Restaurant&Bar	3069.827	3371.038
Total	174	100	Restaurant&Bar	7395.485	8992.125

*Source: Own estimates*

The main market focus of the surveyed firms is fast food (known as take away) and restaurant and bars (Table 4). Operating costs per labour force vary from minimum of

3069.82 to 10409.86 Meticaïs. Average revenue per labour force follows a similar trend with a minimum of 3371.038 Meticaïs to 13367.69 Meticaïs.

The scale of a firm appears to be negatively associated with the level of revenue/labour ratio (Table, 4). This seems to be in line with the results reported by Nancy, et al 2003 on a study about 50 small and medium rural agro-enterprises in Colombia. It implies that as one moves from micro firms to medium scale firms, labour productivity and efficiency reduces. Micro and small firms, mostly those specialized on take away; manage to mobilize high level of revenue/ labour force than large firm while enjoying low costs per unit of labour. Taking the example of Maputo as a reference, this may not be surprising since these firms are frequently found in places of high demand, schools, hospitals, government offices, and medium and large scale private firms.

Table 5 and 6 below correlates firm size with human capital variables (labour force education and years of experience with the firm).

**Table 5: Selected Firm Characteristics 1**

Firm Scale	Nr of Firms	%	Revenue/Labor F			Owner/Manager Ed		
			Max	Average	Min	Max	Average	Min
1-5	52	29.89	85000	13367.69	1100	Higher ed	ESG1	EP1
6-10	52	29.89	19167	9468.608	550	Higher ed	ESG1	No ed
11-20	43	24.71	10455	6788.429	500	Higher ed	ESG2	EP2
21-51	27	15.52	5476	3371.038	1466	Higher ed	ESG2	EP1
Total/Average	174	100	85000	8992.125	500	Higher ed	ESG1	No ed.

*Source: Own estimates*

*Note: ESG1 and ESG2 stands for lower and upper level secondary school education, EP1 and EP2, are lower and upper level primary education. No ed. Stands for absence of education.*

**Table 6: Labour Characteristics**

Firm size	Employees		level of Ed				Work exp.	
	Nr	Average	Max	Average	Min	Max	Average	Min
1-5	201	4	ESG2	ESG1	5	10	3	1
6-10	423	9	ESG2	EP2	0	10	4	1
11-20	582	14	ESG2	ESG1	5	10	4	1
21-51	977	37	ESG2	EP2	0	10	5	1
Total/average	2183	13	ESG2	EP2	0	10	4	1

*Source: Own estimates*

The level of education among employees is quite high by Mozambican standards where 50% of the total population is illiterate. The average level of education among the owners/managers is secondary school. Across the firm size there are owner/ managers with university education (higher ed.). Moving from micro firms to relatively large firms, one finds relatively more educated owners/managers among large firms. In fact the level of education of the owner/managers of relatively large firms is above the average for the sample surveyed.

Table 6 correlates the size of the firm with the number of employees, their average education and years of experience. All the firms surveyed together employ 2183 workers, meaning that on average there are close to 13 employees for each firm. Micro firms (between 1 and 10 individuals) together employ 424 individuals against 977 individuals for large firms. The maximum level of education among employees is upper secondary schools (ESG2) across all firm sizes. On average however upper primary school is dominant among workers.

Employment seems to be more permanent and safe when firms are large and less safe when they are small. The average years of experience with the firm among employees is 3 for those firms employing between one and five individuals. They increase to 4 years for those firms employing between six and 20 workers. For the largest firms is five. The reported difference between average years of work experience among micro and the largest firms is statistically significant at 1% level of significance. Apart from signalling some flexibility in terms of the rules that govern small firm's relationship with their employees, this finding may also be related to large firm's limitations on hiring due to the labour legislation rigidities in Mozambique. The level of compensation for dismissed

labour is still considered high and this was cited as one of the most important barriers for not laying off the labour force considered redundant among firms employing between 20 and 51 workers.

Peace and macroeconomic stability played a major role for the recovery of the tourism sector. Both the maximum (10) and the average years of experience (4) of the labour force point out the fact that the tourism sector in Mozambique is an emerging sector. It benefitted from the political stabilization that followed the first multiparty election in 1994, and growth and macroeconomic stability that followed this event. The concentration of years of work experience between one and ten demonstrate that the positive shift in tourism sector reported in the last subsection have had trickle down effects on micro, small and medium scale, with particular emphasis for the last five years.

## **8. The Determinants of firm Performance**

In the last section we described the firms surveyed in terms of their size, productivity, operating costs, labour force features and market focus. It appeared that among the sample surveyed, high performers tend to be those firms of small size. Here this paper abandons the averages and attempts and to track the profile of high performers. How can they be characterized? This is a preliminary step towards the regression analysis that will be conducted in the next section. Following the literature, the paper groups the firm in five quintiles of revenue per unit of labour.

### **8.1 Human Capital and Firm Performance**

Human capital is measured as the level of education of the owner/manager and their staff. For capturing the staff level of education this paper resorted to the average level of education for waiters. Table 7 and 8 below correlates the reported information with the level of productivity.

**Table 7: Percentage Distribution of Firms by quintile of Income, according to the owner/manager level of education**

Level of Ed. Of the owner/manager	Quintile 1	Quintile 2	Quintile 3	Quintile 4	Quintile 5	Total
0	0	0	0	0	4	1
Ep1	0	11	0	5	0	3
Ep2/ETE	15	0	5	33	4	12
<b>ESG1/ETB</b>	<b>25</b>	<b>39</b>	<b>37</b>	<b>24</b>	<b>54</b>	<b>36</b>
<b>ESG2/ETM</b>	<b>40</b>	<b>28</b>	<b>32</b>	<b>29</b>	<b>38</b>	<b>33</b>
Higher ed	20	22	26	10	0	15
Total	100	100	100	100	100	100

*Source: Own estimates*

*Note: EP1/ETE= primary education and vocational training, ESG1/ETB=Low secondary School and basic technical school, ESG2/ETM= Higher secondary school and mid level technical school, Higher ed. = Higher education*

**Table 8: Percentage Distribution of firms by quintile of revenue/labour, according to the waiter average level of education**

Waiters education	Quintil 1	Quintil 2	Quintil 3	Quintil 4	Quintil 5	Total
No education	0	0	0	0	5	1
EP1	6	22	5	6	14	11
<b>EP2/ETE</b>	<b>17</b>	<b>13</b>	<b>29</b>	<b>47</b>	<b>29</b>	<b>26</b>
<b>ESG1/ETB</b>	<b>50</b>	<b>35</b>	<b>38</b>	<b>35</b>	<b>43</b>	40
ESG2/ETM	28	30	29	12	10	22
Total	100	100	100	100	100	100

*Source: Own estimates*

Ninety two percent of firms on the highest quintile (quintile 5) of labour productivity have owner or a manager with a low or an upper secondary school certificate. An upper secondary school certificate or a mid level technical education, particularly, plays a major role on improving the ability of owner/manager to lead their firm competitively. The percentage of firms with a owner/manager holding no education or primary education is generally low. But it is important to note that in the highest quintile (4 and 5) they are almost absent. In fact, there are 5% firms managed by lower primary school holders in quintile 4 and 4% in quintile 5.

It is important to note that possessing higher education does not necessarily reflect increased management capabilities and income. A possible reason for this is the fact that in many cases owner/managers with higher education tend to work for their firms on part time basis as they are also employees of a private firm or are public servants.

Among firms staff, the level of education is generally low, which poses an additional constrain for the sector performance. The dominant education level across the five quintiles is upper primary school and this correlates positively with labour productivity up to certain threshold when the reference is the waiter's average level of education.

## **8.2 Social Capital**

Social capital was defined as the presence of trusted relationship that a given firm maintains with suppliers, clients and labour. Specific questions were included in the questionnaire that helped in producing categorical variables for each of the three types of relationships. For suppliers, a relationship was assumed to be of trust if the owner/manager at the date of interview reported to buy the main inputs from known suppliers and considered her firm relationship with the mentioned suppliers excellent or good. The same approach was used for clients.

To capture the level of within firm trust as represented by the degree of trust between top managers and workers, the owners were asked to respond to two questions: First whether they believed that their workers could work independently and without major supervision. The last question was about the criteria used for hiring new employees. It is assumed that owner/managers that reported to considerer their workers able to work independently and without major supervision were more likely to trust them than those who responded no. Besides that, resorting to known individuals for selecting and hiring labour was assumed to represent the presence of a trusted relationship.

The figures in the table below are average percentages of firms reporting to resort to inner cycle of friends and relatives for accessing inputs, selling their output and recruiting workers as well as reporting to hold some degree of trust for their workers. A number of lessons can be derived from their trend. First, firms in the tourism sector frequently trade with friends and relatives. On average less than 20% of firms search for inputs using a

network of social relations. The impact of exploiting the supplier’s network of social relations is not fundamental for firm productivity. It appears to be of negative effects because when revenue/labour ratio grows, the percentage of firms making use of a social network of suppliers declines.

These, do not happen when looking at the issue from clients and labour relationship perspectives. The proportion of firms reporting to have their main clients and employees among relatives and friends as well as those reporting to trust their workers, grows with the revenue/labour ratio.

According to the table below, building trust with main stakeholders’ yields positive effects when sourcing costumers and labour. At best it is of marginal or negative impact when it is associated with sourcing inputs.

**Table 9: Percentage of firms that reported trusted relationship**

Indicators	Quintile 1	Quintile 2	Quintile 3	Quintile 4	Quintile 5
Relationship with suppliers.	20	20	2	11	5
Relationship with clients.	74	85	87	79	94
Relationship with labour.	46	66	57	50	70

The implication of the reported results is two twofold. In one case the figures reported reveal a scenario of firm’s attempting to respond to high transaction costs and the government failure to build competitive markets, impose the rule of law and protect private property, by stratifying their business around network of social relations. While for the case of clients and labour this approach yields positive externalities, firms adopting similar approach for sourcing inputs fail to gain in terms of productivity.

### **8.3 Management Practices and Firm Performance**

As it was described on the methodology section, management practices is defined as a set of variables found within a certain firm including: (i) the presence of labour representatives on the shop floor implying strategic openness for dialogue; (ii) The presence of standardized and written procedures to guide workers’ operations; (iii) knowledge of the operation procedures by the labour force; (iv) presence of planning; (v)

frequency of scheduled meetings; (vi) number of firms reporting to invest on training; and (vii) number of firms reporting to invest on building social capital. While some of these indicators (such as the presence of labour representatives on the shop floor, institutionalized planning processes) may not be of major impact among firms with a minimum number of employees, there are relevant when the size of the firms increases.

Table 10, below, group the firms by size in the first column. The figures reported stand for number of firms that reported yes or no to questions related to the first three indicators. In line with the findings of the sub-section 5.3, the first three indicators of management practices are absent in almost all categories of firms. While that may not represent a major handicap for micro firms, it is certainly a problem when the numbers of employees increases. When the number of employee's increases communication becomes a serious problem, peer pressure looses ground as an instrument for eliciting increased effort to achieve firm targets. It is also within similar context that the openness of dialogue spaces and standardization of operational procedures turns to be crucial for success.

The reduced percentage of firms reporting not to have a presence of labour representatives on the shop floor coupled with the fact that a similar percentage did not report to have institutionalized regular meetings with the labour force, reflect a culture of a command firm, where the decision making process is top-down and the labour force is conceived as a passive factor of production that should be ready to receive and understand the orders from top-managers.

In the context of large firms, the costs of opting for top-down approach of management, when procedures are not standardized or, if they are standardized, the labour force is reported not to know them, increases the implicit costs of running business and reduces productivity. It is not surprising, therefore, that poor performers are among large firms and high performers are found within small firms. The latter are less exposed to the challenge of running firms with a significant number of workers. It is also among them that the costs of monitoring and enforcing labour productivity and information is

relatively reduced, making it easy for them to run their business with increased productivity.

**Table 10: Firm size and selected organizational culture indicatorsn**

Firm size	Presence of labour representatives at shop floor		Presence of Standardized and written Procedures		Presence of Knowledge of standardized Procedures by the labour force		
	Nr of firms interviewed	Yes	Nr of firms interviewed	Nr of firms with Absence	Nr of firms interviewed	Yes	No
1-5	43	1	51	44	52	7	45
6-10	39	14	51	31	52	21	31
11-20	37	16	42	27	43	14	29
21-51	26	19	26	9	27	18	9
Total	145	50	170	111	174	60	114

*Source: Own estimates*

Table 11 presents the number of firms for each quintile of income that reported the presence of a selected set of organizational culture indicators. Two lessons emerge from the table. Within the first three quintiles, the percentage of firms adopting management best practices is less than 50%. High performance is less associated with the number of firms that perform better in terms of management practices indicators. This reinforces the argument that while management practices indicators as they are conceived here may sound important for large organization, performance at micro and small scale level may be related to other variables, possibly social capital and location specific variables, such as market conditions. In the next two sections of the paper address these two issues.

**Table11: Firm distribution by quintile of revenue/labour and selected Management Practices indicators**

Revenue categories	Percentage of firms that reported to have a plan of activities	Percentage of firms that reported to have quality written control mechanism	Percentage of firms that reported the Presence of institutionalized channels of communication	Percentage of firms that reported to Invest on Training	Percentage of firms that reported to Invest on Social relations
1st quintile	50	43	46	51	44
2nd quintile	33	45	62	36	29
3rd quintile	38	30	50	24	31
4th quintile	38	35	40	26	41
5th quintile	26	21	42	2	44

*Source: own estimates*

#### **8.4 Regression Analysis**

So far, this paper has discussed possible association between several indicators of human, social, and management practices indicators and firm performance among the sample of firms surveyed. It stressed that micro and small firms tend to be more productive than large firms, a finding consistent with some literature in the area (Nancy et al, 2003). It also found that human, social as well as management practices indicators matter for firm performance since they correlate with the degree of productivity in the tourism sector.

Now, to close the discussions, the paper intends to quantify the impact of indicators associated with these variables on productivity, using regression analysis. The dependent variable was labour productivity which was assumed to be *proxied* by the log of revenue/labour ratio. The set of independent variables included: operating cost per labour costs; human capital; social capital variables and management practices indicators. Operating costs and number of labour entered the regression mostly as control variables. Below we present a summary of descriptive statistics of the variables included in the model. The standard error of most of the variables used is close to normality.

**Table 12: Variables Descriptive Statistics**

Variables	Average	Standard error	Maximum	Minimum	Nr of Observat
Log of revenue per labour force	8.775956	0.845339	11.35041	6.214608	168
Relationship with suppliers	4	0.492722	5	3	174
Constraints on accessing inputs	3.590551	0.928853	5	1	127
Relationship with customers	0.4137931	1.097045	4	0	174
Knowledge of firm objectives	0.8579882	0.3501	1	0	169
Degree of trust on labour	0.6069364	0.489849	1	0	173
Presence of Planning	0.3684211	0.483793	1	0	171
Age	3.570423	2.980785	10	1	142
Owner/Manager Education	3.421569	1.038242	5	0	102
Number of waiters	2.58046	2.877432	13	0	174
Number of other workers	2.298851	4.647368	32	0	174
Region	1.942529	0.795309	3	1	174
Log of operating cost/labour	10.79917	0.852454	11.65269	8.517193	166

Source: Own estimates

The estimation started with a basic model that encompassed proxies for human and physical capital (operating costs), social capital variables and management practices indicators. The second model dropped the proxy for physical capital and the number of employees. The final model dropped the proxy to physical capital.

The performance of social capital and management practices indicators is poor. In some cases, their proxies came up with associated coefficients of either a wrong sign or insignificant value. Despite that, the model estimated is robust and it can be interpreted as giving tentative information about what is happening in the sector. The estimated results are in line with our previous discussions but also raise some additional issues.

Physical capital as *proxied* by the operating cost/labour ratio is significant and it is in line with theoretical prediction, holding an elasticity of 0.6. It suggests that a 1% increase on costs per unit of labour, leads to an expansion of labour productivity by 0.6%.

The impact of human capital as measured by the number of workers and owner/manager education is insignificant. The coefficient for the owner/manager education also came out with the wrong sign.

Social capital as captured by the degree of trust between the owner/manager and the workers plays a positive effect on productivity. The coefficient associated with a categorical variable measuring the degree to which top managers reported to believe that their workers were able to work independently without major supervision is positive and significant at least at 5% level of significance (Table 14).

Another issue that comes out from the regression results is the negative role played by several constraints associated with the prevailing conditions in the input market. Local firms suffer because of high input prices, scarcity of quality goods and service. At the level of significance of 1 and 5%, the coefficient associated to these variables are negative, implying that together these factors depresses labour productivity since they reduce the chances for responding with speed and the necessary quality to customers. It also depresses labour productivity through additional time spent on searching and screening the market for better goods and services. Developing a good network of social relation with suppliers in such an environment has minimum chance for success. At the extreme it can even lead to business failure as the regression results apparently point out. In similar market context what counts is the manager's expertise in procurement and the willingness to keep a more diversified network of supplies including searching on foreign markets.

The coefficient for networking with customers has a positive and sign, implying that there may be gains in developing good relations with clients. This finding however should be taken with care because the coefficients are insignificant (See appendix).

Dropping the labour force level of operating costs/labour force leads to additional insights about the role of regional demands. The coefficient for the categorical variable for Sofala is negative and significant, implying that there is loses in running business there while the positive coefficient for Maputo and Nampula, implies comparative gains for firms running their business either in Nampula and Maputo. Maputo is the most

developed region in Mozambique, while Nampula has been going through rapid economic growth. Because of these high incomes, the demand for tourism services is high, leading to trickle down effects for the two regions small and medium scale tourism firms.

## **9. Conclusions and Recommendations**

This paper discussed the determinants of firm level performance using a sample of 174 small and medium scale tourism firms. Small and medium scale tourism firms in Mozambique face a number of challenges but they also have potential for maximizing gains and improving social welfare. In the current conditions this is however not for all. Micro, small firms appear to be more productive than large firms for our sample.

The reasons for poor performance are found both externally and within the firm. The market for inputs for tourism operators remains harsh for doing business. Prices are considered high. There is scarcity of quality goods and services. The impact of this variable on productivity is negative and statistically significant, meaning that input market supply constraints are detrimental to the tourism sector development.

The level of development of a region matters for increased productivity of small and medium scale firms. Categorical variable for Sofala whose growth has been in line with country trend had a negative and significant coefficient. These findings lead to the conclusion that firms in Maputo and Nampula perform better because they benefit from positive externalities associated with being in the most developed and fastest growing regions in the country (Table, 15).

Within the sector and firms, part of the reasons for the reported performance differences is found in the nature of the problems micro and relatively large firms face. Small firms face minimum demand in terms of labour productivity monitoring than large firms, hence they manage to maximize gains than their counterpart. In typical Mozambican context, this is reinforced by the dismal performance of more large firms with respect to adopting modern practices of managing human resources. Management remains top down and concentrated around the owner/manager. There is lack of appropriate channels for team-

building and nurturing a spirit of a common agenda among managers and their employees.

Local firms do invest in social capital but it seems to play both a negative and positive role. It does not help firms in maximizing gains from networking with friends and relatives from the supply side. But it plays an important and positive role when dealing with customers and workers.

There are several recommendations that can be made from our discussion. This paper raises at best a few of them. First, the introduction of measures to increase competition in the input market may help in reducing prices, increasing the availability of goods and indirectly improving the working conditions of local firms. Second, from government perspective it pays off to invest in creation of management skills as well as tourism sector related skills. Both skills have potential to change the current state of the relatively large firms, which is now disappointing.

More reforms are required from the managers themselves and the government. Managers should invest in social capital particularly with clients and workers as the pay off for social capital is positive. In the meantime the government needs to further remove the constraints that lead to increased high transaction costs in the labor market, and encourage firms to adopt pervasive (though with private gains) strategies for social welfare maximization.

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**Appendix:**

**Table 13: Regression Analysis (Base and Preferred-Model)**

<b>Variables</b>	<b>Coefficient</b>	<b>T-Statistic</b>
Relationship with suppliers (good)_base (reasonable)	-0.5854264	(0.397469)
Relationship with suppliers (Excelent)	-1.060214	(0.35488)*
Constraint in input market (Lack of procurement experts.)_base (low quality of prod.)	-1.371325	(0.498767)**
Constraint in input market (high prices)	-1.618097	(0.307453)*
Constraint in input market (scarcity of inputs in the market)	-1.346222	(0.442859)*
Constraint in input market (other)	-1.659495	(0.270792)*
Relationship with customers' (acceptable)_base(base)	-0.344102	(0.242584)
Relationship with customers (good)	0.6969851	(0.468866)
Relationship with customers (excelent)	0.0128705	(0.253668)
Knowledge of the objectives and mission of the firm	-0.6198569	(0.447355)
Degree of trust on labour	0.9071444	(0.328092)**
Presence of Planning	-0.0975152	(0.178012)
Age	-0.0089836	(0.026295)
Owner/manager education (EP1)_base(absence)	0.4142746	(0.351597)
Owner/manager education (EP2/ETE)	(dropped)	
Owner/manager education (ESG1/ETB)	-0.2296732	(0.291401)
Owner/manager education (ESG2/ETM)	-0.1839491	(0.296034)
Owner manager education(University degree)	(dropped)	
Firm location(Sofala central region)_base(Maputo)	-0.2478791	(0.348985)
Firm location (Nampula)	-0.6653849	(0.396331)
Number of waiters	-0.1572512	(0.027937)*
Number of other employees	0.0192276	(0.033214)
Log of operating costs per labour	0.6653769	(0.099529)*
Constant	4.960675	(1.585042)*

Value for T-statistics in Bracket

\*\*\*significant at 10%

\*\* significant at 5%

\*significant at 1%

Number of observation =49

R-squared=0.8179

**Table 14: Regression Results (Without the amount of labour and the Log of operating costs)**

<b>Variables</b>	<b>Coefficient</b>	<b>T-Statistics</b>
Relationship with suppliers (good)_base(reasonable)	-0.71838	(0.546561)
Relationship with suppliers (Excelent)	-1.15472	(0.590836)**
Constraint in input market (Lack of procurement experts.)_base (low quality of prod.)	-0.7362	(0.683539)
Constraint in input market (high prices)	-2.1886	(0.381803)*
Constraint in input market (scarcity of inputs in the market)	-1.66383	(0.650284)**
Constraint in input market(other)	-1.77793	(0.372006)*
Relationship with customers' (acceptable)_base(base)	-0.52822	(0.478098)
Relationship with customers (good)	0.977953	(0.578376)
Relationship with customers (excelent)	0.005552	(0.583269)
Knowledge of the objectives and mission of the firm	-0.54093	(0.541652)
Degree of trust on labour	0.986989	(0.34231)*
Presence of Planning	-0.35883	(0.257525)
Age	-0.0364	(0.038504)
Owner/manager education (EP1)_base(absence)	(dropped)	
Owner/manager education (EP2/ETE)	-0.00958	(0.468812)
Owner/manager education (ESG1/ETB)	-0.65139	(0.472296)
Owner/manager education (ESG2/ETM)	-0.50885	(0.465417)
Owner manager education(University degree)	(dropped)	
Firm location(Sofala central region)_base(Maputo)	0.012693	(0.50618)
Firm location (Nampula)	-0.55636	(0.525566)
Constant	12.92218	(1.129124)*

Values for T in brackets

\*\*\*significant at 10%

\*\* significant at 5%

\*significant at 1%

Nr of observations =49

R-squared=0.4908

**Table 15: Regression Analysis (Without the log of operating costs)**

<b>Descrição das Variáveis</b>	<b>Coefficiente</b>	<b>Estatística do t</b>
Relationship with suppliers (good)_base(reasonable)	-0.84157	(0.324441)**
Relationship with suppliers (Excelent)	-1.3087	(0.426189)
Constraint in input market (Lack of procurement experts.)_base (low quality of prod.)	-1.63444	(0.30775)*
Constraint in input market (high prices)	-2.27789	(0.295879)*
Constraint in input market (scarcity of inputs in the market)	-2.0914	(0.353908)*
Constraint in input market(other)	-1.99417	(0.296134)*
Relationship with customers' (acceptable)_base(base)	-0.6836	(0.43299)
Relationship with customers (good)	1.442951	(0.384226)*
Relationship with customers (excelent)	0.535807	(0.311649)***
Knowledge of the objectives and mission of the firm	-0.25165	(0.214485)
Degree of trust on labour	-1.38718	(0.360649)*
Presence of Planning	1.033486	(0.225277)*
Age	0.055699	(0.026743)**
Owner/manager education (EP1)_base(absence)	(dropped)	
Owner/manager education (EP2/ETE)	-0.41549	(0.485357)
Owner/manager education (ESG1/ETB)	-1.08165	(0.46912)**
Owner/manager education (ESG2/ETM)	-0.8758	(0.412779)**
Owner manager education(University degree)	-1.55007	(0.543796)*
Firm location(Sofala central region)_base(Maputo)	-0.15678	(0.025965)*
Firm location (Nampula)	0.028488	(0.024346)
Number of waiters	15.12965	(1.147132)*

Number of other employees

Nr of observation =52

Log of operating costs per labour

R-squared=0.6522

Constant

\*significant at 1%