

## Teaching Business Climate Development with the Help of Case Studies

PÉTER FUTÓ

**Abstract** This article presents a practical conceptual framework of Business Climate Development as an area of development policy, and introduces the terms used for evaluating Business Climate Development projects and programs. The structure of such programs and the method of their evaluation is demonstrated with the help of an illustrative case study in which a Business Climate Development program is evaluated in a post-soviet republic. The evaluated program was financed by an international development organization and lasted for five years. It supported central and local authorities to register businesses, issue various businesses permits, dispatch inspectors to oversee various business activities and manage taxation. The program was evaluated by a team of consultants who identified, classified, assessed and judged the activities of the above-mentioned Business Climate Development program. The program and its evaluation has been presented as a case study to students of a Joint Master Course for Comparative Local Development.

**Keywords:** • business climate • case studies • evaluations • policy measures

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CORRESPONDENCE ADDRESS: Péter Futó, Ph.D., Professor, Corvinus University of Budapest, Institute of Sociology and Social Policy, Közraktár utca 4-6, H-1093 Budapest, Hungary, email: peter.futo@uni-corvinus.hu.

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## 1 The business climate and its evaluation: a conceptual framework

The business climate is the general legal, institutional, economic and social environment of entrepreneurship and enterprises in a particular locality, region or country, comprising of the attitudes of the central, regional and local governments, of financial institutions, labour organizations and non-governmental organizations towards businesses and business activity. A business-friendly environment is demonstrated by the ease of doing business as influenced ...

- By the institutional and regulatory framework of fair competition, employment, trade and taxation;
- By favourable macro-economic constraints such as inflation and economic growth;
- By the wide availability of support offered to businesses by authorities;
- And by the positive attitude of society towards businesses.

Why are business climates more favourable in some countries than others? According to the theory of institutional economics, between-country differences in business climates as a rule are explained predominantly by legal and institutional factors. In particular, the presence of an informal economy is explained predominantly by unfavourable business conditions (Dabla-Norris *et al.* 2005). Within one country the business climates of various regions and settlements may also show significant differences (OECD 2001; Shane 2005). Local variations in business climates are as a rule explained by a wide range of theories that take into consideration differences in inherited economic structure, social capital, social stratification, tradition, and also by centrum-periphery relationships (European Commission 2010). Business climate development is one of the major tasks for local economic development (The Cities Alliance 2007; Swinburn *et al.* 2006).

The business climate has frequently been a subject of comparative research. The business climates of various countries are comparable, and are indeed compared with the help of numerous qualitative studies and various quantitative indicators. One of the most influential quantitative indicators is the "Ease of Doing Business" indicator, which has been determined for a wide range of countries (The World Bank 2008). The components and influencing factors of a business climate have been tackled not only with the help of numerical indicators, but also by qualitatively investigating the impact mechanisms of relevant development programs, supporting projects, and business development regulations in order to evaluate their success or failure.

*Case studies* are qualitative instruments of research which possess high didactic value in development education. Case studies are not only suitable for descriptive purposes but may be used to highlight a preferred contextual framework and, with the use of theories, can be used to explain observed and presented phenomena (Yin 2003). However, research is not the sole area in which case studies may be instrumental: likewise, case studies are excellent ingredients of evidence in consultancy and teaching. Most case studies of business climate development are of the stand-alone type because of the national or local

limits of interest, or due to difficulties with data collection. Consequently, it is not easy to find comparative case studies, in spite of the fact that comparative case studies are much more suitable for supporting or rejecting certain general hypotheses about the causal mechanisms of policy interventions.

*Evaluations* involve consultancy efforts to assign value to certain policy measures; i.e., to assess whether certain projects, programs, or policies were (or are) successful. Specific measures of business climate development are evaluated according to their contribution to local economic development (OECD 2009). In particular, case studies of project evaluations are frequently used in teaching about local development to demonstrate how a selected policy area – in this case, business climate development policy – functions in a particular country. Additionally, students of local development, when writing their dissertations, frequently choose project and program evaluation as the preferred genre.

## 2 The case-study program

*The evaluation project.*<sup>1</sup> The following case study relies on experiences from a real-life consultancy effort. The consultants prepared an interim<sup>2</sup> evaluation of a business climate development program in a post-soviet republic in 2014. The evaluation took place when the program under evaluation had already lasted for seven years, and was still ongoing. The evaluation project lasted for two months. The team of evaluators consisted of four consultants (three international consultants and one local) and was delegated by an independent private consultancy.

*The evaluated program.* The beneficiary of the program under evaluation was the government of the case-study country. The program was financed by a developed country in the framework of a bilateral development agreement, and implemented by an international development organization. The first wave of the program ran from September 2007 to June 2013 with a budget of nearly five million USD. At the end of the first wave of the program (in 2013) the donor country decided to extend it by another one-and-a-half years and contributed to the budget an additional more than one million USD.

*Policy areas.* The evaluated program promoted business climate development reforms in the case-study country in the following policy areas:

1. The initial registration of businesses;
2. The issuing of permits to businesses;
3. The implementation of business inspections by government authorities;
4. The simplification of taxation; and
5. The modernization of agricultural governance.

*Aid delivery mechanisms.* According to the conceptual framework of the evaluation, the activities of the evaluated project were implemented with the help of four so-called “Aid Delivery Mechanisms,” including:

- “Monitoring and Research” (e.g. implementing business surveys and analysing them using statistical methods, providing quantitative and qualitative studies about small business development).
- “Promotion of legal changes” (e.g. lobbying government agencies for business-friendly regulations and supporting such measures with know-how and study trips).
- “Capacity building” (e.g. providing technical assistance to government agencies, creating web portals, drafting regulations and providing services that facilitated the membership of the beneficiary country in various international bodies).
- “Awareness Raising” (e.g. workshops and training courses for NGOs and for associations of entrepreneurs).

The evaluation covered the program's activities in the above five “policy areas,” as detailed in the above four “aid delivery mechanisms”.

The evaluators used the following traditional qualitative evaluation criteria:

- Relevance (coherence with stakeholder needs and government policies);
- Effectiveness (delivery of planned results);
- Impacts (direct and indirect effects of program activities on the targeted policy areas and on beneficiary institutions); and
- Sustainability (the capability of program outcomes to survive for several years).

A traditional fifth criterion, efficiency (program delivery model, value-for-money, timeliness, etc.), was dropped due to the lack of time for gathering and validating financial data.

The evaluators were requested to assign quantitative indicators, or so-called Evaluation Rankings, to each of the four “aid delivery mechanisms” and to each of the five “policy areas”. Evaluation Rankings ranged theoretically from "Highly Unsatisfactory" (numerical value = 1), "Unsatisfactory" (2), “Fair” (3), and "Satisfactory" (4) to "Highly Satisfactory" (numerical value = 5). For the purposes of the present article, the actual ratings are not relevant, but their justification may be enlightening, because:

- They demonstrate the various important factors and components of a business climate;
- They indicate by what “aid delivery methods” these components are addressed by the measures of specific “policy areas;”
- They suggest what instruments can be used for developing the business climate of a particular country.

*The main information sources* of the evaluation were:

- Desk research; i.e., analysis of internal program documents, of the online- and paper-based deliverables of the program, and of documents provided by the beneficiaries;
- Interviews undertaken with the expert staff of the evaluated program; and
- A number of personal interviews with government officials, international donors, national experts, private sector representatives, businesses, social and labour organizations in the case-study country.

### **3 Comparative overview of the business environment in the case-study country**

The case-study country is rich in natural resources, but according to national plans its economy must be diversified by developing entrepreneurship in the service, manufacturing, trade and agricultural sectors as well. In the few years preceding the evaluation, the case-study country had made moderate progresses in improving its business climate. However, compared to some neighbouring countries the country had lagged behind in various business areas. The comparison was made feasible with the help of the yearly “Ease of Doing Business” indicators and related sub-indicators.

During the years preceding the evaluation, several independent experts had assessed the business environment of the case-study country, and the reports were available online. The general opinion of these independent experts was that the country was not fulfilling its own potential in terms of entrepreneurship development, the readiness of firms to grow, and their innovative activity. Business surveys implemented by the evaluated program and also by other projects showed that business-people in the country perceived serious obstacles to doing business, such as the lack of financial resources, regulatory deficiencies, and their interactions with courts.

An analysis of the recent “Doing Business” indicators compiled by the World Bank (2014) enabled the evaluators to compare the business climate of the case-study country with that of its neighbouring countries. During the preceding years, the case-study country had implemented some decisive reforms in a few areas: for example, business registration had been simplified. However, the same Doing Business rankings showed that the complex regulatory areas where the intervention and co-operation of numerous ministries and subordinated authorities were needed still required new approaches and reforms.

The relevant professional literature recommended implementing reforms in a wide range of policy areas, such as:

- Competition policy;
- Taxation;
- Anti-corruption policy;

- SME financing;
- Governance of permits, with special respect to the simplification of construction permits;
- Governance of inspections;
- Property registration;
- Foreign trade; and
- Resolving insolvency.

#### **4 Activities of the evaluated program by policy area**

The activities of the evaluated program can be sub-divided into distinct groups of deliverables according to the policy areas that were relevant for business climate development. The ease of doing business in a particular country depends on a multitude of factors. The following description illustrates the multi-dimensional and multi-disciplinary components of a business climate and the wide variety of policy measures available for its development.

*Business Registration.* Previous business surveys that assessed the needs of entrepreneurs revealed that in the case-study country prior to 2007 the administrative burdens and insecurities associated with business registration constituted a serious obstacle to small business development. By 2007, the government had decided to modernize the registration of new enterprises. At that time registration took one or two months and involved the completion of thirty administrative procedures, including obligations towards the register of companies, statistical authorities, and various sectoral inspectorates (labour, fire prevention, food safety, etc.). The evaluated program supported the respective efforts of the government using a wide range of deliverables to simplify business registration. Program experts did research on comparable business registration systems worldwide and submitted discussion papers about best applicable practices for business registration. Moreover, the program also organized study tours for officials to countries with well-functioning business registration systems. Subsequently, reform of this policy area followed and the government set up a countrywide network of “One Stop Shop” offices and an e-government system for business registration.

*Permits and Licenses* issued for businesses by local and central government agencies are very important ingredients of the business environment. The needs assessment survey of 2007–2008 had shown that there were some 230 types of administrative procedures associated with the permits and licenses in force. Such a complexity of obligations constituted a serious obstacle to entrepreneurship development in the case-study country. Research indicated that this thick interface between business and government was infected by corruption and favouritism and was causing administrative burdens and insecurity to businesses.

In order to achieve the aims of the program, the capacity building of the respective stakeholder organizations had to be supported by lobbying efforts. During the first years of the program, its experts had co-operated with the respective sectoral line ministries to reform the field of permitting and supported them with know-how, dissemination events (e.g. workshops), and subsidized study tours of government officials. However, the reform of permits did not progress as quickly as expected. Therefore, at a later stage, the program changed its target group within the government and identified a different network of government agencies that was closer to high-level political decision makers. As a result, the business-friendly messages of the program were more likely to receive attention. However, one of the compromises that the experts of the program had to make was that the range of permit areas to be reformed had to be limited, and could not include the crucially important area of construction permits.

Nevertheless, program activities in the area of permits and licenses resulted in ...

- Some legal reforms;
- The launch of an e-permits webpage;
- The organization of awareness-raising conferences; and
- The dissemination of several brochures about permits.

*Business Inspections reform.* Previous research into small business development in the case-study country had repeatedly shown that inspections implemented by labour-, fire prevention-, veterinary- and other government agencies constituted obstacles to entrepreneurship development in the country. The evaluated program successfully lobbied high-level policy makers and various sectoral government agencies to improve the legal framework of inspections. Various aid delivery instruments were implemented, such as inviting specialized consultants to hold training courses, research, publications, study tours, the provision of legal and IT advice, and website development.

Importantly, the above efforts culminated in the critical support given to the drafting of the Inspection Law of July 2013. This law has considerably reduced and limited the arbitrariness of inspections. In particular, the scope of business functions that inspectors were entitled to control was limited, the fines issued by inspectors were more thoroughly regulated, and the timing of inspections was also reformed by limiting the occurrences of unannounced, unexpected inspections. Moreover, the law resulted in the establishment of an e-government website (an “E-registry of inspections”) which has made inspection visits more transparent, predictable, and provided accountability and supervisory mechanisms for the respective government bodies. In particular, the program has engaged with the Labour Inspectorate Service, the State Fire Safety Inspectorate, and the State Veterinary Service, and has helped to introduce international best practices for inspections. Moreover, the evaluated program has compiled checklists for inspectors and drafted guidelines for risk-based inspection.

*Taxation* is a crucially important policy area for business climate development. The administrative burdens associated with taxation as well as the level of tax burden are major components of the business environment. The program offered technical assistance to the government in the relatively narrow policy area of transfer pricing. Transfer pricing refers to rules and methods for pricing cross-border transactions between various national subsidiaries of international enterprises. Countries with transfer pricing legislation generally follow the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations. These rules allow tax authorities to fight money laundering and tax evasion by adjusting prices of products, services, and tangible and intangible property in the case of cross-border transactions within the same multinational firm. With the help of the technical experts assigned by the program, the government of the case-study country obtained the necessary know-how about exchanging tax policy information according to internationally agreed methodology.

*Agriculture* is the biggest sector of the economy of the case-study country, besides the extraction of raw materials by the mining sector. Therefore, improving the business environment of farmers was very relevant for meeting the objectives of the program. The program offered two components in this policy area: (a) seed certification, and (b) value chain analysis.

- The modernization of seed certification was implemented through various technical assistance activities that contributed to the simplification of the associated administrative procedures and accelerated the application of best international practices. Although seed certification is a relatively narrow area within agricultural policy, its reform has impacts on food safety, environmental management, and on the subsidization of agricultural entrepreneurs, among other areas.
- The other deliverable of the program in relation to agricultural policies was the elaboration of value chain analysis models. Value chain analysis is a method which helps to identify market failures in subcontracting-supplier relations, and identifies promising areas of investment, thereby improving the competitiveness of selected products. The program established such models for the horticultural sector, thereby enhancing the export potential for the fresh fruit and vegetable products of the case-study country.

## 5 Aid delivery mechanisms applied by the evaluated program

*Monitoring and research of the SME sector.* The advisory activities of the program were based on a series of surveys that assessed the needs of local businesses. The surveys were based on the professional compilation of policy-area-specific questionnaires and on good and feasible sampling strategies. In particular, a 2012 survey of the awareness of businesses about the e-registry of inspections served for both the purpose of needs assessment and impact assessment. Additionally, experts from the program prepared legal analyses and policy assessments and published studies.



*Promotion of legal changes.* The evaluated program intervened with regulatory agencies for the purpose of reforming certain rules that were perceived as disadvantageous to the business sector. For each selected policy area, the program engaged with one (or more) governmental counterpart institution to obtain commitment for the intended reform. The relevant advocacy activity was supported by legal drafting, by offering technical expertise to government agencies, and by organizing thematic public-private consultations. The success of such lobbying activities depended to a large extent on the co-operation of the counterpart beneficiary organizations. Some government agencies – e.g. inspectorates in certain sectors – were more open to applying business-friendly international best practices, while others eagerly guarded every bit of their administrative and controlling power. The project was coordinated with the activities of some donor organizations that were active in the case-study country. These organizations co-operated with each other in promoting various legal changes on behalf of small- and medium-sized businesses.

*Capacity building for institutional development.* The evaluated program assisted a wide range of counterpart government agencies in applying international best practices, by setting up e-government websites, by setting up awareness-raising websites, by publishing and disseminating various brochures about the legal and institutional changes promoted by the program, by funding and organizing study tours for staff of government agencies and other stakeholders, and by organizing consultations with business associations.

*Awareness-raising.* The evaluated program organized a wide range of workshops and training courses for the staff of the relevant government agencies, for associations of entrepreneurs, NGOs and other organizations.

## **6 Conclusions and recommendations of the evaluation**

The overall judgement of the program was positive, especially when considering the fact that the results of the program had been achieved in a difficult administrative context. In this particular setting, the term “difficult” means that some government agencies were not interested in or were even opposed to reforms. In spite of this, the program delivered satisfactory results overall, which not only benefited the business sector of the case-study country, but also involved the building of trust and goodwill at the highest level of government.

The evaluators recommended improving the business environment of the case-study country by engineering reforms that produce higher quality regulations and well-trained, committed regulators. It was also recommended to continue the activities of the program by extending its advisory-advocacy functions. In particular, it was recommended that the project offer professional help to the government in the policy area of improving regulation. This involves efforts to establish administrative processes for systematically reviewing and updating regulations, and, if necessary, phasing out obsolete regulations

by taking into consideration evidence about their impacts on businesses. An important tool for taking such a systematic approach to better regulation would be advocating for the introduction and application of regulatory impact assessment within public administration.

## 7 Didactic conclusions

Evaluations can be readily used for educational purposes. Case studies of development consultancy activities such as project and program evaluations may serve as useful illustrations of development policy measures. Stand-alone (single-country) case studies of business climates may serve as useful evidence for demonstrating the structure of business climates in a particular country, region or settlement. Such case studies may highlight the constituent factors of the business environment and identify the policy measures for improving and eventually reforming the business climate. Comparative case studies are more suitable for generalization and for delivering lessons that can be learned and used in other territorial units. If the investigation covers two or more comparative territorial units, than it is possible not only to reveal ...

- How certain policy interventions work; but also
- Why under certain circumstances the investigated policy intervention has succeeded or failed.

### Notes:

<sup>1</sup> Throughout this article the evaluation effort is called a “project,” while the aggregate of the evaluated activities is called a “program”.

<sup>2</sup> Interim evaluations differ from ex ante evaluations and ex post evaluations in relation to their timing: in the case of interim evaluations the development project which is the subject of the evaluation is ongoing at the time of the evaluation.

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