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Market Imperfections and the Effectiveness of Subcontracting and Informal Institutions in Export Market Transactions in Ghana

By

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**A thesis submitted to The University of Birmingham for the Degree of
DOCTOR OF PHILOSOPHY**

International Development Department

College of Social Sciences

The University of Birmingham

December 2009

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ABSTRACT

The study set out to explore how small exporting firms coordinate production functions and the extent to which the chosen path of institutional arrangements enable them to reduce market imperfections, access resources, meet export market requirements and succeed in the export market. The literature posits that in the absence of effective state institutions, informal and private institutional arrangements tend to govern market transactions. However, little is known about the effectiveness of these arrangements in supporting distant and expanding trade transactions, especially, in Africa. Using the Ghanaian craft export sector as a case, the study showed that the small-scale exporters rely predominantly on informal institutions and subcontracting ties in their export transactions. Yet these informal and subcontractual relations remain inadequate coordination mechanisms for engendering greater export success. Under conditions of market imperfections and endemic opportunism, the informal trade arrangements and loose arm's length subcontracting relations only enable the small firms to achieve imperfect results even in modestly complex and expanding trade transactions. Notwithstanding, informal subcontractual ties potentially offer the platform for the small enterprises to succeed in the export market given improvements in the socio-cultural and the microeconomic environments.

The emergence of "in-house contracting" in the industry is linked to the move by some of the exporters to reduce transaction costs and meet quality standards. By this arrangement, the entrepreneur has some level of control (albeit less rigid) necessary to reduce transaction costs, meet quality requirements, and flexibly adjust to fluctuations in export market demands. The in-house exporter maintains multiple informal and trust building relationships with segmented buyers and subcontractors to keep the production system operational.

ACKNOWLEDGEMENT

I am the unlikely candidate to embark on this PhD journey considering my humble social background but for some individuals and institutions whose immeasurable assistance played a part in the successful completion of this project. Their names need mentioning for appreciation. My foremost gratitude goes to my lead supervisor, Prof. Paul B. Jackson (Head of School of Government and Society), for his constructive comments, direction and advice that helped me to navigate through the PhD process. When my confidence was low, he provided me with one and when my destination was unclear he guided me to chart one. Thanks Paul! Dr. Philip Amis (Director of International Development Department) is worth remembering for his sharp questioning at panel meetings that helped to bring to the fore issues that sometimes escaped my attention. The organization of Research Students Seminars by the International Development Department (IDD) provided an important platform for me to make presentations on the various stages of my work to elicit comments and critique from staff members and colleague research students. Again, the grant received from IDD through its Research Student Bursary in no small way helped to finance part of my tuition fees, without which it would have been extremely difficult for me to start let alone to complete the PhD process.

The next gratitude goes to my grandmother; Dora Sarpomaah. She never had formal education but saw the need to give me one in the absence of my dad (late). Out of her meagre resources as a farmer and a petty trader, she planted the seed and watered it for it to sprout and now it is growing. I share the frustrations and the joy of this achievement with her. Also worth acknowledging are my mother; Theresa Acquah and sisters (Dora, Ama Antwiwaah, Afriyie and Nana Asare) for their encouragement, prayers and love. I say thanks Nana for the support you provided throughout the writing-up process.

My expression of appreciation would be incomplete without acknowledging all the small scale exporters and the other respondents who sacrificed their time to grant me the interviews. Also to Caroline Boateng of Daily Graphic (Ghana) is my heartfelt thanks for proofreading my draft thesis on such a short notice.

TO GOD BE THE GLORY

LIST OF ACRONYMS

AFE	Action for Enterprise
AGI	Association of Ghana Industries
AMC	Associated Merchandise Corporation
ATAG	Aid to Artisans, Ghana
CIP	Craft Initiative Programme
DFID	Department for International Development
EDIF	Enterprise Development Innovation Fund
EPV	Export Production Villages
FAWAG	Furniture and Wood products Association of Ghana
GEPC	Ghana Export Promotion Council
GOG	Government of Ghana
GTZ	Deutsche Gesellschaft Technische Zusammenarbeit
IDD	International Development Department
ITC	International Trade Centre
KNUST	Kwame Nkrumah University of Science and Technology
MOTI	Ministry of Trade and Industry
NAHE	National Association of Handicraft Exporters
NGO	Non-Governmental Organization
NTE	Non-Traditional Exports
PSI	Presidential Special Initiatives
SAP	Structural Adjustment Programme
SGS	Société Générale de Surveillance
SSA	Sub-Saharan Africa
TFOC	Trade Facilitation Office Canada
UNCTAD	United Nations Conference on Trade and Industry
UNDP	United Nations Development Programme
USAID	United States Agency for International Development
WATH	West African Trade Hub

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CHAPTER ONE: INTRODUCTION

1.1 Background to the Research

This project is about the costs to transactions in the export market and the local institutional responses by market participants to reduce these costs. The study is premised on the perspective that there are costs to transacting in the market and therefore institutions are required to mitigate the costs to market transactions. This is the postulation that is found in the intellectual works of new institutional theorists (Coase 1937; Williamson, 1975; North, 1990). This forms a major critique to the neo-classical economic theory that assumes costless economic exchange. An agent involved in market transactions may fail to comply with trade agreements he has entered into with another partner due to capability constraints, information problems, and exogenous economic factors or purely due to indiscipline and dishonesty. In this instance, the market may be imperfect. The works of these leading authors have inspired other studies that have looked at the various dimensions of institutions that support the operations of the market in both the developed and developing countries.

There is now overwhelming support in favour of the argument that unbridled “getting the prices right” policies based on neoclassical economic theory do not sufficiently enable markets to realize their full potentials (Fafchamps, 2004; Parker et al. 1995, World Bank 2001; Lall and Pietrobelli, 2002). In fact, there is the recognition that the post-SAP economies continue to experience endemic market imperfections and failures at the microeconomic level despite some moderate improvements in the

macroeconomic environment. The persistence of market imperfections in many of these economies, according to some commentators, reinforces the insufficiency of neo-classical economic model in addressing those imperfections and to effectively support the operations of the market. This weakness gives strength to the role of institutions in addressing market imperfections. Thus goes the proposition that institutions are required as instruments to reduce market imperfections and promote economic growth. Stein (1995), for example, maintains that the neo-classical economic model remains largely a-institutional and therefore ill-equipped to promote the development of markets, particularly, in Africa.

There is no substitute for effective institutions that support market exchange. The inability of societies to develop effective and low cost enforcement institutions is argued to be the most important source of both historical and contemporary underdevelopment in the Third World (North, 1990). Some observers attribute underdevelopment in Sub-Saharan Africa to the fact that many countries on the continent possess ineffective formal institutions and suggest that Africa's economic experience should be looked at beyond the availability of factors of production and attention directed at seeking institutional explanations to African economic problems (Aron, 2000). The linkage between institutions and development within African context is often not described in palatable terms. Institutions in Africa are regarded as underdeveloped; consisting of ineffective contract enforcement mechanisms with the consequence of restricting the expansion of trade and market development because

ineffective institutions make Africa a high risk and unattractive environment for business (Luiz, 2009).

Posner (1998) draws attention to the need for formal legal institutions like the courts to ensure compliance with contractual obligations and deter opportunism in developing and transition economies. There are those authors who argue for formal institutions that provide third party business services to be strengthened with the appropriate internal tools so as to support many firms in developing economies to overcome technical and informational constraints they face at the micro level (Jackson, 2002; Lall and Pietrobelli, 2002). These studies labeled as meso-level institutional analysis of economic problem are inspired by the recognition that there are deep seated constraints existing at the microeconomic level that critically impede the operations of, especially, small enterprises in developing and transition countries. Meso-institutions (formal and quasi-government agencies) are therefore proffered to enable entrepreneurs to address micro-economic constraints. Without denying the importance of some of these institutions, other arrangements stressing the enabling role of inter-firm relations and other informal institutional arrangements both in developing economies as well as in advanced countries in dealing with market imperfections are also noted (Woodruff, 1998). Macaulay (1963), for instance, demonstrated how businessmen in the USA preferred to rely on inter-personal relations to achieve compliance to contractual obligations instead of resorting to formal enforcements like the courts.

The general consensus in the literature is that in economies where formal third party enforcement systems and service provision agencies are weak or non-existent, economic agents tend to resort to informal institutional arrangements and inter-firm relationships to address their capability constraints and deal with other market imperfections. The lack of effective state-sponsored institutions to provide trade support services and also enforce commercial contracts encourages entrepreneurs to restrict their dealings to those persons they know (Pedersen and McCormick, 1999). This idea is also found in the works of authors that have investigated institutions that supported markets in pre-industrial societies and developing economies (Ensminger, 1996; Greif, 1993; Milgrom et al. 1990). They made similar claims about the availability of informal institutional mechanisms to actors engaged in some sort of economic exchange whether among the Pastoralists in Orma village in Kenya or the medieval traders in Europe. Brautigam (1997), for example, argues that indigenous institutions and personalized relations represent a good substitute and fill the gaps left by failures of both the market and the state in the African context.

1.2 Research Problem

How much do we know about institutions that support market operations in developing economies and especially Africa? There is a lot more to do regarding our understanding of how institutions of their various forms support market exchange. Fafchamps (2004) underscored this need and points to the little knowledge that exists about the institutions that support market exchange and how markets are structured over time, especially in Sub-Saharan Africa. He makes a case for studying African

markets and institutions, and arguing that the analysis of markets in Sub-Saharan Africa within the framework of new institutional economics is not a misplaced venture. The problem of agency arising from the failure of trade partners to commit to trade agreements that plague markets in Sub-Saharan Africa is the very same issue that we find in developed markets and are at the core of the analysis of new institutional economics (Fafchamps, 1997; 2004). It is not in dispute that the imperfections that bedevil markets in developing economies are also commonplace in developed economies but what explains the differences in the operations of these markets is the nature and endowment of the country's institutions. The debate about the appropriate institutional forms for dealing with market uncertainties and risks is raging and unsettled particularly in developing and transition countries. This study seeks to contribute to the discourse on markets and market institutions and takes as its starting point the instrumental role of informal institutional mechanisms and inter-firm relations in addressing market imperfections. This study adopts a tone that is less optimistic about the effectiveness of informal and private institutional arrangements in fostering firm growth as the complexity of trade increases in the context of risk-prone environment. The pervasive opportunism and other forms of market imperfections may be counter-productive to fostering collaborative trade behaviour and thus limit the extent to which agency problems can be reduced.

The general view is that informal mechanisms are effective in more localized markets in which parties to a trade transaction have good information about the market and know each other. Posner (1998) draws attention to the fact that there are "hidden

costs” to the reliance on informal mechanisms as substitutes for formal legal enforcement mechanisms. One such hidden cost, according to Posner, is the bias of informal ties and networks in favour of simple economic exchanges over complex transactions. He accepts that when third party enforcement is weak or nonexistent, economic transactions will be governed by familial alliances but adds that such informal alliances may be dysfunctional in the conditions of a modern economy.

Trade across geographical boundaries brings with it new challenges, which do not lend themselves easily to more localized market arrangements and informal institutional practices. Woodruff (1998) observes that as local enterprises produce and sell over long distances they are confronted with the contractual obligations of meeting large order volumes, tight delivery timelines and quality standards. Trade linkages with international clients may as well expose local enterprises to new opportunities, including access to new market information, product designs and financial resources. Granovetter (1983) observes that market actors who develop *acquaintances* with new economic agents in distant places stand to gain from new ideas and information. The counter argument to this is that individuals who lack ties with outsiders and are confined to their “provincial news and views of their close friends” are deprived of latest ideas and information (ibid, p202). Building trade relationships with external agents such as international buyers may serve as new sources of information and learning for local producers to innovate and upgrade their processes.

The current global value chain literature frames the challenges and opportunities that confront exporting firms from developing countries to encompass either *inclusion* or *exclusion* from international trade. The ability by small firms in developing countries to adapt their products and organizational forms to export market pressures and buyer demands may lead to their inclusion in global trade whereas failure to respond to the market demands and buyer requirements may lead to exclusion from global value chains. The available empirical evidence shows how inter-firms relationships with global buyers have opened new opportunities for firms in developing countries, especially, Asia and Latin America to upgrade their production processes and compete in international markets (Schmitz, 2004). The global value chain analysis focuses largely on how global retailers and wholesalers, wielding enormous market power, coordinate the global chains and how their actions and decisions determine who participates in those chains (Humphrey and Schmitz, 2001, 2002;). There is little knowledge about how local inter-firm relations and local market practices utilized by small enterprises, particularly in Sub-Saharan-Africa, enable them to effectively engage in performance-enhancing trade arrangements with international clients (Bigsten et al. 1998). This study looks at the effectiveness of local institutional responses and market practices in enabling small-scale exporters to reduce domestic market uncertainties and meet export market requirements in their participation in transnational commodity chains.

The study attempts to address the question: *what sort of institutional arrangements and coordination activities make the market work well given that markets are*

imperfect? Within the context of this broader question, the study explores the nature and effectiveness of local institutional responses and market strategies to local market imperfections and export market requirements.

1.2.1 Research Objectives

The specific objectives of this study are to:

- identify the specific socio-economic circumstances at the micro-level (i.e. market imperfections) and export market forces that influence the activities of the small-scale exporters;
- understand the nature of the institutional mechanisms and the inter-firm relationships utilized by the small enterprises in coordinating production activities and;
- explore the extent to which the market arrangements and institutional forms adopted by the small-scale exporters sufficiently enable them to overcome domestic production challenges, reduce transactions cost and address market requirements.

1.2.2 Argument of the Study

Based on North (1991) this study posits that:

The reliance on informal and inter-firm subcontractual relations is useful for coordinating production activities yet it remains inadequate in engendering greater business success in an environment characterized by market imperfections and endemic opportunism.

The new institutional theorists take market coordination as their starting point and their position has been that when it is costly and risky to transact in the market, economic actors may rely on institutions (either formal institutions or informal relations, or both) to provide stability to economic activities and exchange. Coordination of market activities assumes different forms but as demonstrated above, formal institutional mechanisms are

often weak or non-existent in developing economies and as a result firms in these economies tend to rely on informal (private) institutional arrangements to overcome market imperfections (Biggs and Shah, 2006). Private coordination arrangements mean that emphasis is placed on inter-firm linkages encompassing subcontracting arrangements, which are underpinned by informal institutions. That is private coordination arrangement between lead entrepreneurs and their trading agents utilized in combination with elements such as trust and informal group dynamics in their attempt to mitigate transaction costs and gain access to market resources. Subcontracting as a production mode represents a decentralized system in which an entrepreneur contracts out production orders to an independent producer and takes responsibility for the final products. In the subcontracting case investigated in this study, trade agreements are not comprehensively written and are sometimes based on oral agreements. The only written document may be an *order sheet* specifying the physical quality attributes of products that needs to be met but silent on safeguards for breaches of trade agreements and risks.

1.3 Methodology

The study adopts an in-depth case study approach with the aim of obtaining qualitative information on how informal arrangements and inter-firm relations enable the small-scale exporters to access resources; meet export market requirements; contribute to the reduction of opportunistic risks and resolve other constrains pertaining to the local microeconomic environment. This study is about the extent to which inter-firm subcontracting relationships and informal arrangements utilised by small-scale exporters enable them to overcome constraints to production and meet contractual obligations. These phenomena are better understood in their naturalistic state and thus require an

attempt to collect subjective and perceptual information from the selected small-scale exporters about their production processes and the relationships they establish with other firms and economic agents (Nadvi and Schmitz, 1994). These issues do not easily lend themselves to rigid quantifiable measures. The case study approach with its focus on in-depth investigations into real-life and contemporary events using multiple sources of evidence is therefore germane in helping to address the goal of this study (Yin, 2003). In using the case study approach, the stages procedure offered by Nadvi and Schmitz (1994) is adapted to this study (see chapter three for detailed presentation of the stages approach to network studies).

1.4 Conclusion

This chapter introduced the research problem, the research objectives and the main argument of the study. The chapter briefly looked at the debate on the significance of institutions to market exchange and the fact that the absence of effective state institutions partly contributes to the economic underdevelopment in most Third World countries. The paucity of empirical studies on institution and market development in developing countries, especially, in Sub-Saharan Africa highlights the rudimentary nature of market exchange, which is often governed by informal mechanism. In the absence of effective state-sponsored institutions, the argument goes that economic agents tend to rely on self-enforcing and self-provisioning arrangements (private and informal) in their trade transactions. The main thrust of this study is that the availability of the devices of informal mechanisms and inter-firm subcontracting relations to small enterprises makes it possible for them to engage in export market transactions yet these arrangements can

prove inadequate in meeting contractual obligations under conditions of market imperfections and endemic risks. This theme is supported with case-study evidence from the Ghanaian craft export industry, which is characteristically informal but has succeeded in penetrating the international market where the exporters have to confront new challenges to production.

The study is organized into eight chapters. Following the introduction is the chapter on the conceptual framework that provides the theoretical basis for the study. The discussion begins with the premise that market exchanges are neither risk-free nor costless and may entail a lot of failures. That institution is required to provide certainty to market exchanges and the incentives necessary to induce acceptable market behaviour. The relative strengths of (in)formal institutional arrangements, sub-contracting and inside-contracting coordination mechanisms in mitigating market risks and resolving market imperfections are discussed. Also discussed in chapter two is the *governance* of global value chains, which is considered central to transnational organization of production activities, and the implications it has for African enterprises participating in transnational commodity chains. This is followed with a discussion of African informal market; discussed within the framework of institutional approach as a tool for analyzing the form and the dynamics inside the informal economy. The research method is presented in chapter three. The case-study approach to scientific inquiry and particularly, its relevance to not-easy-to-quantify informal network relations are discussed this chapter. Also considered in this chapter are the procedural steps that were followed through during the data collection process. A review of the historical development of the Ghanaian non-

traditional export sector and the characterization of the craft export industry are undertaken in chapter four. Chapter five deals with the microeconomic environment (viewed from the perspective of the respondents) pertaining specifically to the sector of choice. Also considered in chapter five is the presentation of the evidence on the sub-contractual relations between the small export vendors and their transaction partners and other informal trade arrangements. The empirical evidence on inside-contracting arrangement as probably “new” institutional response to coordinating production activities among some of the exporters is undertaken in chapter six. This is followed with a discussion in chapter seven in which the empirical evidence is explicitly and directly related to the theoretical discourse in chapter two. Chapter eight concludes the study.

CHAPTER TWO

CONCEPTUAL FRAMEWORK

2.1. Introduction

The focus of the study is the contractual relationships between principal entrepreneurs and their trading partners and how the relationships they establish enable them to successfully meet their contractual obligations and grow their firms given the context of the microeconomic and institutional environments. The study of inter-firm linkages to economic activities requires a framework with the power to help explore how economic agents interact with other partners and why they decide to interact with others the way they do (Knorringa, 1996). In an attempt to understand how and why the small Ghanaian enterprises interact with other trading agents the way they do in their export transactions, the study relies on the ideas from the industrial organization literature, network analysis and their incorporation into transaction cost theory (Williamson, 1975; Knorringa, 1996; McCormick et al. 1997); all being part of the broader discipline of new institutional economics. Williamson (1975, 1980), explains that the choice of the type of institutional arrangement may depend on the effectiveness of the arrangement in enforcing contractual obligations and minimizing transaction costs surrounding exchange. This is an issue that is concerned with the choice of market and institutional arrangements that best addresses the risks and costs to market exchange. This thinking is premised on the principle that there are risks and costs to transacting in the market and therefore institutions (of different kinds with relative effectiveness) matter to minimize risks (North, 1990).

New institutional theorists unlike mainstream economists do not assume away the costs that are inherent in market exchanges. The market is not costless, for there are costs to negotiating, assembling information, concluding and enforcing contracts (Coase, 1937, Williamson, 1975, 1980). These costs come about because partners to a transaction may behave opportunistically but there are limits to the cognitive abilities of human beings to determine whether or not partners to a transaction would behave dishonestly after contract agreement is completed (Williamson, 1975). Lead entrepreneurs adopt a coordination strategy that enables them reduce transaction costs associated with opportunistic risks and market failures.

This study in particular pays attention to informal trade arrangement, external subcontracting relation, inside-contracting coordination mechanism and their relative strengths in enabling entrepreneurs to minimize transaction costs and at the same time enhance enterprise growth. Also considered in this analysis is the idea that successful entrepreneurs may combine a mixture of coordination arrangements instead of a singular institutional arrangement in responding to agency problems and production challenges.

The chapter is divided into six main sections. Following the introduction is Section 2.2, which delves into transaction cost theory and the concept of market failures. Section 2.3 is about institutions and their economic importance and rehearses the debate in the new institutional economics with emphasize on the relative importance of formal and informal institutions in reducing uncertainties and market risks. Section 2.4 is devoted to subcontracting and inside-contracting coordination mechanisms, stressing the

preconditions for successful subcontracting arrangements and the motivations for inside-contracting as well as their relative strengths in meeting contractual obligations and reducing market risks. An analysis of the global value chain concept and its implications for firms in developing countries, particularly Sub-Saharan Africa, in international trade is presented in section 2.5. The literature that has attempted to interpret African informal markets within the new institutional economics framework is reviewed in section 2.6. Section 2.7 concludes the chapter with a summary of the main themes in the theoretical discussions.

The core themes of the theoretical discussion regarding the choice of market and institutional arrangements by lead entrepreneurs under conditions of extreme uncertainties and risks considered in this chapter are that:

- Informal institutional mechanisms and inter-firm subcontractual relations matter to the coordination of economic activities but remain inadequate in engendering greater enterprise success in an environment characterized by endemic market imperfections (North, 1991);
- Under conditions of high transaction costs and endemic market imperfections rational firms would seek to internalize functions *partially* in-house to gain control over the production process in a bid to reduce market risks and meet market requirements (Williamson, 1975).

2.2 Transaction Costs and Market Failures

2.2.1 Transaction Costs

The neo-classical doctrine places a premium on individual rational choices in resource allocation and assumes zero transaction cost. In the neo-classical economic exchange institutions are considered unnecessary and the economy characterized by efficient market exchanges. If trading partners were to live in a business environment where they could assemble all possible information about their transactions and enforce contract compliance without cost, then they could use the market to insure themselves against risk. This, new institutionalists argue, is far from the real world of economic exchanges that is often characterized by incomplete information, uncertainty and market failures. There are costs to accurately determining the various dimensions of a trade transaction in detail and/or the performance of agents ex ante as well as enforcing agreements ex post. Transaction costs consist of the costs of measuring the attributes of the product or the service that is being exchanged and the cost of enforcing contract agreement (North, 1990, 1991). Williamson is credited with the conceptualization of transaction costs to include the combined human problems of opportunism and bounded rationality, without which there would be no need for economic institutions. These two concepts as put forward by Williamson are discussed below.

Bounded rationality and Opportunism: Human agents in the market place are limited in their cognitive abilities to receive, store and retrieve information. There are bounds to how much information can be gathered by trading partners during contract agreement and execution. This human limitation is compounded by the fact that there is the tendency by

some economic agents to behave opportunistically. Opportunism defined as “self-interest seeking with guile” (Williamson, 1975, p26) together with the cognitive limitations of humans to identify hidden behaviour has implications on the choice of institutional arrangements. However, in the view of Williamson, opportunism poses no problem in a repeated trade interaction in a situation of transparent markets characterized by homogenous goods and many suppliers and where there is no capital or investment of human effort in the transaction process—opportunism is consequently checked through the loss of subsequent transaction. But there are occasions where trading partners may invest in human resource or invest capital specifically in customized goods or idiosyncratic tasks; a phenomenon Williamson refers to as asset specificity.

Asset-Specificity: More importantly, when the principal firm makes certain investments in the transaction that is specific to its needs and such investments are large, uncertain environment and any dishonest behaviour leading to hold-up may raise the cost of monitoring and enforcing contractual obligations. Mackenzie (2008, p869) sums up this transaction cost argument this way:

In an environment of small number exchanges created by asset specificity or idiosyncratic tasks, coupled with uncertainty, complexity and, crucially, the assumed propensity of contract partners to act opportunistically, negotiating, monitoring and enforcing contracts is a complex and costly undertaking.

High level of asset specificity makes threats of opportunism more costly to the investing party. According to Williamson the lead party would seek ways, under this circumstance, to control the other trading partner either by *locking* the partner *into* the relationship or

through hierarchical managerial control to minimize transaction risks (Williamson 1975, 1981). Williamson (1985) considers the degree of transaction-specific investment vis-à-vis the level of opportunism (transaction costs) and uncertainty as cardinal factors that influence the choice of institutional arrangements. In addition to the degree of asset specificity, there are other factors such as length of relationship between the trading partners (Williamson, 1985, Kahkonen and Meagher, 1997) and the size or the volume of the transaction (Hong Hai, 2007) that may affect the choice of institutional mechanism in the midst of threats of shirking and dishonest behaviour.

In a nutshell, transactions involving simple, standardized products, numerous suppliers and buyers where there are low asset specificity and dependency, trading actors can depend on competition as a mechanism to discipline dishonesty by switching or turning to alternative sources of supplies or buyers. In this case market exchange is likely to take the form of arm's length arrangement. On the other hand when the specific investment made in a transaction is high but the risk of opportunism or transaction cost is high the institutional arrangement is likely to take a hierarchical form, especially, where the enforcement of both formal and informal contracts is imperfect.

2.2.2 Market Externalities

According to Bates (1995) market failures arise when the conditions necessary for achieving the efficient workings of the market are absent. The choices of rational individuals may clash or be inconsistent with the “public” good; this Bates calls the “social dilemma” (choices made by rational individuals may yield outcomes that are

socially irrational). He looked at production externality as a type of market failure. It occurs when the activities of one agent impose cost or confer benefits on actors. Some firms may provide generalized services e.g. training of labour that go to promote the productivity of other firms in the industry. Though such externality may be in the general good of the industry, it may not be in the private interest of agents who seek to maximize their self interests to continue to provide such services. In situations of such externalities, the economic actors would have to be induced to continue to provide such services through other forms of incentives. The non-provision of such services because of the lack of incentives to do so may be a cost to the general good of the industry, especially if it is essential for the effective workings of the industry. For example, product designers may be discouraged to come out with innovative designs if other members in the industry can copy their designs without respecting patent rights. Institution provides the mechanisms that could help to overcome the tensions that may arise between private choices made by rational individuals and what are “publicly” rational outcomes. The assignment of, for instance, property rights(institution), in the view of Bates (1995), limits the problem of free riding and provides incentives for maximizing private agents to make production decisions that are “publicly” beneficial.

2.3 Institutions and their importance to economic activities

Transaction costs and market failures provide the sources of importance for institutions. Williamson (1981) places the combined existence of bounded rationality, asset specificity and opportunism at the centre of transaction costs theory and the analysis of economic institutions. Under the conditions of imperfect information and opportunistic risks,

institutions are required to provide the incentives and the certainty for trade interaction to take place (North, 1989, 1990). Institutions matter when it is costly to transact (North, 1995) and when market failures are pervasive (Bates, 1995). The utility of institutions as human devices are designed:

...to create order and reduce uncertainty in exchange...and therefore determine transaction and production costs and hence the profitability and feasibility of engaging in economic activity (North, 1991, p97).

The theoretical discourse in this section looks at the enabling role of institutions in economic exchange. In particular, attention is given to the elements such access to information about trading partners, effective enforcements and sanctions as critical in reducing transaction costs. In doing this, an attempt is made to analyze the relative importance of both formal and informal institutions in reducing transaction costs. The debate surrounding the role of informal institutional arrangements to transaction cost reduction and their inherent inadequacies in facilitating economic exchange is given weight in this discussion. Almost all the scholarly works on institutional analysis tend to reduce the function of informal institutions to enforcement, often neglecting the other functions of informal relations. Informal trade arrangements are self-enforcing as well as self-provisioning. Barr (1998), for example, showed that informal institutions in the form of interpersonal ties could play multiple functions of minimizing risks and at the same time be a conduit for the sharing resources. This study views informal institutions in both its enforcement and resource provision functions. The theoretical position that forms the basis of this analysis is that informal trade arrangements enable enterprises to minimize risks, enforce contractual obligations and facilitate access to resources for growth *but*

limitedly so under conditions of pervasive market failures and complexities that accompany expanding trade.

2.3.1 What are Institutions?

The new institutional economics literature is replete with different perspectives as to what the definition of institutions is. Following North (1990, p3), institutions are conceived as the “rules of the game” or “humanly devised constraints that shape human interaction”. Human constraints expressed in rules, codes of conducts and the associated enforcement mechanisms, according to North, reduce transaction costs and facilitate division of labour and specialization. The thinking from the transaction cost school of thought is that we live in an uncertain world where there exist risks and complexities. Human beings therefore devise institutions in their attempts to control their economic environment so as to reduce transaction costs (de Soysa and Jutting, 2006). The understanding of institutions is not only conceived in terms of rules-setting or the accepted behaviour that should be followed through by transaction partners or groups of people but also extends to mechanisms for enforcing compliance and prescribes the consequences of violations. Institutions define what people are “prohibited from doing and the conditions under which individuals are permitted to undertake certain activities” (de Soysa and Jutting, 2006, p3). The consequences of dishonesty must be severe enough to deter future breaches in repeated interactions: “the future costs should outweigh the immediate benefit in the individual’s own calculation...whether for material things, social standing, internal guilt or whatever” (Dixit, 2004, p60). Through its effect on reducing transaction costs and safeguarding agreements, institutions can also generate the incentives for economic actors

to undertake productive activities. Strong institutions can discourage dishonesty and free riding and induce productive behaviour by positively affecting the incentive structure that agents face by safeguarding investment (Luiz, 2009). Institutions as market constraining devices embody the elements of rules or norms, effective monitoring and enforcement of the rules or the norms to ensure that trading partners or a group of market participants them and breaches consequently sanctioned.

Based on the degree of formality, institutions can either be classified as formal or informal. Though operating on different principles and mechanisms both formal and informal institutional arrangements can achieve the goal of reducing transaction cost and as a result create the condition for economic exchange to take place. While formal institutions such as contract law, property rights and public standards are created and enforced by the nation-state, informal institutions essentially remain undocumented, may emerge spontaneously and be self-enforcing (Williamson, 2009). There is no firm agreement in the literature regarding which of these types of institutions is more important or effective in supporting market exchange. One side of the debate supports the view that formal institutions (laws, property rights, legal contracts, and public quality standards) enforceable by state-sponsored third party are better able to support complex and impersonal trade arrangements. There are also those who hold the position that informal institutions provide good substitute for ineffective and inefficient state-sponsored institutions in facilitating market exchange. The third way is the position that both formal and informal institutions are complementary institutional forms in facilitating market exchanges. These three strands of the debate are discussed below. This study in

particular shows that informal institutions and informal subcontracting relations are important to market transactions because they are predominantly utilized by the case-study enterprises in their export transactions. The main caveat, however, is that informal ties and informal subcontracting relations are least robust in addressing agency problems and complexities associated with expanding trade under conditions of local capacity difficulties, socio-cultural problems, informational problems and enforcement challenges.

2.3.2 Formal Institutions and Market Transactions

Formal institutions are written rules that are devised to constrain human interaction and exchange. Formal enforcement mechanisms rely on third party agencies such as the court to enforce contract agreements or quality assurance bodies to provide standard formulation, certification and quality monitoring. In this case the rules of the game may be set or designed by the partners to the transaction (or a third party) and contract breach litigated for example by the court or quality assurance bodies (private or public) providing standard formulation and monitoring services to ensure compliance. The argument that is often put forward in support of formal institutions is that they are better able to support complex and impersonal transactions. According to Kahkonen and Meagher (1997), impersonal market exchange is made possible because effective state sponsored institutions can provide for predictable, transparent, impartial and low cost enforcement of contract. These, according to them, provide certainty for market transactions and also the threat of legal action can act as a check on opportunism. Contract law, for example that is administered by a third party, normally the state, specifies the terms of agreement, sets out the grounds and consequences of breach, and

backs up transaction with the third party's power to extract penalties (Hadfield, 2004). The understanding that strong formal institutions reduce uncertainty and risks induces economic agents to make credible commitments to strangers, thus making it possible for anonymous individuals and firms to transact business across communities (Kahkonen and Meagher, 1997). This is because formal institutions protect and tie the hands of economic agents so that they do not behave opportunistically in entering trade relations by misrepresenting their performance or behave opportunistically afterwards by walking away from commitments (Hong Hai, 2007). The assumption is that by clearly setting out the parameters of a contract and specifying *ex ante* consequences of breach, opportunism is prevented *ex post* (after agreement is written) and as a result increase the confidence of actors to engage in anonymous market exchanges. But what if, for instance, formal enforcement mechanisms are ineffective and what is the implication for the choice of institutional responses by market participants (Fafchamps, 2001)? North (1990) sets out the conditions for effective formal enforcement to include the *ability* of the third party enforcer to measure the attributes of the contract and enforce agreement impartially at low *costs* such that the offending party always has to compensate the injured party to the degree that makes it costly to violate the contract. The costs to formal contracting and enforcement may relate to information gathering and dissemination, time and investment in human resources. Hadfield (2004) has observed that for third party enforcement to be effective, these costs must not outweigh the gains of resolving contract dispute. For "in an environment with only high-cost enforcement mechanisms, only high-value contracts and those that are supported effectively by baseline institutions such as trust and family relationships are likely to go forward" (Hadfield, 2004, p10). Greif's (2006) analysis of

the Maghribi traders highlights how commitment problems by the traders were resolved outside the realm of the court system. Not only was the settlement of commercial dispute via the court system expensive and time consuming but also the courts lacked the capacity to collect information that was required to adjudicate trading dispute or simply some of the trade agents were above the law and could not be sued. They instead relied on “coalitions” to surmount commitment problems (the concept of coalition is discussed further under informal institutions).

The primary focus of this study has not been to explicitly investigate the effectiveness or otherwise of formal institutions in mitigating agency problems. This is not in any way to discount the importance of formal institutions to market transactions. The reason has more to do with the theoretical disposition of this study, which emphasizes the facilitating role of inter-firm linkages and personal ties in market transactions and the extent of their effectiveness. It is also informed by the fact that the environment within which this study (based on the reviewed literature) was conducted is generally characterized by imperfect and unresponsive formal institutional arrangements. It is true that where the legal system is weak, where dispute settlement through the court is cumbersome or where the size of the transaction between the partners is relatively small, trading partners may bypass formal enforcement mechanisms and resort to personalized enforcement mechanisms to circumvent the time consuming and expensive dispute resolution through the court process (Fafchamps 1996; 2001). The literature highlights the existence of weak formal mechanisms of enforcement in the areas of commercial dispute resolution, compliance with quality standards and unresponsiveness of formal institutions to small-scale

enterprises in many countries in Sub-Saharan African (Fafchamps, 2001; Lall and Pietrobelli, 2002). Under the conditions of weak formal institutional setting, certain agents resort to self-enforcing mechanisms to reduce commitment problems as well as a reliance on private provisioning to overcome internal capability constraints to trade, which is often the case in many Third World countries. The next section examines the extent of the role of informal institutions in market transactions as espoused in the literature.

2.3.3 Informal (Private) Institutions and Market Transactions

Opportunism and dishonesty could alternatively be mitigated by personal ties between transacting partners. The use of informal enforcement mechanism through group pressure and reputation effect could lower the cost of transacting and therefore the need for fewer formal safeguards to achieve contract compliance (Knorringa, 1996; Keefer and Shirley, 2000). The idea of the role of interpersonal relationships in reducing deceit and shirking in economic transactions is firmly rooted in Granovetter's (1985) idea of embeddedness. This concept "stresses...the role of concrete personal relations and...networks of such relations in generating trust and discouraging malfeasance" (p490). Granovetter argued that the widespread preferences for transacting with agents of known reputation imply that few are willing to rely on generalized (formal) institutional arrangements to guard against opportunisms. He identifies four grounds that make it is better to rely on personal relations for information in economic transaction; i) it is cheap ii) it is richer, more detailed and known to be accurate iii) individuals with whom one has a continuing relation have an economic motivation to be trustworthy, so as not to discourage future

transactions and iv) continuing economic relations that are embedded in social relations carry strong expectations of trust and abstention from opportunism.

Informal institutions, from a Northian perspective, are human constraints that emanate from shared norms of behaviour or code of conduct of social groups that govern human interaction. Viewed against formal institutions, informal institutions are private human constraints that stem from norms and customs (Williamson, 2009). Unlike a formal institutional arrangement in which contractual obligations are enforced by a third party mostly through the authoritative power of the state, informal institutional arrangements rely on self-enforcing mechanism to ensure that contract terms are adhered to. The members of a social group police themselves to enforce compliance to group's norms. Informal constraints are socially sanctioned norms of behaviour and internally enforceable standards of conduct (North, 1990). Members belonging to informal trading associations or groups often share the common view that they are "in it together" (Mead 1984, p1101) and that, even though informal constraints are unconsciously designed, "it is in everyone's interest to keep" (North 1990, p41). Therefore, aberrations of the norms of behaviour and the code of conduct by a member are viewed as negatively affecting the reputation and cohesion of the group and as such are met with sanctions that may see the member being ostracized. The fear of being ostracized from a social group or the expectation of future loss of trading relationship may check deceit and induce acceptable commercial behaviour between trading partners and among groups (Nadvi and Schmitz, 1994; Bigsten et al. 1998). Sanctions in this context take the form of loss of reputation or valuable future relationship.

There is rich empirical evidence that highlight how informal institutional mechanisms have enabled trading partners to mitigate problems of contract commitment and trading risks. The Maghribi traders' coalition (Greif, 1993, 2006) and the Grameen financial arrangements (Morduch, 1999) are both cases in which informal institutions were utilized in their respective transaction regimes. The Maghribi traders through the instrumentality of the "coalition" were able to deal with overseas agents despite the commitment problems that were inherent in the relations. The "coalition" was an institution in which implicit contractual relations and specific information-transmission mechanism supported the operation of a reputation mechanism that enabled the traders to overcome commitment problems. That a reputation mechanism governed agency relation such that traders conditioned future trade engagement on past conduct, practiced community punishment, and ostracized agents who were considered cheaters until they compensated the injured, and that agents were ready to forgo immediate gains to sustain their standing in the trader's group (Greif, 1993). Greif noted that the coalition was closely knitted together such that members were committed to engage in transactions with other Maghribis in far places.

The Grameen model is touted in the microfinance literature as offering institutional promise for mitigating information asymmetries between a formal lending institutions and small-scale borrowers by utilizing a *peer monitoring system*, which economizes on monitoring costs and maximizes the rate of repayment (Stieglitz, 1990; Ghatak, 2000). The Grameen banking model illustrates how formal banking institutions rely on informal mechanisms such as group solidarity pressure to administer loans to small scale

producers in many developing countries (Morduch, 1999). This informal financial arrangement, which originated from Bangladesh and has been replicated in a number of developing countries, enable small firms who may lack physical collateral to access formal credit (Morduch, 1999). The basic principle of this model is that by making a group jointly liable to loan repayment members are induced to monitor their peers to ensure that the loans are used productively for the intended purpose, which ultimately minimizes default rate. The group members only gain access to further credit if the group debt is discharged; a default by a member leads to denial of credits to any other member of the group. In this instance, the members have the incentive to monitor each other and to exclude risky borrowers from participation, thus promoting repayment (Morduch, 1999). The peers possess rich information about each other regarding their conduct in utilizing the credit to execute the actual production activities. Through the peer monitoring mechanism, the bank is able to minimize information asymmetries and monitoring, which often present the main challenges of managing small credits to small producers. Peer monitoring, in other words, acts in stead of conventional collateral in insuring against default but there are conditions under which this is sustainable. The success of this model according to Stiglitz (1990) depends on the size of the group. The model, according to him, thrives on small group size because that increases the risk from a default by a single member but increases the incentives for peer monitoring. He argues that large group increases the problem of free riding; each member in the group would prefer that others invest time and energy in monitoring. It is also not clear how effective these intangible assets such as peer monitoring in minimizing default are as both the size of the group and credit increase.

Ensminger (1996) similarly observed a situation where Orma traders in Kenya rely upon informal arrangements i.e. paternalistic relations to address pervasive agency problems. Keefer and Shirley (2000) made a similar claim in China, where informal institutions i.e. personal ties with local leaders, help insulate foreign investment against local deceit. They were, however, quick to point out that informal institutions incompletely explain the success of foreign investment in China and add that formal institutional checks embedded in the Chinese decentralized political system complement informal institutions in this regard.

Related to the foregoing analysis of informal mechanisms is third-party private enforcements and provisioning (private intermediaries), which is argued to constitute an alternative path for filling institutional gaps that may arise as a result of weak state institutions, which provide trade support services. “If the government does not provide contract enforcement using its general revenues, then a private person may be able to do so for a profit” (Dixit, 2004, p97). Gambetta’s (1993) classic work; *The Sicilian Mafia and the business of private protection* is cited to support the claim of third party enforcement in the context of weak public provision of security by the state. Gambetta begins his book by recounting what a cattle breeder had told him to highlight the core thesis of his analysis of the business of mafia protection:

When a butcher comes to me to buy an animal, he knows that I want to cheat him [by giving him a low quality animal]. But I know that he wants to cheat me [by reneging on payment]. Thus we need Peppe [that is a third party] to make us agree. And we both pay Peppe a percentage of the deal (Gambetta, 1993, p15; also cited in Dixit, 2004, p99).

Gambetta (1993, p16) went further to explain that the intermediary function of:

Peppe was mainly selling information, thereby making the transactions possible, and that it was for this service that he received a 2 percent commission. When in addition he acted as a guarantor of quality and payment, the percentage increased.

The services of Peppe were of two kinds, provision of information specific to the transaction and ex post enforcement to deter shirking and achieve compliance on commission basis (Dixit, 2004). The success of private third party intermediation as an alternative institutional path is contingent on the extent to which the intermediaries are able to discourage free-riding by making their services unavailable to non-clients. And for clients to continue to transact or use third party services, the intermediaries must credibly commit themselves not to use the trade information they possess for extortion or double crossing (Dixit, 2004).

2.3.4 The limits of Informal Institutions

Despite the significance of informal institutions to market exchange in the absence of strong formal institutions, there are those authors who question the efficacy of informal institutions in supporting complex, impersonal and expanding trade volume. Keefer and Shirley (2000), in their analysis of the relative weight of formal and informal institutions in safeguarding contractual obligations argued that informal institutions are insufficient when it comes to sustaining economic growth because informal institutions are weak in protecting specific investment from opportunistic hold-up and also do a poor job in guaranteeing quality of goods of manufacturers that exhibit important and hard-to-measure quality attributes. Informal institutions are also regarded as restrictive in that they are often not available to most potential participants in the market since network

participants tend to trade with people they know. Greif (1994) makes a contrasting analysis of the efficacy of the institutional arrangements adopted by the Maghribi traders and the Genoese traders. The Maghribi traders as indicated earlier relied on informal group dynamics to assemble and transmit information and reduced agency problems but could not expand the scope of their trade outside the Maghreb's coalition (overseas trading was even done through agents who were themselves Maghribis). On the other hand, the Genoese traders who were culturally individualistic and used more bilateral arrangements backed up with formal enforcement systems benefitted from opportunities that emerged from trading with other traders outside the Genoese group. Another downside to the use of informal networks is that it may also minimize the gains of trade because the long-held trusted and few partners in the locality may face the same problems (Ensminger, 1996) and may impede exposure to new ideas. In a more recent study of contract enforcement in the Mexican footwear industry, Woodruff (1998) observed that informal associational mechanisms facilitated and sustained trade by reducing the cost of information (by creating a common data-base platforms easily available to members) about the reliability and behaviour of trading partners. Clients who reneged on payments were blacklisted and the agents of the trading association frequently used threats of listing defaulting clients in the "defaulted clients" bulletin as a reputation mechanism to enforce repayment. He indicated further that this informal enforcement mechanism worked effectively within the context of the Mexican closed economy but trade liberalization in 1987 weakened the sanctions that the manufacturers were able to apply to domestic retailers who behaved waywardly. This is because the latter were able to procure products from abroad and as such could not be held captive in the informal associational

mechanism. Likewise, since foreign buyers had never been captive to Mexican producers, the informal associational “coalition” was ill-equipped to monitor them. In effect, informal institutions may be imperfect for enforcing contract obligations within the context of an expanding and complex trade. The difficulties of monitoring and enforcement make informal contracts as market constraining mechanisms less effective.

According to North (1990, 1991), in the early stages of a country’s development, its economy is characterized by informal institutions that seemingly work well for the largely traditional economic activities. Most transactions in this instance takes place within a dense social network of informal constraints and the reputation of the parties to the transaction are known. Contracts are enforced through these mechanisms to avoid deceit. The simplicity of trade makes the reliance on informal mechanisms possible.

An expanding trade regime and increasing specialization consequently increases agency problems and the difficulty of contract enforcement becomes more complex and elaborated. In the view of North (1991), as trade expands and transcends geographical boundaries, the possibilities for conflict over exchange grow; difficulties over information gathering and enforcement of contract terms also increase. Formalized rules, contracts and third party enforcement bodies help to align the interest of agents to that of principals and resolves transaction disputes and thereby reduce monitoring cost. The expansion of trade:

...need[s] effective, impersonal contract enforcement because personal ties, voluntaristic constraints, and ostracism are no longer effective as more complex and impersonal forms of exchange emerge. It is not that those personal and social alternatives are not important; they are still

significant ...in today's interdependent world. But in the absence of effective impersonal contracting, the gains from "defection" are great enough to forestall the development of complex exchange (North 1991, p100).

Following North, Luiz (2009) makes a similar observation about the relative rigour of informal and formal institutions in supporting anonymous and complex trade regimes and indicates that in simple economies one can trust one's neighbour because one knows the family or the community and therefore reputation effects and community sanctions are possible. But as the economy becomes more sophisticated, a corresponding need arises for formal institutions because one is more likely to engage in anonymous exchange where the family is not known. Investment of trust in formal institutions would be a better substitute for group sanctions.

North (1991) and others in effect are arguing that as the market expands and trade increases, there is a parallel need for the evolution of institutions from informal to formal to deal with the complexity of trade. Legal enforcement and not personalized transactions enhances the economic reach and the range of partners they can transact with, without prior acquaintances (Fafchamps, 1996). In this case impersonal institutions replace personalized interaction and one is likely to engage in anonymous transaction without necessarily having to know the other partner. The accessibility and the large reach that is obtainable from formal institutions encourage high volume trade and specialization (North, 1991; Keefer and Shirley, 2000). Hence formal institutions can promote trade in ways that informal institutions cannot (Keefer and Shirley, 2000). Ensminger (1996) also notes that traders stand to gain from broader trade and specialization but this is

achievable when formal institutions are developed, which would enable the traders to deal with anonymous partners in good faith. But North (1991, p107) notes that the incentive to devise or the willingness to resort to formal enforcement mechanisms largely depends on the volume of trade. In other words, the evolution of formal institutions is causally related to the volume and complexity of trade:

That is the increasing volume of distance trade raise[s] the rate of return to merchants of devising effective mechanisms for enforcing contract. In turn, the development of such mechanisms lower[s] the costs of contracting and [makes] trade more profitable.

Similarly, Posner (1998) on his commentary of legal reforms in developing and transition economies alludes to the chicken and egg dilemma that characterizes the relationships between legal reforms and economic development. A poor country may not be able to pay for a good legal system, but without a good legal system that country may fail to grow its economy in order to be able to afford good legal system. Economic growth in his view is important on both the demand and supply sides of legal reform: i.e. to stimulate demand for legal services and to generate the resources necessary for the supply of legal services. He, however, indicated the need not to over-exaggerate the debate but instead for countries to proceed in building legal systems gradually and incrementally, commensurate with the modernization of their economies.

The possibility is also there for economic agents to engage in trade transactions in a society that boasts effective formal institutions to apply legal contractual arrangements and simultaneously resort to informal institutional arrangements. Macaulay (1963) for

instance demonstrated that even in the US with developed formal systems, businessmen do resort to inter-personal relations in their business dealings. He showed that in some instances trade agreements may take on the form of formal contracts but breach of contract terms may not be subjected to legal sanctions but instead “good faith” dispute resolution may apply. The motive here is that parties to a transaction may choose to rely on informal enforcement mechanisms instead of more coercive formal legal actions to extract contract compliance if they want to preserve their business relationship (Fafchamps, 1996). Formal enforcement mechanisms, especially the more coercive actions may undermine personal trust building (Klein Woolthuis et al. 2005; Mackenzie, 2008). Even if formal contracts are considered effective institutional tools for reducing opportunistic risks, the imperative according to Williamson is that reaching a comprehensive contract entailing all unforeseen contingencies is an impossible exercise during and after contracting due to limits on rationality. This implies that to arrive at a complete contract with all the relevant information to a trade transaction in order to protect oneself from opportunism would be deficient without informal institutions or trust (Lorenz, 2000). Relational contracting as a complementary institutional tool has the advantage of enabling market participants to access hidden information about quality and standards as well as the behaviour of trading partners (Johnson et al. 2002).

The foregoing discourse looked at the theoretical debate regarding the relative effectiveness of formal and informal institutions in reducing agency problems and high transaction costs. Strong formal institutions according to the literature are effective in sustaining impersonal economic transactions and high volume trade. In the absence of

effective public formal institutions market participants may either resort to informal institutions in their business transactions or rely on third parties to meet contractual obligations. Both public formal institutions and informal self-enforcing/self-provisioning mechanisms could reduce the problems of agency and sustain specialization; however, of the two forms of institutions, self-enforcing institutions (inter-personal ties and informal networks) may prove less equal to the task of mitigating non-commitment to contractual obligations. Particularly, the lack of personal trust, a prerequisite for sustaining inter-firm relations, implies that informal institutional arrangement becomes less suitable mechanism for sustaining trade specialization. The distinction between the instrumentality of formal and informal institutions in facilitating market exchange may remain at the artificial level since both institutions may be used to complement each other in supporting market transactions.

2.3.5 What if Informal Institutions are Insufficient and Opportunism Pervasive?

It is obvious that the original theorists of new institutional economics undertook their analysis within the specific context of the industrialized countries where there exist, generally, strong formal institutions that support trade specialization. How do economic agents reduce transaction costs and market failures in an institutional environment characterized by informal institutional mechanisms that seem limited or inadequate as agents seek to engage in long-distance and expanding trade? Clearly, these characterize the institutional setting of many developing countries; more so, in Sub-Saharan Africa (see a detail discussion on this subject in section 2.5). More questions are raised as to how economic agents organize or coordinate economic activities in response to imperfect

institutional and economic environment in those societies. Bigsten et al. (1998), for example, makes an important observation about countries in Sub-Saharan Africa relying on market practices where delays, late payments and breach of other contract obligations are to some extent tolerated in order to surmount not just deceit but also other exogenous factors pertaining to the broader socioeconomic environment that may impede contract performance. The question of how such practices, for instance, fare as African entrepreneurs seek to trade with international clients, where there is the culture of stricter adherence to contract terms, largely remains open (Bigsten et al. 1998).

What happens to market transactions in situations where informal mechanisms are infeasible, either because the scale of market participants is too high or the informational network and the system of group sanctions are too weak, formal institutions unavailable and transaction cost high (Dixit, 2004). The solution in terms of institutional arrangement offer by Coase (1937) and Williamson (1975) is that entrepreneurs who are faced with extreme market imperfections would seek to internalize transactions in-house to save on the cost of opportunism and other market risks. This study also takes the position that entrepreneurs facing uncertainties regarding their trade transactions would internalize production functions within the boundaries of their firms in an effort to minimize risks and market failures. However, in the particular case of entrepreneurs in the sector of choice for this study, the extent of the internalization they adopt assumes a form that is partial in nature to accommodate the flexibility that is required to adjust to changes in the volatile end market; an arrangement termed as inside-contracting. Inside contracting is a quasi-firm arrangement in which the production process is conducted partially in-house

under the indirect command of a principal entrepreneurs; affording the entrepreneur control over the production process.

2.4 Sub-Contracting and Inside-Contracting Arrangements

The obsession with the human problem of opportunism blinds Williamson to recognize other positive aspects of human behaviour such as personal trust in allowing production functions to be undertaken independently of a leading enterprise without having to internalize those functions in-house. The crafting of organizational hybrids between market and hierarchy offer the lead enterprise more flexibility than the rigid hierarchical structure, which enables the lead firm to reduce transaction costs and at the same time able to adjust easily to unstable markets situation (Mackenzie 2008). Production networks conceived to be intermediate arrangements, for instance, are described as “lighter on their feet” than centralized firms (Powell, 1990) in responding to unanticipated changes in demand.

Williamson’s classical transaction cost theory is also criticized for its prime focus on the alternative organizational forms or contractual relationships between market and hierarchy, ignoring intermediate modes of organizing production such as production networks and subcontracting. Again, the transaction cost framework regards the flow of inputs, output and skills as given (Cooke and Morgan, 1998) and organizational forms as “comparative static” instead of treating them as a dynamic process (Foss 1993, in Cooke and Morgan, 1998). Between the extremes of spot-market transactions and highly centralized firms are intermediate forms of organization:

Moving from the market pole, where prices capture all the relevant information necessary for exchange, we find putting-out systems, various kinds of repeated trading, quasi-firm, and subcontracting arrangements towards the hierarchy pole... (Powell, 1990, p297).

The evolution along the continuum is not unidirectional. The development of the production arrangements could begin from subcontracting arrangement towards either spot market arrangement or hierarchy. Intermediate production arrangements, whatever form they take, may be adopted for more than just the motive of reducing transaction costs but also could facilitate access to finance, the flow of market information and sharing of innovative ideas; necessary for firms' growth.

Both sub-contracting and inside-contracting are conceptualized as intermediate market coordination arrangements between the "buy or make" hypothesis. The basic idea that is expressed in this section of the analysis is that inside contracting systems and external subcontracting have relative strengths in addressing agency problems as the size and complexity of trade increases under conditions of market imperfections. The purely market-based putting-out production arrangement may enable entrepreneurs to gain access to some important resources and also overcome their own internal capacity difficulties, however, within the context of weak institutional and microeconomic environments, entrepreneurs relying on inside contracting arrangement are comparatively better able to deal with agency problems and address product/process complexities associated with modest trade expansion. Opportunistic tendencies and weak contract enforcement make the sustenance of informal subcontracting as a production arrangement

less appropriate for enterprise success. As demonstrated in chapter 6, the reality is also more complex than the simplistic alternative responses of either external contracting or inside contracting. Instead rational entrepreneurs may choose a complex mix of external and internal contracting arrangements in response to differing risks and production challenges. This complexity pertaining to the case study industry on one hand reflects a drive towards internal integration as manifested in inside contracting. On the other hand, it shows the development of steady network of contracting relations based on inter-personal trust building.

2.4.1 Trust and Subcontracting Relations

The burgeoning literature on network analysis stresses the role of inter-firm relations in enhancing the performance of small enterprises and enabling them to compete both in the domestic and international markets. Nadvi and Schmitz (1994) carried out an extensive review of empirical works on clusters in developing and developed countries and stressed the importance of inter-firm relations to the competitiveness of small firms. Generally, production networks facilitate sharing of information about product development/specifications, quality standards and also could help to lower transaction costs and uncertainty (Nadvi and Schmitz 1994; Barr 1998). Abigail Barr also looked at the linkages between the structure and functions of networks and how they may affect the performance of enterprises. She distinguished between what she called innovative networks and solidarity networks. Innovative networks are diverse, relatively large, allowing information about markets and skills to accrue to network members and utilized for the motive of enhancing enterprise performance. Solidarity networks on the other

hand, are small and homogenous and deployed for the purpose of reducing uncertainty and mostly patronized by small firms.

Sharing important market information and technical skills, even involving specific investment, between independent trading partners is made possible when there is long-term trust building relationship between the partners (Schmitz, 1999). Trust remains an important intangible ingredient that sustains production networks. Personal trust enables inter-firm relations to flourish, whereas opportunism or distrust can be counter-productive to the building of robust production networks (Fafchamps, 1996).

Sako (1997, p3) defines trust as “an expectation held by an agent that its trading partner will behave in a mutually acceptable manner (including the expectation that neither party will exploit the other’s vulnerabilities)”. Gambetta (2000) explains that when we say someone is trustworthy, it means the possibility that the individual will perform an action that is beneficial to us is high enough for us to consider engaging in some form of cooperation. Humphrey and Schmitz (1998) observe that trust involves an accepted vulnerability to a partner’s ill-will and go on to raise the question of how one can locate trustworthy partners for transactions if the world does contain opportunists. On what basis is trust formed and how does its basis change over time (Schmitz, 1999)?

Zucker (1986) makes a distinction between characteristic-based and process-based trusts. According to Zucker, characteristic-based trust is tied to a person depending on features such as family background, ethnicity or a group membership. The “trustworthiness of an individual is defined by membership of a group who the agent considers trustworthy...

and this identity establishes common meanings...about exchange” (Humphrey and Schmitz, 1998, p 38). The Magribi traders’ coalition discussed under informal institutions in section 2.3.3 bears resemblance to the formation of trust based on social-cultural identity. Characteristic-based trust is developed as a result of the inter-personal embeddedness of trading parties who share common cultural or social norms (Granovetter, 1985). Members belonging to a common social group (in addition to internal sanctions to sustain the reputation of the group) would be more confident in transacting business with each other. Schmitz (1999) terms this as ascribed trust; implying a belief in solidarity (in addition to sanctions) and not in the sense of blindly trusting anybody belonging to a particular family, ethnic group or a local community.

Processed-based trust is formed as a result of direct *experience* of cooperation with trading partners (Zucker, 1986). It develops through recurring inter-firm transactions, where partners invest in the relationship over a period of time (Humphrey and Schmitz 1998). According to Humphrey and Schmitz (ibid) repeated interactions allow the partners to learn and understand the motives of their partners. It is developed through the actual processes of doing business and the partners commit themselves to the transactions by consciously investing in the relationship for their mutual good. Sako (1997, p3) refers to this as “good will” trust, where the parties “make an open-ended commitment to take initiatives for mutual benefit while refraining from unfair advantage taking”. This way trust is *earned* through conscious investments by the trading partners (Schmitz, 1999).

The basis of trust also changes with time. Humphrey and Schmitz (1998), Nadvi (1999) and Schmitz (1999) in their analyses of industrial clusters in Brazil and Pakistan have shown how the basis of trust can evolve from characteristic-based trust to earned-trust. The authors showed that early industrial activities in the clusters were facilitated by trust based on socio-cultural ties. However, the influence of socio-cultural ties diminished over time as outsiders with whom local producers share no social ties began to play a key role in the clusters' growth. Schmitz (1999, p144) summarized the changing ties in the Brazilian Sino Valley shoe cluster as follows:

The resulting boom...weakened the socio-cultural ties which had facilitated exchange and cooperation. Export agents were beginning to play a major role, not only as traders, but also in product development, quality inspection and technical assistance. In order to succeed in external markets satisfying the foreign export agents took precedence over all other business relationships ... by 1980s the local industry had become highly differentiated and the old socio-cultural ties had little influence on inter-firm relationships.

As local producers begin to trade with external clients, who may serve as new sources of market information and technical know-how, it implies the need to build new bonds of relationships with the external agents in order to benefit from such resources (Nadvi, 1999). Schmitz (1999, 145) observed that in the 1990s as the Sino Valley cluster experienced stiff competition from China and the export boom that began in the 1980s abated, the local producers had to return to “ a greater spirit of cooperation” based largely on conscious investments in inter-firm relationship. Schmitz's observation is consistent with Granovetter's (1983) analytical distinction between strong ties that are formed around non-economic identities and weak ties developed through frequent business interactions. The latter is regarded as important for achieving competitive advantage,

however, there may be barriers to building weak ties or business ties since building them requires investment. Meagher (2010) argues that the ability of economic agents to build and maintain stable business ties is a function of the social and economic characteristics of the agents. According to her, wealth, gender, education and the performance of individual firms are important requirements for shaping how producers navigate the shift to new business ties. Meagher (ibid) observed that producers in the informal shoe and garment clusters in Aba, Nigeria are increasingly developing weak ties based on considerations such as quality, reliability and price rather than communal solidarity. In other words, having the capacity to produce quality products in a reliable manner is an important condition for building weak ties. However, for the less well-endowed informal producers:

weak ties are not always sources of strength. While they may widen access to resources, they involve more exacting conditions for the development of trust and economic collaboration. Those unable to meet these requirements are either thrown back on narrow and under resourced networks or abandoned to more unstable business contacts based more on opportunism and desperation than trust (Meagher, 2010, p88).

It will be demonstrated in this study that the ability of the Ghanaian craft exporters to build processed-based trust with local artisan subcontractors and international buyers are important in enabling the exporters to gain access to skillful artisan labour, market information and sometimes finance. The exporters in the Ghanaian craft industry rely predominantly on subcontracting relations for their production activities but the effectiveness of the subcontracting relations in ensuring growth depends on the degree of *built* trust that pertains to the relationships. It will be shown in chapter six that the

exporters who are formally educated, possessing in-house production capacities and able to meet quality standards and delivery timelines have been able to build business ties with artisan subcontractors and international buyers, enabling them to gain access to skilful labour, market information and working capital. Conversely, the less well-endowed exporters tend to rely on arms length business ties often characterized by deceit and opportunistic tendencies and least suitable for securing resources and meeting market demands.

How is Subcontracting related to Network?

There is some confusion in the literature as to whether or not subcontracting arrangements and networks are related. Knorringa (1996) points out that both subcontracting and networks are collaborative arrangements constituting intermediate arrangements between markets and hierarchy. The differentiating factor is the amount of trust, derived either through inter-personal ties or formal institutional arrangements (generalized trust) that prevails in the particular production relations. Subcontracting arrangements may range from hostile bargaining based on distrust to more collaborative and intensive relations (Knorringa, 1996). In much the same way network relations can “degenerate” to fluid and distrustful relations. The Japanese example of relational contracting of “moralized trading relationships of mutual goodwill” (Dore, 1983, p463) is often cited as typical example of subcontracting arrangements overlapping with network relations. In the end:

subcontracting and network relations may be rather similar in that they are hybrids between market and hierarchy, most network relations

significantly differ from the average subcontracting relation in that they contain a more significant degree of ...trust...in some situations subcontracting relations may evolve into network relations (Knorringa, 1996, p64).

Subcontracting arrangements according to Knorringa (1996) occupy a substantial space between the market-hierarchy continuums and assume many faces. Mead (1984), for instance, identified three forms of subcontracting arrangements, which he claimed are prevalent in many developing countries and shed light on how small firms resolve contractual difficulties emanating, for instance, from opportunism and its varying implications on the growth of small firms. The first subcontracting arrangement identified by Mead is characterized by unequal market power relations between independent producers and few dominant leading enterprises. The buyer in this relationship can easily switch to a variety of suppliers and can undercut any potential market strength of the subcontractors, especially when the activities of the subcontractors seek to threaten their market position. Producers are restricted to simple activities based on the utilization of unskilled labour and the use of simple tools. This “traditional” subcontracting arrangement, which is cost-reducing and based on lower input prices, can provide modest levels of incomes to large numbers of individual subcontractors or producers, but is least suitable in terms of the potential for enabling the subcontractors to achieve a long-term growth—there is limited flow of information and technical skills for developing new products and improving production process. The logic of such an arrangement though is often to help principal firms to reduce supervision costs and spread risks (Nadvi and Schmitz, 1994), yet supervision costs and risks may be high in deploying this subcontracting arrangement in an environment of pervasive opportunistic behaviour. It

will be shown later in the discussion how the “putting-out” system which is synonymous to this first stage subcontracting arrangement (Lazerson, 1990), was rendered ineffectual by pervasive market imperfections and gave way to the development of a relatively robust production arrangement i.e. the inside contracting system.

Mead (1984) characterizes the second subcontracting arrangement as a competitive relationship comprising many buyers and suppliers in which the producers use machinery of some reasonable sophistication compared with the first arrangement. The multiple buyers and suppliers in this arrangement shift the subcontracting arrangement from unequal market power relations to a competitive situation, representing a much better pattern for growth.

The third subcontracting arrangement involves a reliance on market arrangements as well as non-market links to resolve risks inherent in the transaction environment. In this arrangement, the leading firms may support the subcontractors or the producers by providing them with raw materials, finance and training to bolster the capacity of the producers. According to Mead, the principal entrepreneurs adopt this to overcome their own lack of supervision capability as well as technical skills. It is based on more collaborative inter-firm relations entailing substantial sharing of skills and information, and a lot of learning takes place—the potential for growth in this arrangement is relatively large. The actors in this arrangement utilize personalized networks to resolve the “market-or-hierarchy” problem. This contracting type uses social sanctions to pressurize suppliers to eschew opportunistic behaviour. Dore (1983) observed that

transaction costs for Japanese firms are lower because opportunism is less a problem and there is the prevalence and explicit promotion of personalized trade arrangements. Subcontracting arrangements in this sense become *relational arrangements* when they are built on trust and entail qualitative flow of information and enforcement achieved through effective informal sanctions. To revisit the observation earlier about the complementarities between formal and informal institutions in facilitating market exchange it is important to recognize that relational contracting could be strengthened with formal institutional tools. The prevalence of relational contracting in Japan as indicated earlier has much to do with greater amount of goodwill that existed in the Japanese society. Dore, however, observed that even in this society where there is a high degree of interpersonal trust, there is no immunity to market abuse and therefore formal contracts are used to minimize market abuse. He cited the example of the official encouragement of the use of written in addition to oral contracts in business transactions, which aims at “strengthening moral constraints on ...the abuse of market power” (p465). He characterized this arrangement as the “... formal institutionalization of the ethics of relational contracting” (p466). In this instance formal contract is deployed in addition to relational contracting, instead of replacing it, in constraining market abuse.

In other words, the elements of formal institutional mechanisms, intangible assets such as trust and other social control mechanisms are instrumental in facilitating trade specialization between principal enterprises and their external partners (North, 1991). Excessive opportunism could be counter-productive to the building of personalized trust and transactions are more likely to be costly to monitor when formal enforcement

institutions are weak and the complexity of trade relatively high (North, 1990). The typical arm's length subcontracting, in this circumstance may be untenable or insufficient as a source of innovation/ resources and transaction cost reducing strategy. Inter-personal trust, effective informal monitoring/enforcement and strong formal institutions are important requisites for enabling external subcontracting to thrive. On the other hand, weak institutional environments characterized by lack of trust and unresponsive third party service provision or enforcement bodies are inimical to successful external subcontracting arrangements. In line with this reasoning, Mead (1984, p1099) observed that:

“...the more prevalent are imperfections in the market, the more difficult it would be to introduce subcontracting arrangements into a production chain...one might add to this list one characteristic of many developing countries: a complex and antiquated legal system, with cumbersome and time-consuming court procedures, making it particularly difficult to enforce contracts or to penalize those who break them. All of these characteristics suggest that ‘parent’ firms might have substantial problems... enforcing contracts with independent producers whereby the latter would undertake certain activities on their behalf”

A more robust production arrangement would therefore be required to address the complexities of production i.e. quality concerns and risks associated with pervasive deceit.

Entrepreneurs seeking to overcome these challenges and grow their firms may employ a production path that emphasizes the advantage of balancing the flexibility advantages often associated with external subcontracting with the need to increase supervision to reduce opportunism and gain control over production in order to meet quality and timelines requirements (Nadvi and Schmitz, 1994). The choice of a typical vertical integration as prescribed by Williamson may also be less preferable for it has many

caveats. Typical in-house production is rigid and least responsive to meeting different types of production orders and idiosyncratic market needs because most often in-house production is limited to few or a single client (Lazerson, 1990). Tastes and preferences of consumers change rapidly and these place enormous challenges on vertically-integrated firms to adapt to such changes, unless such in-house producers have developed multi-purpose capacity and versatile workforce to adapt to those changes, which in itself could be regarded as flexible. Traditionally, centralized factory production is associated with building buffer stocks of semi-finished products as a way of fully utilizing the labour force but this has its own cost implications because capital may be locked up in the stock (Lazerson, 1990).

In the face of these concerns, lead entrepreneurs seeking to minimize agency problems, increase control over production process, meet domestic production challenges and simultaneously adapt flexibly to changes in demand may adopt the organizational path of inside contracting that seems to enable the entrepreneurs to address these concerns. Insights from the industrial history literature are relied on for our analysis of inside contracting. Its development is traced to the putting-out system.

2.4.2 From Putting-Out to Inside-Contracting

The origin of subcontracting, according to Lazerson (1990) is traced back to the putting-out system that was a dominant mode of organizing production until the late eighteenth century in the industrialized countries. It shares a lot in common with today's subcontracting arrangement. The basic characteristic of the putting-out system is that it is

a home-based production system, which is coordinated by a principal entrepreneur or merchant-coordinator. The principal entrepreneur provides raw materials and finance to the individual producer who performs one of the stages of the production process at his or her workshop using his/her own tools (Landes, 1966, Williamson, 1980, Dietrich, 1994). The principal merchants then collect the semi-finished or the finished product and market them as their own. The basic contribution to production by the entrepreneur apart from marketing was to establish design standards and technical requirements (Lazerson, 1990).

Landes (1966, p 12) describes the putting-out system as follows:

...the merchant-manufacturer “put out” raw materials...to dispersed cottage labour, to be worked up into finished or semi-finished products. Sometimes the household was responsible for more than one step in the production process...but the system was also compatible with the most refined division of labour...the manufacturing process was broken down into as many as a dozen stages on the path to industrial capitalism. For one thing it brought industrial organization closer to modern division between employers who own the capital and workers who sell their labour. To be sure most domestic [workers owned their tools]. They were not, however, independent entrepreneurs selling their products in the open market; rather they were hirelings, generally tied to a particular employer, to whom they agreed to furnish a given amount of work at a price stipulated in advance.

The putting-out system is considered as marking a significant transitional phase of industrial production for the reason that it pulls large numbers of rural folks into exchange relationships (Lazerson, 1990). Characteristically, the workers of the putting-out system are left unsupervised, they set their hours of work and payment connected to output. According to Williamson (1980), each producer maintains a considerable contractual independence in their relationship with the central entrepreneur and makes distinct profit margins based on the agreed contract terms. This does not suggest that the decision-making process is on equal terms. Whether or not the relationship would be

hierarchical relates to the bargaining strength of the producer vis-à-vis the principal entrepreneur, which in turn is dependent on the extent to which the partners have acquired trade-specific skills and knowledge, and the ownership of particular assets (Williamson, 1980).

The importance of the putting-out system is suggested to have been diminished by the late nineteenth century and succeeded by factory setting production arrangements. The explanation for this shift is partly given as the weakness in the traditional putting-out arrangement whereby central entrepreneurs could not directly control the individual producers. As indicated earlier on, the producers enjoyed enormous independence under the putting-out system. They controlled production in their dispersed workshops, determined how much and when to work; all proved as obstacles to production supervision (Lazerson, 1990). It was not only the output that was difficult to control but also the behaviour of the home-based producers (Dietrich, 1994). Landes (1969, p59) captured the difficulty the central entrepreneurs encountered in controlling the home-based producers this way:

[The entrepreneur] had no way of compelling his workers to do a given number of hours of labour; the domestic weaver or craftsman was a master of his time, starting and stopping when he desired and while the employer could raise the piece rate with a view to encouraging diligence, he usually found that this actually reduced output.

The difficulties of supervision consequently, first, led to poor and uneven quality production and delays. Second, the lack of supervision is also observed to have led to embezzlement of the resources provided by the merchants and from the perspectives of transaction costs theory, this undermined the putting out production arrangement. Third,

it is observed that the lack of work discipline on the part of the putting-out producers was linked to subsistence farming where planting and harvesting were given priority over industrial production (Sewell, 1967 in Lazerson, 1990).

Theft, supervision difficulties, poor product quality, delayed deliveries and insufficient output made the loose putting out system less popular. These factors to a large extent rendered the putting out arrangements less suitable mode of production towards the late nineteenth century but the question is, has the putting-out system in the face of these deficiencies lost its relevance as a mode of organizing production in the contemporary era? Lazerson (1990), offers a contrary view, arguing that the putting-out system was incorporated into factory production, particularly for labour intensive activities. The putting-out system remains a significant form of production in both developed and developing countries often interpreted in the form of modern subcontracting arrangement. The underlying principles of both putting-out systems and modern day loose subcontracting are similar. Subcontractors and putting-out producers have no direct outlet to the market, produce on order for a leading entrepreneur and are formally independent (Lazerson, 1990). “Putting-out” and “subcontracting” are used interchangeably in this study. The difficulties of controlling independent subcontractors undermine the efficacy of subcontracting to reduce transaction costs and meet contractual obligations. The inside-contracting system was devised by the entrepreneur-coordinator to overcome the problems of poor product quality, labour supervision and avoid delays.

2.4.3 Inside-Contracting System: Controlling the Production Process to Mitigate Market Imperfections

The putting-out system was succeeded by a factory system in the nineteenth century called the “inside contracting system”. Inside contracting is regarded as a “refined version” or “a natural development from the putting-out system as it existed in Great Britain” (Buttrick 1952, p206). Buttrick (ibid, pp205-206) described the inside contracting system as follows:

Under the system of inside contracting, the [owner] of a firm provided floor space and machinery, supplied raw material and working capital, and arranged for the sale of the finished product. The gap between raw material and finished product, however, was filled not by paid employees arranged in [a] descending hierarchy...but by [inside] contractors, to whom the production job was delegated. They hired their own employees, supervised the work process, and received a [negotiated] piece rate from the company.

The relationship between the inside contractors (master craftspeople) and the enterprise owners was contractual and the contractors worked as semi-independent producers (Englander, 1987). The enterprise owner negotiated a piece rate with the contractor for components that were produced. The contractor hired, fired and set the wages of their own workers but production took place inside the owners’ factories instead of the contractors’ workshops. The advantages of inside contracting were that, first, it freed the owners, even though they owned the plant, from some of the technical problems (i.e. craftsmanship skills) associated with production and labour supervision (Buttrick, 1952). The inside contracting system, from an evolutionary perspective, is a development that offered the entrepreneur a “transitory” solution to the problem of how to organize

production in the emerging factory (Dietrich, 1994). The second is that the system afforded the owners the opportunity to exercise some level of control over production information and operations, which were outside their immediate control (Englander, 1987). The supervision of the workforce, however, was indirectly exercised through the master craftsmen. As the scale of production increased, the entrepreneurs who seemingly did not have the requisite supervisory skills or the ability necessary to organize production had to subcontract the responsibility of labour supervision to agents within the firm (Englander, 1987; Dietrich, 1994). Accordingly, the entrepreneurs of the inside contracting system had to:

carve [their] work force up into units small enough so that the accustomed form of labour control could be maintained through the agency of contractors, craftsmen, and foremen...the unifying thread was the decentralization of labour supervision [inside] the enterprise. The conclusion to be drawn seems clear: whatever the imperatives in the direction of ...production, on specific matter of managing workers, the nineteenth century manufacturer conceded the superiority of the close, personal supervision that characterized small-scale enterprise (Brody, 1980 cited in Englander, 1987, p433).

The inside contracting system also presented some advantages to the master craftsmen and their workers. The system enabled the master craftsmen to maintain their autonomy within the changing market environment. They wielded the craft skills, hired and supervised the work force and yet spared the problem of finance and salesmanship (Buttrick, 1952; Englander, 1987). The incomes of the master contractors were the difference between the negotiated price with the factory owners and the piece rate they paid to the workforce under them. The inside contract system provided the new artisans with the opportunity to acquire skills under the tutelage of a master and the masters kept

those workers who demonstrated ability to perform. In turn, the workers were assured of reasonably steady job inside the factory building (Englander, 1987).

The emergence of the inside contracting system was a rational response to market imperfections (high transaction costs), which the putting out system with its inherent laxity of control was least able to address (Englander, 1987). Besides, other circumstances played a part in the change process. Buttrick (1952) observed that as demand increased, the use of “interchangeable principle” technology suitable for achieving production of standardized products in large volumes also emerged. There was also the existence of a body of a workforce that was used to the concept of producing on contract. These factors propelled the development of the inside contracting system:

The increased demand for fabricated metal products accompanying...the Civil War made it increasingly difficult to fill orders without additional capital and labour. These the toolmaker [the early toolmaker and armorer of New England had small work shops where guns and implements were made on order for people in the neighbourhood] could not supply himself. If to this situation are added two other factors, we will have a picture of the setting from which the contract system developed. The first of these was the increasing use of the principle of interchangeable parts; the second was the existence throughout the nineteenth century of inside contractors within the government arsenals...given the increased in demand and the cost advantages of ...making use of interchangeable principle, inside contracting developed into an important and widely used system (Buttrick, 1952, p206-207)

As the firm evolves from the home-based production situation as it is the case of the putting-out system to a factory environment, the entrepreneur will begin to be confronted with increasing overhead cost as he embarks on detailed supervision to minimize

cheating. However, transaction costs savings that are achieved through production inside the firm will be evident with quality control economies (Dietrich, 1994).

The relevance of the inside contracting system began to diminish at the beginning of the twentieth century. As the owners adopted more formalized internal control and recruitment systems, the nature of the firm began to take on a hierarchical character moving towards what Williamson described as the vertically integrated firm. The basic principle of inside-contracting as a rational response to addressing quality control concerns, labour supervision difficulties/opportunism, and in dealing with the complex changes in the physical characteristics of the traded products makes it relevant to this study. The inside contracting as adopted in this study is viewed as an extension of the subcontracting arrangement, which is more hierarchical but less so than the vertically integrated firm. Though its development is a dynamic process in response to addressing some of the weaknesses of the rudimentary putting-out system, the putting-out subcontracting arrangement, however, serves as the bedrock for the development of the inside contracting system and is not a complete breakaway. Inside contracting economizes on transaction costs within the context of uncertain environment, through indirect supervision in-house. It effectively addresses complexity of production better than the largely market-oriented subcontracting arrangement under risky production environment, even though from the perspective of industrial organization it is a transitional arrangement and less stable compared with vertically integrated firms.

In one view, the external subcontracting relationship can evolve into inside-contracting and in another it could be considered as alternative production forms used by entrepreneur-coordinators. These production arrangements viewed as alternatives have relative robustness in dealing with transactions costs and risk as well as the extent to which they enable the availability of resources to the participating enterprises for success. In effect these alternative production strategies would have differing outcomes on the success of small enterprises in an uncertain and weak institutional environment. The basic idea that is being expressed here is that the success of small leading firms in the market may be linked to the relationships they establish with external trading partners (Lorenzoni and Ornati, 1988; Lazerson, 1988).

The analysis in this section sought to conceptualize the different modes of organizing production within the context of the buy-and-make hypothesis. The production arrangement, depending on where it is located in the market and hierarchy continuum, could lean either towards market exchanges or hierarchical arrangements. Nevertheless, the organizational choices made by principal entrepreneurs, in reality, are far more complex than the simple dichotomy between market and hierarchy or between subcontracting and inside-contracting. Instead, lead entrepreneurs choose a complex mix of institutional arrangements to encompass *buy, make and collaborate* in their relations with other partners in responding to their environment (Knorrinda, 1996). In agreement with this position, Lazerson (1988, p340) had this to say:

Even more incongruous with the dichotomous vision of hierarchies and markets was the fact that, within a single firm, movements towards

hierarchy and away from markets in one area were often counter-balanced by a greater dependence on markets in other areas.

Knorringa (1996) has stylized these arguments into what he calls transaction regimes. He defined transaction regimes (Fig.1) as a set of common characteristics of exchange of transactions that take place in a specific institutional context. At the extremes of the transaction cost framework are the “buy” and “make” regimes. The intervening transaction regimes between the “buy and make” poles of the continuum included subcontracting regime, network regime, industrial district regime and clan regime. Knorringa used this framework to analyze the Agra footwear cluster in India. What is conspicuously missing in these transaction regimes is the system of inside contracting. The industrial cluster (spatial agglomeration) and clan regimes are not given consideration in this study because they do not provide direct theoretical explanation to the empirical evidence. Knorringa indicates that these labels are meant to invoke mental images for analytical clarity regarding the different production arrangements that may be employed by entrepreneurs in response to their environment. A major theme discernible from the above discourse is that given the context of the institutional environment, different organizational strategies may yield different outcomes in terms of their influence on enterprise success and growth. However, this should not prevent us from recognizing the complex reality whereby a production arrangement may evolve from one regime to another or a single firm may deploy more than a single transaction regime in response to peculiar circumstances. This theoretical framework guides our analysis of how Ghanaian craft exporters organize production activities given the existing institutional and socioeconomic contexts in which they operate.

Figure 1 represents the various transaction regimes designed by Knorringa. The auction regime symbolizes spot transaction entailing intense price haggling among anonymous actors and assumed to be effective under conditions of perfect information and homogenous products whose quality can easily be verified. The subcontracting regime is a relationship in which a lead actor places an order with a subcontractor to produce all or part of the order to which the leading entrepreneur takes and markets as his own. It may involve a written or oral contract in which the lead firm sets out the precise specifications of the order in advance. The subcontracting regime could overlap with the auction regime and takes on the form of market-based relation. Similarly it could intersect with the “direct control” regime leading to hierarchical or “locked-in” subcontracting relations. The direct control regime on the other extreme on the transaction costs framework is a hierarchical arrangement within the firm in which the lead entrepreneur enforces compliance through direct controls and operational routines. The network regime carries the notion of close collaboration and trust building relationships between the trading partners. Like, the subcontracting regime the network regime is conceptualized as occupying the space between buy (market) and hierarchy (direct control) regimes. Subcontracting relations may develop from a hostile bargaining based on distrust to a more durable trust based relations thus overlapping with network regime.

Leading Actors' Choices and Transaction Regimes

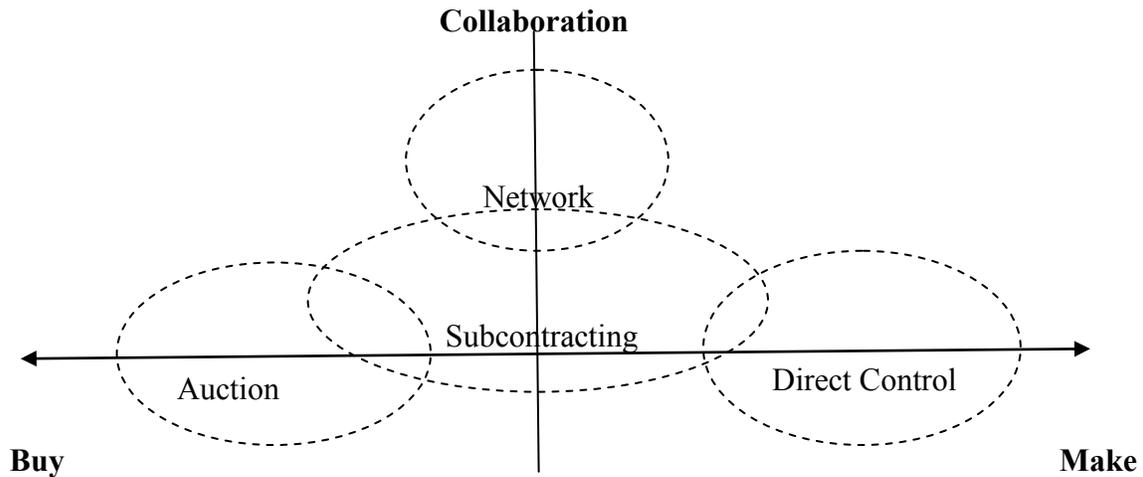


Fig. 1(Adapted from Knorringa, 1996)

2.5 The Global Value Chain Concept and International Trade

This study is also about how international market forces shape the production activities of the small-scale Ghanaian craft exporters locally. It is therefore important to seek a framework that enables us to understand the organization of production activities across both firm and transnational boundaries and in particular how the organization of industrial activities is driven by international market demands and pressures. Gereffi et al. (2005) have attempted to capture the organization of industrial activities across firm and geographical boundaries using the global value chain concept. The contemporary global economy, according to Gereffi et al. (ibid), is marked by two main processes. First, Western corporations have been restructuring their operations in order to concentrate on their core competencies such as marketing, product strategy, and high value-added segments of manufacturing and in the process farm out non-core activities to suppliers in

developing countries. This has extended the organization of industrial production across national boundaries. Second, this process is believed to lead to the upgrading of supply capabilities of firms in developing countries participating in global production chains.

The global value chain concept is concerned with how global production and distribution systems are organized, involving recurrent transactions between various firms, across geographical boundaries (Humphrey and Schmitz, 2002). Organizing industrial production on a global scale involves independent economic agents such as traders, export agents and global lead buyers who *link* supply to final consumption. To ensure that that the discrete roles of these agents are smoothly linked together as a unit presents enormous coordination challenges; agency problems may be high. This requires an institutional mechanism for aligning the interests of the different trading agents and actors for smooth flow of goods and services along the chain.

Governance of global production networks is used to express the control that is exercised by some economic agents along the chain to ensure that all the discrete activities in the production network are neatly meshed together (Humphrey and Schmitz, 2001). Gereffi (1994) made reference to “a governance structure” (i.e. authority and power relationships that determine how financial, material, and human resources are allocated and flow along the chain) as central to the coordination of transnational production arrangements. Gereffi (ibid.) in his original conceptualization of transnational industrial organization made a distinction between producer-driven and buyer-driven chains. The bases of the distinction

between the buyer and producer driven chains are located in their key barriers to entry (Gereffi et al. 1994). The producer driven chains are largely controlled by multinational corporations and they are typical of capital and technology intensive industries such as the automobile and aircraft industries. Barriers to entry in such chains are located in the heavy investments that are required to build large-scale, high-technology production facilities (Gereffi et al. 1994, Gibbon and Ponte, 2005).

Buyer-driven chains refer to those industries in which global retailers, brand-named merchandisers and trading companies play a central role in coordinating the activities in the production networks. The buyer-driven chains are common in labour-intensive industries such as garments, footwear, toys, house wares and hand-crafted items (Gereffi, 1994). The lead actors exercise control along the chain through the specification of what type of product needs to be supplied, in what quantity, when, and at what price (Humphrey and Schmitz, 2001). Global buyers who are usually the lead actors in the global value chains attain their powerful positions by specializing in high-value added functions such as marketing, branding and product development; activities in which entry barriers are high (Kaplinsky, 2000). Humphrey and Schmitz (2001) note that chain governance is important for market access, the acquisition of production capabilities by suppliers and the distribution of gains along the chain. They maintain that even if trade quota and tariff barriers are removed, access to Western markets would not be automatic because the chains into which developing countries' producers feed are often controlled by a limited number of buyers. Gaining access to the lead firms or buyers in the chain is an important precondition for exporting into Western markets. The decisions of the lead

global firms regarding quality, price and delivery timelines may lead to particular producers and traders losing out in global trade, especially, small producers who lack the capacity to meet buyers' demands. Producers that gain access to the lead buyers tend to face new pressures as well as new opportunities for improving their production activities. The lead firms make exacting demands for cost reduction, higher quality and speed. They may at the same time transmit information about best practices to their suppliers and provide hands-on support and pressure on how to improve production processes. Humphrey and Schmitz (*ibid.*) also note the centrality of chain governance to the distribution of gains along the chain. Actors who govern the chain by virtue of specializing in functions that are characterized by high entry barriers command high returns whereas producers undertaking activities with low entry barriers often reap low returns. The exercise of control along the global chain is considered to be the source of the appropriation of the chain's value, marginalization and the sharing of risk burden (Gibbon and Ponte, 2005). This raises the development question of how the gains that accrue to global value chains can be distributed fairly along the chain, since the powerful actors tend to appropriate a greater share of the gains (Humphrey and Schmitz, 2001) or how such gains can be captured by weaker producers. This question is largely beyond the scope of this study.

Sturgeon (2008) added to the value chain governance debate by drawing attention to the loci of power at different levels of the global value chains instead of the prime focus on the singular dominance of global lead buyers in driving global value chains. He indicated that suppliers could wield competence power when their products and services are seen as

nearly indispensable for the lead firm. He, however, added that by virtue of the enormous market power that they possess, lead firms can undercut supplier power by switching suppliers. This study is particularly concerned with the exercise of power or the lack of it by the chain actors (both local and international) in ensuring the smooth flow of inputs and outputs and the integrity of the production chains. Again, instead of international buyers who are the prime focus of most global value chain studies, this study focuses on the domestic actors (i.e. exporters/producers) who coordinate and control production activities at the supply end of the export commodity chains. The study is, however, not oblivious to the influence and pressures international buyers exert on local production for export as well as the economic risks the local exporters have to bear for participating in the buyers' value chains.

Gereffi et al. (2005) have constructed five governance structures of global value chains based on:

- The complexity of information and knowledge transfer required to sustain a particular transaction, particularly, with respect to product and process specifications;
- The extent to which information and knowledge can be codified and, therefore, transmitted efficiently and without transaction-specific investment between the parties to the transaction;
- The capabilities of actual and potential suppliers in relation to the requirements of the transaction.

The patterns of value chain governance described by Gereffi et al. (ibid.) include the following:

Markets: buyers respond to specifications and prices set by sellers and because the complexity of information is relatively low, transactions can be governed with little

explicit coordination. The products types involve in these transactions are relatively simple and asset specificity may fail to accumulate.

Modular value chains: the ability to codify complex product specifications may give rise to modular chains. This chain, which is based on codified knowledge, has many of the benefits of arms-length market linkages i.e. speed, flexibility, and access to low cost inputs. It differs from market linkages in that there is information flow, albeit in a codified form; across inter-firm links. Because of codification, complex information can be exchanged with little explicit coordination.

Relational value chain: According to Gereffi et al. (ibid.), relational value chains emerge when product specifications cannot be codified, transactions are complex and supplier capabilities are high. In this case, information about product specification (i.e. tacit information) is exchanged through frequent face-to-face interactions and governed by high level of explicit coordination. The mutual dependence that emerges from the trade interaction may be regulated through reputation, social and spatial proximity, family and ethnic ties (see also the discussion of the role of informal institutions in facilitating mutual market exchanges in section 2.3.3). The relational value chain is particularly important for this study because of its emphasizes on the importance of the capability of the supply-base as a precondition for gaining access to transnational trade networks, the regulatory and resource provisioning roles of ethnic-based and process-based trusts. The dynamic dimension of trust in facilitating inter-firm trade relations to enhance competitiveness of small firms in transnational trade is discussed in section 2.4.1.

Captive value chains: when the ability to codify and the complexity of product specifications are both high but supplier capabilities are low, then value chain governance assumes the captive type. This may occur because of low supplier competence in the face of complex products and specifications, which requires a great deal of intervention and control on the part of the lead firms. The lead firms seek to lock-in their suppliers to prevent others from reaping the benefit of their effort. Opportunism is controlled in a captive chain through the dominance of lead firms, while at the same time resources are made available to subordinate firms to make exit an unattractive option.

Hierarchy: when product specifications cannot be codified, products are complex and competent suppliers cannot be found, lead firms will then seek to develop and manufacture products in-house. This governance type is motivated by the need to effectively manage inputs and output flows and to control resources, especially intellectual property rights.

Gereffi et al. (2005) view modular, relational and captive value chains governance as extensions of a network approach to industrial organization across national boundaries, forming intermediate arrangements between market governance and hierarchy.

As small African firms seek to enter the export market, they do not only have to contend with local factors, but they also have to confront export market forces and buyer demands that call for organizational adjustments. There are barriers to participation in global value chains. The export markets to which African labour-intensive enterprises desire access

are the very markets that are highly controlled by buyers and access to these markets is contingent on buyer-specific standards, product specifications, speed, and volume. The extent to which African exporters are able to meet or adapt to these requirements may either lead to participation or exclusion from the export market. These issues present unique challenges to many small African enterprises, which very often do not have access to the relevant market information needed or just do not have the capacity to meet these requirements. Gibbon and Ponte (2005) characterize Africa's participation in international trade as *trading down*, which they regard as the shorthand for the processes underpinning Africa's experience of trade disintegration into the Western economies. The process of exclusion is in part attributed to the failure of:

African Firms to meet *new* expectations concerning quality, lead times, volumes, and prices, and their failure in actively shaping new standards to their advantage—including ones related social and environmental concerns raised by Northern NGOs. In some cases, exclusion ... [has] even occurred as a result of the failure of Africa's farms and firms to continue meeting traditional expectations in relation to these dimensions, as the provision of public goods like quality control has collapsed (p202).

These challenges, however, are not unique to small firms in Africa. Developing economies are regarded as latecomers in the global economy and are “dislocated from the mainstream international markets [they] wish...to supply (Hobday, 1995, p34 in Humphrey and Schmitz, 2001). Keesing and Lall (1992) aptly recognized this problem and argued that new suppliers from developing countries are expected to meet requirements that frequently do not (yet) apply to their domestic markets. This creates a gap between the capabilities required for the domestic market and those required for the export market. The role of international buyers, as exemplified in the global value chain discourse, has been central in helping some developing countries to bridge the gap

between their local capacity and export market requirements. This process is very evident in many Asian as well as Southern American countries, where buyers have been instrumental in enabling small enterprises to overcome some of their capability challenges, upgrade their production process and products, and integrate into the Western market. Except in some few cases, and mostly in the area of agricultural products (Dolan and Humphrey, 2002; Gibbon and Ponte, 2005), African firms have not been able to establish strong and performance enhancing collaborative relationships with foreign buyers in manufactured products. In a study of three African countries, including Ghana, Kenya and Zimbabwe, Biggs et al. (1995) observed that the interaction between indigenous African firms and foreign buyers is generally weak, though there is limited evidence of instances whereby foreign buyers have assisted local enterprises to upgrade their product quality, become more cost competitive and reduced production turnaround times. The risky African business environment and imperfect enforcement systems are argued to discourage the building of strong relationships with foreign buyers. Thus small firms on the continent miss out on the advantage of the transfer of skills, technical know-how and market information that could be derived from establishing strong business ties with international buyers (Fafchamps, 1996, 2004; Pedersen and McCormick, 1999).

Buyers are usually concerned with whether or not their trading partners possess some minimal technical, organizational capacity and export experience required to meet contractual obligations. Levy et al. (1999) observed in a study of Jeparan carved furniture in Indonesia that foreign buyers were more willing to establish a strong and sustainable relationship with firms with a proven record of success in the export market than new

entrants into the export markets. The implicit understanding here is that the length of experience in the export market and demonstration of a reasonable capacity level to deliver on contract terms are important requisitions for building strong and direct producer-foreign buyer linkages. This is what Sako (1997) refers to as competence trust, which touches on the issue of whether or not parties to a transaction are capable of doing what they say they would do. The lack of competence trust may in part explain the non-existent or the lack of depth of the relations small African firms establish with foreign buyers in export manufacturers.

Traders have been identified as important economic agents who could help fill an important link between local producers and foreign buyers (Knorringa, 1999; Nadvi and Schmitz, 1994). Traders and trade intermediaries are often conscious of information regarding market intelligence whereas producers may possess production knowledge, and so bridging this functional divide between these agents and producers could be an important source of market information for growth (Nadvi and Schmitz, 1994).

The story is told especially in the Asian countries about the difficulty of nascent exporters and foreign buyers working together in the early years who were able to overcome this institutional gap through the mediating role played by export agencies and other trading agents (Levy et al. 1999; Weijland, 1992). Despite the claim of the instrumental role played by export agents and traders in other developing countries in helping small firms to succeed in the export market, our knowledge of the role of traders in industrial development in Sub-Saharan Africa is underdeveloped (Akoten and Otsuka, 2007).

Recent studies report the emergence of a myriad private trade intermediaries on the African business landscape—though the evidence still remains sketchy—whose functions enable local firms to transcend barriers to exchange and build trade links with distant buyers (Fafchamps 1996, 2004). In the same vein Jackson (2002) reported that the market facilitation and trade promotion functions performed by public and quasi-government agencies in Ghana and Zimbabwe enabled small and medium firms to overcome information and capacity difficulties. One theme that emerged from Jackson’s study was that these agencies face many administrative, organizational and financial constraints internally, which restrict their ability to meet the end of providing trade facilitation and promotion services. This present study in particular reports on the role of private intermediary agents that feed into the production chains of small-scale exporters that are being studied.

The export agents and trade intermediaries are like any other private economic agents operating within the same domestic economic and institutional environments. The effectiveness of the role of trade intermediaries, whether in the area of contract enforcement or in the provision of market information and other trade services, may also be constrained by market failures. They are agents who seek to maximize their self-interest and so would be reluctant to invest and continue to provide trade intermediation services for greater success if there were very few economic incentives to do so.

2.6 African Informal Economy and Institutional Analysis

Can we talk of African markets and how do African institutions shape markets? Can we apply the tenets of new institutionalism to the analysis of African markets that are largely

informal in nature? Pro-African institutionalists and economists have attempted to chart the uncharted waters by way of situating the analysis of African markets in the new institutional economics thinking. The current understanding in the literature emphasizes the point that African markets are like any other markets everywhere. However, the institutions that support various markets may differ according to different surroundings and the ways in which they are embedded. The coordination of market activities by African firms is embedded in local institutional and environmental settings, which to a greater extent influence their success as market participants. Fafchamps (2001) identifies three modes of allocating resources in Sub-Saharan Africa: gift exchanges, markets and hierarchies. Among the three, he claims, gift exchange is more prevalent, but hierarchies in the form of large vertically integrated corporations are less prevalent than markets in Africa. Arguably, he indicated that markets are important in Africa than in the West because there are few hierarchies in Africa (except few large multinational corporations) and the few that exist are in themselves weak. He draws attention to the small scale transactions and large numbers of small intermediary firms that dominate market transactions in Africa compared with the West where market transactions are coordinated within large corporations, the size of transactions is large and the production chain dominated by few intermediaries. Despite the fact that markets are a commonplace in Africa, they are imperfect—“the truth is that market activity in Africa is not without form: it is only without economic formalization” (Fafchamps, 1997, p733).

Most economic activities in SSA are argued to take place in the informal realm and beyond state’s regulation. It is suggested that the informal economy employs more people (outside the agricultural sector) than the official economy in Africa (Meagher, 2010). It is

also estimated that about seventy per cent of the non-agricultural labour force earn their livelihoods informally and that this accounts for about forty percent of Gross National Product in Africa (Meagher, *ibid*). An informal economy and informalization are not uniquely African phenomena: they are global in nature. The African version of informal enterprises and informalization, however, represent “an extreme in a wider global trajectory of rapid informalization” (*ibid*, p 14). In view of this, a discussion of markets in SSA would be inadequate without a consideration of the concept of informality.

Keith Hart (1973) is credited with inventing the term “informal sector” as distinguished from the formal economy. Hart (*ibid.*) demonstrated in his study the ingenuity and the entrepreneurial spirit of the urban poor who had no access to formal work in a suburban area of Accra. Hart’s study departed from the earlier marginalistic view (famous between the 1950s and 1960s) which considered the informal economy as residual, backward, traditional, unproductive and populated by a marginal mass of “excess reserve army”(see discussion in Portes and Shauffler, 1993). Hart’s version of informality celebrates the potential of the informal economy for independent employment creation and growth (Meagher, 1995). Like Hart (2006), De Soto (1989) subscribes to the entrepreneurial dynamism of the informal economy but urges the deregulation of the state to allow the spirit of entrepreneurship among the working people to flourish. De Soto (2000) has, however, modified his position and advocated for another form of regulation through the legalization (formalization) of informally-held assets of the poor and informal workers in order to improve their livelihoods.

Informality is widely defined as “income generating activities that take place outside the regulatory framework of the state” (Castells and Portes 1989, p12). Maintaining the notion that the unofficial and official sectors of the economy are dichotomous pair is considered problematic because it tends to obscure the complex relationships, and the blurred boundaries, between the two. Instead of the notion of economic dualism, the Marxist structuralists such as Portes and Schauflier (1993) place emphasis on a unified systems encompassing a dense network of relationships between formal and informal enterprises and allowing for a role for the state in the expansion of the informal sector (Meagher, 1995). According Meagher (2010), it is difficult, if not impossible, and perhaps a fruitless classificatory exercise, to try to decipher the boundaries between the official and unofficial spheres of economic activities whether one is observing global commodity chains or trade in conflict diamonds since “goods originating in unregulated ... contexts are integrated into formal sector production and distribution systems (ibid, p14). Chen (2006) equally emphasized the complexity and sheer numbers of formal-informal linkages and stressed the importance of the allocation of authority and economic risks embedded in these linkages. Informal enterprises may produce goods and services existing within *value chains* where the terms and conditions in the chains are determined by a lead firm, either a lead national firm in domestic chains or international lead firms in global value chains (see the earlier discussion on the role of global buyers in the governance of global value in section 2.5). The major suppliers who receive orders from lead firms in the value chain can also determine the terms and conditions of orders for products they subcontract to informal workers down the chain. “These commercial relationships are not likely to be regulated [formally]” (ibid, p85).

The current discourse on the concept of informality shifts the debate from the dualistic perspectives to a focus on regulatory and organizational roles of social networks to economic exchanges within the informal economy. Meagher (2010) argues that what matters most to the analysis of African informal economies are the unique organizational mechanisms and authority relations that characterize informal forms of economic order instead of the primary focus on the dichotomy between formal and informal economic activities. Hart (2006, p33) also recognizes the inadequacy of the analytical value of the dual informality concept and suggests the need to explore the...“social forms [that] have emerged to organize the informal economy and to examine the institutional particulars sustaining whatever takes place beyond the law”. According to Meagher (2010, p16), “social networks have moved centre stage in the analysis of unofficial forms of economic organization, emerging as a means of investigating the informal economy”. Framed by the rubric of new institutional economics, a case is made for the ability of social networks to provide effective and cheaper bases for economic development outside the framework of the state. The regulatory and organizational roles of social networks are seen in the areas of reducing opportunism through identity ties, reputation and group sanctions (see section 2.3.3 detailed discussion of this) and by enabling access to new sources of information and resources (see also the discussion of the role of earned trust in facilitating access to resources in section 2.4.1). According to Meagher (2010, p26) “an institutional approach to network analysis offers new tools for interpreting the dynamics of informal organization in contemporary Africa”. The focus on institutional analysis helps better to explain the dynamics and the processes of informality by dwelling on such issues as enforceability and credibility of contracts (Sindzinger, 2006).

The challenges pertaining specifically to African informal markets are commitment failures and breaches of contracts, information asymmetries, and lack of capacity of African firms to meet quality requirements. It is always difficult to discern genuine agents from “hit-and-run” or “fly-by-night” agents (Fafchamps, 2004). While breaches and contract non-conformity may be purely due to opportunism, it may also be as a result of exogenous economic factors, for example, bad roads and power outages may unduly delay the conveyance of supplies and the production process (Fafchamps, 2001). Fafchamps likens African markets to the rudimentary flea market arrangements and garage sales of the developed countries; systems that are inherently fraught with opportunism, spot market exchanges in which transactions take place predominantly on a “cash and carry” basis.

Coupled with these challenges are the issues relating to weak formal institutional enforcement mechanisms. Third party quality assurance agencies (state and private) are often non-existent or where they do exist they lack the capacity to design and enforce quality standards or they are just unresponsive to the needs of small enterprises (Lall et al. 1994; Lall and Pietrobelli, 2002). Lall et al. (1994, pp44-45) made this observation regarding third party public provision of standard and quality enforcement services in Ghana:

Along with the absence of quality control systems, there is a widespread lack of appreciation of standards in Ghanaian industry. The GSB [Ghana Standard Board] lacks the resources (financial and human) to prepare engineering standards, to encourage industry to use them, and to enforce standards in a meaningful way...The absence of a range of approved and published ...standards means that there is a danger of substandard

specification being used to define product performance, with consequent effects on sales and export.

Recourse to legal institutions to resolve trade disputes is not a common practice. Fafchamps advances a number of reasons to explain this situation. The small enterprises and producers rarely possess valuable assets that could be used to service judgments and in that case threat of court action is not credible since recovery is very often problematic. If defaulters could be forced to pay, the size of transaction is often too small to warrant court action and if agents were free they:

...would still not take small contractual disputes to court because irrespective of court and attorney fees, valuable time is lost in court. This implies that it would be difficult...to significantly broaden the reach of courts by reducing their cost” (Fafchamps, 2001, p116).

This observation is consistent with the Northian perspective that it becomes increasingly uneconomical for agents to resort to formal systems of enforcement the smaller the size of trade transaction (North, 1991).

How do small producers and agents seek to reduce the high transaction costs inherent in the African markets? According to Fafchamps (2001), two main institutional responses are adopted by small African enterprises in order to minimize transaction costs and also enforce contract obligations. Fafchamps’ (ibid) main thesis is that in an environment of high uncertainty and risks and when formal contracts are imperfectly enforced, relational contracting based on trust and contractual flexibility are adopted by small African firms to minimize opportunism and delays that may arise from uncertain production

environments. In this sense trust becomes a substitute for formal enforcement mechanisms. Relational contracting economizes on transaction costs and at the same time serves as the source of innovative ideas for enterprise performance (Barr, 1998). Though Africa lacks effective formal institutions, thanks to informal institutions based on personal ties and social sanctions, small African firms are able to reduce high transaction costs and also gain access to resources for their production activities (Fafchamps, 1996, 2001, 2004, Barr, 1998; Brautigam, 1997). Meagher (2010) highlights two main perspectives on African social networks “optimists” and the “pessimists”. The pessimists see the African social networks as representing social liabilities that are inimical to economic development. The optimists regard Africa’s social networks as a solution to the problems of state and market failures, which emphasize the role of trust, communal solidarity, indigenous institutions of reciprocity and social sanctions. From the latter perspective, Africa’s informal systems are crafted as “weapons of the weak to emphasize the triumph of local organizational solutions in impossible situations” (ibid, p20). The extensive use of informal systems and informal institutions by small-scale African entrepreneurs to reduce uncertainty and agency problems had led some to argue that they could be perfect substitutes for weak formal institutions in supporting market exchange (Brautigam, 1997). This study takes issue with this claim and maintains that informal institutions and informal networks may enable small African firms to reduce agency problems and ensure the flow of resources for productive activities locally, but they are not rigorous enough to enable small firms to meet contractual obligations as they seek to participate in expanding and complex trade arrangements under uncertain microeconomic

environments. The incentives to provide certain services through informal trade networks may be stifled by opportunistic tendencies, mistrust and competitive pressures.

Meagher (2010) argues that in the contexts of extreme economic stress and global competition, the economic performance of African social networks can be enhanced by the nation-state. She argues that successful networks cannot be defined as independent of the state but are rather shaped by their relationships with the state. She states: “dynamic networks are as much a product of, as a substitute for, effective state intervention” (ibid, p174). The nation-state is relevant because:

In a globalizing economy, a viable small enterprise sector requires a wide range of services that cannot be provided through social networks...these include facilitative trade policy, decent roads ...technical up-grading, and assistance in meeting the administrative and quality requirements of access to global markets. Even sustaining the social cohesion that underpins collaborative enterprise networks is as much a product of state policy as of cultural affinities” (ibid, p174)

In addition to considering the roles of state policy and trade networks is also the issue of whether or not governments’ policies can foster the creation of business networks for enterprise competitiveness (Humphrey and Schmitz, 1996, 1998; Schmitz, 1999). According to Humphrey and Schmitz (1996) cooperation and trust can be produced in situations where there exist no prior social ties. They support this position with the examples of networking programmes in Denmark and Chile where cooperation and networking among small-scale producers was brought about by external intervention, though, they admitted the approach is new and requires further testing.

Situating African (informal) markets within the framework of institutional analysis breaks new grounds in helping us to understand the workings of market institutions, especially, the role of relational contracting or social networks in enabling economic exchanges in Sub-Saharan Africa to take place in the context of weak states. To what extent do relational contracting and informal market practices enable small enterprises to succeed in terms of meeting the more exacting market obligations in distant markets given the uncertain environments within which African enterprises operate?

The major caveat of seeing relational contracting as a response to the environment of high risks is that it leads to the fragmentation of the markets into small networks as partners are only comfortable dealing with people they know and can trust (Pedersen and McCormick, 1999, Fafchamps 2004). In other words, the consequences of the pervasiveness of weak formal institutions and the adoption of informal institutions in their stead lead to the fragmentation of African markets. This is consistent with the view expressed by North (1991) regarding the limitation of informal institutions in enabling local producers to engage in distant trade. Fafchamps (2004, p71) in particular reference to African markets elaborates this position as follows:

...although effective in enabling business to develop and firms to gain access to trade credit, [it] leads to the fragmentation of the economy into networks. It limits the range of commercial partners a firm may possibly deal with in a businesslike fashion. Because the economic reach of firm is reduced, one expects specialization and firm growth to be restricted.

Although flexible contracting (for example by allowing renegotiation of late deliveries, risks are shared) and relational contracting are beneficial to enabling enterprises to deal

with contractual non-performance and risks locally, they become problematic as local manufacturers seek to trade with international clients. Flexible contracting practices are often (mis)interpreted by foreign clients as bordering on opportunism and unreliability, and inconsistent with the strict adherence to contractual obligations that is required by international trade; this together with other obstacles may explain why African entrepreneurs trade very little with the rest of the world (Bigsten et al. 1998).

The workings of African markets are still far from the neoclassical prescriptions pertaining to an ideal free market system. Market exchanges based on inter-personal relationships may be prevalent in African contexts but this study will show that pervasive opportunism, which is counter to trust building, may erode the effectiveness of trust-based market exchanges. It may therefore ultimately not be cheaper to transact business in such an environment, economic agents may have to expend resources and efforts policing and safeguarding transactions to avert deceit. Monitoring costs are raised, especially, when some investments have been made in the relationship. These may provide some explanations for the differences in the success of Asian and African informal networks in trade transactions. Informal institutions will be ineffective as a market constraining device if information about the conduct of market participants are hard to come by and breaches of informal contract are weakly enforced. The Chinese Guanxi informal trade network is often cited as an effective informal market institution and its effectiveness is attributed to the internal sanctions of losing trade relationships with all network members which, serves as incentive for cooperative behaviour (Standifird and Marshall, 2000). The success of informal networks critically lies on the

availability of information about partners, effective monitoring and enforcement (i.e. biting sanctions taking the form of loss of valuable future relations).

Unlike advanced economies, Sub-Saharan Africa lacks indigenous large vertically integrated firms capable of addressing some of the institutional challenges inherent in their environments. Hierarchies tend to protect the ownership of know-how; better enable the enforcement of contractual obligations and also internalize important talents of particular individuals (Fafchamps, 2001). Why small African enterprises rarely graduate to become large firms still remains an open question. The general observation in the literature of small enterprise development suggests that the majority of micro-enterprises hardly graduate to become large-scale enterprises. Those that succeed to be become medium or large-scale firms are in the minority. Commenting on the growth of micro-enterprises in five Sub-Saharan countries, Mead and Liedholm (1998, p67), observed that “about only 1% ‘graduated’ from micro-enterprise seedbed and ended up with more than 10 workers”. The explanation for this trend is often attributed to differences in location of enterprises, educational background of enterprise owners, availability of financial resources, technology and market orientation. The very few that manage to graduate from their survival stage and grow are the very ones that have relative good access to 1) stable markets, 2) finance for working capital and capital investment, 3) adaptable technology, labour and raw materials, 4) urban locations and 5) entrepreneurs with good educational background willing to take risks and able to innovate, and solve the various transaction issues that influence their firms growth (Fafchamps, 1994; Grosh and Somolekae, 1996; Mead and Liedholm, 1998; McCormick et al. 1997; Rogerson, 2001). Fafchamps (1994),

particularly, highlights the significance of market size and technology adaptability to firm's size. He argues that the small size of markets in Sub-Saharan Africa is a hindrance to firms' growth. The small firms generally, tend to serve localized rural and urban markets, dominated by poor consumers. These enterprises offer products that are low in quality and least amenable to the use of mass production techniques. In the words of Fafchamps (1994, p5), "...mass production techniques have not yet been developed or adapted to local tastes; small-scale technology *is* the state of the art technology" for many small enterprises in Sub-Saharan Africa. He pointed out that even if the technology is available, the incentive for its acquisition or adaptation would come from an increasing market size resulting from the emergence of new market sources. Murphy et al. (1989) makes similar claims about the linkage between the size and composition of the market and the question of whether or not an enterprise would adopt handmade artisan production or mass production techniques. A market composed of quality-conscious rich upper class consumers is bound to favour the demand for high quality handmade products (high end niche markets). Conversely, the market that is dominated by large and relatively rich middle-class is more likely to sustain mass production profitably. Small-scale African firms may potentially adopt mechanized mass-production strategy for growth if they are able to access larger markets.

2.7 Conclusion

The discussion in the chapter delved into the debate of the relative importance of formal and informal institutions in minimizing transaction costs and facilitating market exchange. Formal institutions are state-sponsored rules-setting and enforcement whereas informal

institutions are spontaneous, self-enforcing and self-provisioning market mechanisms. The consensus is that both institutions could reduce market risks and uncertainties and provide stability to the market on condition of effective monitoring and enforcement. There are those who maintain that effective formal institutions and its associated enforcement mechanism are better able to sustain expanding and anonymous trade than informal institutions that relies on personal ties. The theoretical and empirical evidence, however, points to the persistence of informal institutions in both developing and developed economies and they may be used in complement with, or as substitute to formal institutions. Informal institutions as complete substitute for formal institutional arrangements is questioned on the basis that in an expanding trade regime and under the circumstances of endemic opportunism, informal mechanisms are weak in protecting specific investments from opportunistic hold-up, poor in guaranteeing quality of goods and arrest other forms of market failures like free-riding. In the context of weak enforcement, informal trade institutions make imperfect substitute for formal institutions. Credible formal institutions and generalized trust are important prerequisite for trade specialization; otherwise coordination of economic activities would take on the form of restricted and simple market exchanges.

The fourth section of the chapter embodied the discussions on other market coordinating mechanisms that are the subcontracting and inside-contracting relations and the extent to which both arrangements could reduce market risks and also enable firms to grow. The various dimensions of subcontracting were discussed and how they interlock with production networks. The understanding is that strong subcontracting relations built on

trust are important for minimizing risks and sharing of resources. The discussion also dealt with the various dimensions of trust and their relative strengths in enabling firms to access critical resources in order to remain competitive. The absence of trust or pervasive opportunism and weak enforcement renders subcontracting an ineffective tool for coordinating market activities. Though subcontracting is considered a modern phenomenon, its origin is traced to the putting-out system that existed in the 19th century, which later evolved to become inside-contracting arrangement. The inside-contracting system differs from subcontracting in that the contracted producers operate *inside* the production premises of the lead entrepreneur. Inside-contracting from the historical accounts was a coordination response to address the market imperfections to which the rudimentary subcontracting was not robust enough to deal with because of its inherent weakness of laxity of control over the production processes. The purported demise of the putting-out system and the rise of inside contracting was attributed to the following factors: 1) the independence of the subcontractors made it difficult to supervise production 2) the behaviour of the independent subcontractors was difficult to keep in check 3) lack of supervision led to embezzlement of resources provided by lead entrepreneurs 4) absence of supervision also led to poor and uneven quality products and delays 5) lack of work discipline on the part of subcontractors resulting preferences given to farming and other cultural activities over industrial production. The view was that the inside-contracting that emerged was more effective compared with the loose putting-out system to deal with these sources of imperfections. The increased in demand and volume of trade coupled with the availability of workforce willing to work on contract and the emergence of technology for standardized production contributed to the natural

development of inside-contracting. The advantage of the inside-contracting system is that it affords the entrepreneur indirect control over the labour process and direct control over product quality.

The fifth section was devoted to the concept of global value chains and how the governance structures of the chain may either constrain or enable small-scale enterprises from developing countries to participate in global trade. The section also highlighted the challenges African firms face in their attempts to build performance-enhancing linkages with global buyers in order to benefit from market information, product innovation and technical upgrading.

The reviewed literature showed that the new institutional economics offers an important framework for gauging institutional arrangements that support market transactions in Africa. The converging theme regarding markets and market institutions in Sub-Saharan Africa generally is that they are imperfect. Market exchanges are generally rudimentary and bedeviled with deceit and opportunism and thus raise the cost of transacting business in this environment. The small and microenterprises dotted on the continent rely mostly on informal mechanisms or relational contracting arrangements to minimize transaction risks and again access to critical resources. This enables trade to take place but on a limited scale where enterprises trade with individuals they know personally. Endemic mistrust and monitoring difficulties may weaken the strength of relational contracting as a market coordinating tool. These, it is argued limit the ability of microenterprises and small firms relying on trust-based relations to participate in trade on a wider scale for the

purpose of growing their enterprises. Those firms that attempt to engage in wider trade with individuals they don't know tend to face larger threats of opportunism and are also confronted with the huge challenge of addressing the mismatch between their domestic coordination constraints and the conditions pertaining to the distant markets. Very often these small exporters lack the relevant export market information and the local capacities to meet market demands. The small firms are somehow able to overcome the problem of market information asymmetric by relying on trade intermediaries. This, however, may leave them vulnerable to intermediaries acting as agents who may be in a position to exploit their contacts with foreign buyers to make excessive profits e.g. Lebanese traders in West Africa and US agents buying for US retail chains.

CHAPTER THREE

THE RESEARCH METHODOLOGY

3.1 Introduction

The study has been designed to help understand the forms of market and institutional arrangements adopted by Ghanaian craft producers in meeting export market demands and to overcome uncertainties and high transaction costs locally. By institutional arrangements, the study looks at arrangements that stress inter-firm linkages and informal mechanisms of exchange. The discussion in the previous chapter looked at the significance of institutions in minimizing transactions costs. In particular, the importance and the limitations of informal institutions in facilitating market transactions in the absence of effective formal institutions were highlighted. Also discussed were subcontracting arrangements and inside-contracting and their relative effectiveness under extreme market imperfections. How do the exporters respond in terms of organization of production to challenges pertaining to their local production environments as well as to the demands of the export market? The study attempts to address this question using an in-depth case study approach. The chapter is divided into four main sub-sections. Section 3.2 follows the introduction and entails the theoretical discussions of the case study approach and the justification for doing network analysis using this approach. It is followed by the rationale for the sector of choice of this study in section 3.3. A detailed description of the actual data collection process, which took place between July and September 2007, using in-depth interview techniques is found in section 3.4. Section 3.5

concludes the chapter with a summary of the theoretical understanding of case-study research and the main lessons learnt during the data collection process.

3.2 Case Study Approach to Network Analysis

A qualitative case-study approach is adopted for our investigations into the coordination responses that Ghanaian craft exporters adopt in their attempt to overcome the constraints placed on them by their environment and access critical resources in order to meet market requirements and obligations. The case study approach is considered suitable for exploratory research where understanding of the research issues is the prime objective, the phenomena being explored are difficult to quantify, particularly if they are not easily identifiable, and there is the need to study the phenomena in their natural settings (Yin, 2003; Klein Woolthuis et al., 2005). Anderson et al. (1994) have suggested a case study approach to network analysis. In their view, to be able to deepen our knowledge of the processes within different types of networks requires a detailed case study approach that seeks to cover substantial time periods and attempts to seek information from several of the firms in the industry as well as from different functions within the firm.

Nadvi and Schmitz (1994) similarly suggest an in-depth case study approach that relies on multiple sources of evidence for network analysis. They argue that network analysis is not just about describing the characteristics of inter-firm relations but it is also concerned with dynamic processes underlying interactions between various economic agents in the network. To be able to deal with the dynamic processes, which depend on the subjective accounts of events by the actors in the subsector, requires a research tool that is capable

of capturing these perceptual views from the actors considered in the study (Leonard-Barton, 1990). Thus, the case study approach with its emphasis on in-depth investigation into contemporary and historical processes through the use of multiple sources of evidence (Yin, 2003) is therefore an appropriate research approach for undertaking network analysis (Nadvi and Schmitz, 1994).

3.2.1 Validity and Reliability of Case Studies

In-depth case-study research is often criticized on the grounds that it is overly subjective and the research findings tend to be coloured by the researcher's and the researched's biases and opinions. The critics argue that qualitative case study approach is less suitable for generating theory because of its context-specific nature and the fact that the findings are based on the subjective views of selected few. The response to this critique is that the rigour of qualitative case study like any other scientific inquiry is assessed based on whether the investigations follow transparent research trajectory and employs the use of appropriate tools and techniques for gathering data and reporting findings so that the conclusion would be judged as credible and dependable. Adopting a case study approach is not so much an issue of the size of sample that one interviews but whether the research process has been undertaken in a systematic fashion: "No matter how small our sample or what our interest, we have always tried to go into organizations with a well-defined focus—to collect specific kind of data systematically" (Mintzberg 1979 cited in Eisenhardt, 1989, p532). In the language of qualitative research, validity conveys the notion of the steps taken by researchers to achieve accurate and credible results (Creswell, 2003). Yin (2003) in particular, offers certain criteria for judging the quality and rigour of

qualitative case study approach which includes construct validity, external validity and reliability. These concepts are explained in turns below.

Construct validity: is concerned with the explicit specification of the concepts or objects that are being studied in relation to the study objectives and asks whether correct operational procedures have been established for delving into what one says he/she is studying. Am I measuring or investigating exactly what I said I was going to study? Once this is done, Yin suggests among other tactics the following to increase the quality of construct validity during the data collection stage. The first is the use of multiple sources of evidence in a manner that encourages convergent lines of inquiry, a process referred to as data triangulation. He argues that case-study findings are likely to be much more convincing and accurate if it is based on several different sources of information, allowing for data corroboration. Real triangulation is achieved when the facts of a case study are supported by more than a single source of evidence. It is also possible for the facts to diverge using multiple sources of evidence. In this case, the data is said not to have been triangulated and thus analyzed as separate facts to the case study. The second tactic is to establish a chain of evidence. This is about maintaining clear linkages between the various stages of the study so that the conclusions can, for instance, be traced to the research questions, the data collection tools employed and the evidence. In this instance, a third party observer should be able to convince himself of the basis by which a researcher arrived at a certain conclusion by tracing the evidentiary process from the conclusion backwards to the study objectives.

External Validity: as indicated earlier, in-depth single cases are criticized for being narrowly focused on selected few actors who may not be representative of the “universe” and therefore forms a poor basis for generalizing. Yin draws our attention to the major flaw of confusing qualitative case study research with quantitative surveys:

Critics are implicitly contrasting the situation to survey research, in which a sample (if selected correctly) readily generalizes to a larger universe. *This analogy to samples and universe is incorrect when dealing with case studies* (p37).

He argues that qualitative case studies are distinct from quantitative surveys in the sense that they rely on analytical generalization in which the researcher strives to generalize a particular set of results to some broader theory. In the particular case of this study, an attempt is made to relate the findings to the theoretical framework derived generally from the new institutional economics and its sub-disciplines of transaction costs framework and network analysis. The use of theories is important both during the pre-data collection processes as well as providing the framework for interpreting the case study findings. The theoretical ideas that are developed tend to influence the research questions, the propositions, units of analysis and provide the logic for linking the data to the research propositions: “the complete research design embodies a ‘theory’ of what is being studied” (Yin, 2003, p29).

Reliability: is about whether a later researcher conducting the same case study can achieve the *same results* by following the same procedures as described by an earlier researcher (it is about doing the same case over again and not replicating the results of one case by doing another case study). The precondition for allowing a repetition of the

same case study is through the documentation of the procedures and the operational steps that were followed through in the earlier study. Yin likens the process to accounting in which the accountant has to be aware that an external auditor performing a reliability checks on his balance sheets must be able to produce the same results if the same procedures are followed. Cautious documentation of the various stages of the research process makes the case-study research a reliable inquiry.

Though this set of criteria if followed through could increase the quality of the case-study research, they are not straightjacket prescriptions; they would have to be adapted to suit specific circumstances. The whole process is an iterative one; allowing the researcher to adjust the research design ranging from research objectives, fieldwork techniques and theoretical dispositions to the existing circumstances. The flexibility that is in-built in the case-study data collection methods enables the researcher to take advantage of emergent themes and unique case features (Eisenhardt, 1989). The research questions change, in much the same way that the theoretical propositions would have to be re-shaped in line with the evidence. The open-endedness, however, does not suggest that the qualitative case-study researcher can do whatever that he/she likes; “the need to balance adaptiveness with *rigour*—but not rigidity—cannot be overemphasized” (Yin, 2003, p61).

Nadvi and Schmitz (1994) have proposed that network case studies begin with the gathering of secondary data with the view to obtain information on: the general performance trends in the sector; the number of active firms (focal enterprises) in the sector, and the range of other trading actors these firms collaborate with in their business

transactions. This is then followed with a more in-depth data gathering on selected active firms in the industry. This phase focuses on the *firm's histories* and *relationships*. It covers issues such as how the firm was established, how it has developed over time and critical turning points in the firm's history. The focus on relationships entails seeking qualitative data on the linkages between the focal enterprises and its various link units and the resulting resources derived from the interactions. Collecting detailed information about the focal enterprises and their production link units, according to them, is done with the ultimate aim to disaggregate the processes underlying the linkages between the various economic agents in the network. They suggested that if possible data should be sought from all the link units within the network since this could have the advantage of enabling the researcher to triangulate evidence from multiple sources thereby enhancing the validity of the study. It also ensures that certain actors who perform important functions within the network are not excluded (Murty, 1999). However, not all the agents in the firm's trade transaction network can be identified and interviewed in all practicalities, especially, when these trade interactions takes place in the informal realm.

3.2.2 Setting of network boundary and inclusion criteria

The practical difficulty of engaging in detailed dialogue with all the possible link units in the network is what is referred to as the boundary problem. This is an issue that requires a judgment to be made about which firms or organizations are to be included in the firm's network of trading partners if all the actors or the agents in the network, in practical terms cannot be identified and interviewed. But this cannot be done arbitrarily; it ought to be carried out in a well thought manner. To overcome this requires setting the network

boundary by selecting the actors, which are of strategic importance to the objectives of the study (Nadvi and Schmitz 1994; Murty, 1999). Setting the network boundary also demands an effort to establish a set of rules about the actors that will be included in the study (Spren and Zwaagstra 1994; Murty, 1999). The more convenient approach, generally, is to delimit the network actors through the use of spatial boundaries—however; some important actors outside the defined geographical vicinity may be excluded (Murty, 1999). To ensure that certain actors with strategic influence on the network are not excluded, priority is given to sectoral connections over geographical proximity (Nadvi and Schmitz, 1994). Beyond geographical boundaries, Murty (1999) proposes that the decision on the inclusion criteria be made either on the *attributes* of the actors in the network or the *relations* they establish with other actors. The attributional criteria could be based on specific features or the functions of the actors, whilst the use of relational criteria is about the inclusion of those agents that are cited by other agents as important to their trading relationships. The relational criterion is noted to be appropriate when a complete list of actors to which a selection could be made for interviews is non-existent. Using members of the network to cite others in the network i.e. snowballing, even though time consuming, is considered an ideal method to avoid excluding actors who may have important influence on the network. Whilst the use of inclusion criteria seeks to limit the numerous actors that could potentially be considered and to ensure that important actors with strategic importance in line with the study objectives are considered, it in the end excludes other actors in the network. The point that is of paramount importance is that the decision to use inclusion criteria must be based on the study objective (Murty, 1999). Confusion could arise as to the exact object of study when one

attempts to study abstract and intangible phenomena such as inter-firm trade relations and informal trade networks.

3.2.3 Unit of Analysis

The units of analysis in this study are the “*focal enterprises*” (Nadvi and Schmitz, 1994) and the production *relationships/networks*. The focal enterprises in the context of this study are the exporters. In network studies, the ultimate unit of analysis is the relationships that are established among trading partners. In this instance, it is argued researchers interested in studying trade networks can no longer focus solely on individual firms since attention shifts to a focus on the “whole” (Vandenberg, 2006, p19-10); for efficiency is derived from the “whole” instead of the parts. Feasibly and as indicated earlier on, not all enterprise units within a particular trade network can be identified and interviewed during the course of the fieldwork. Hence the focal enterprises become the starting point for studying the production network; recognizing the influences of the other enterprises within the network. The craft exporters have been selected as the focal enterprises in the craft export industry because of their strategic role in organising and coordinating production activities for export and the reason of being the principal risks takers in coordinating craft export activities. The characterization of the various categories of focal craft enterprises is presented in chapter four.

3.2.4 The Researcher's Position in the Research

The sector chosen for this study is not the researcher's "backyard". Backyard research according to Creswell (2003) often entails studying the researchers' own working setting. Despite the fact that this may facilitate easy access to information and deeper understanding of the issues under investigation, the danger of the researcher overly introducing his own biases into the data collecting and reporting process could be high. This researcher has been a "professional student" and had no historical background in the sector of choice and so the initial motivation for undertaking this study had more to do with the theoretical fascination with network approach to industrial development than with the experience of practicing in trade and industrial development. In 2004, when this researcher was exploring how informal (casual) port workers in Tema, Ghana organize themselves the importance of the functionality of informal groups and collective alliances with other agents in enabling the informal port workers to survive their fragile and difficult economic circumstances and also seek improvements in their working conditions became apparent (Boampong, 2005, 2010). The role of informal groups in enabling the informal workers to minimize difficulties related to their working environment and also survive their economic exigencies, albeit, in a fluid manner, inspired this researcher to further test the idea of how informal networks and ties enable small firms that predominate in the Ghanaian economy to survive their own economic realities and possibly grow. There are some studies that have specifically looked at this theme in the Ghanaian context, notably Barr (1998), Fafchamps (1996), and Lyon (2000). However, the empirical evidence is scant, particularly, on the question of the robustness of informal

networks in fuelling success as small scale firms operate beyond the territorial boundaries of Ghana.

This researcher had very little understanding of the sector of choice at the start of the study. So part of the initial efforts during the pre-data collection stage was directed towards the search for secondary background information on a number of industries to see how they fit into the network perspective and also to seek information on performance trends as well as the major actors operating in the case study industry. The literature search yielded four studies that either focus solely or partially on the sector of choice. They included the works by Biggs et al.'s (1994) "Africa can compete!", the World Bank study (2001) on the international competitiveness of the Ghanaian non-traditional export, Action for Enterprise (2004) study; sponsored by DFID on embedded business services for craft exporters in Ghana and Pageau's (2004); GTZ sponsored survey into the Ghanaian craft industry. These studies provided the researcher with useful empirical background information on the craft industry prior to the actual data collection process.

3.3 The choice of sector

This study is confined to the enterprises of Ghanaian craft producers who export their products abroad, especially, to the West. The sector is dominated by mainly small-scale enterprises and traders whose activities remain largely informal and yet have succeeded in gaining access to the much difficult international market. The birth of the craft industry as a source of foreign exchange earning coincided with the implementation of SAPs and

since then the sector has achieved some modest success in the midst of uphill challenges in the export market. It holds the potential for poverty reduction, if coordination dysfunctions and problems to exchange are resolved. The industry is a labour intensive activity based on renewable natural resources with strong backward linkages to a number of craft villages with enormous potential for employment generation and poverty reduction (World Bank, 2001). Given the level of informality in the industry, it would be appropriate to infer that the actors in the industry are more likely to rely on inter-firm relations and informal ties in their business transactions instead of formal institutional mechanisms. Indeed, Sørensen and Nyanteng (2000) in a study of Ghanaian non-traditional export to the regional West African market hinted that small-scale traders who dominate this market rely predominantly on traditional trading systems and highlighted the environmental constraints that confront the traders. These constraints, they indicated include dishonest behaviour on the part of fellow traders and the difficulties they face in monitoring their goods against theft. According to these authors, the traders have naturally responded to opportunistic risks by “doing things in-house... rather than relying on the market” (p58). What this means is that each trader carries out many activities herself or himself. Traders monitor and control their goods to avoid risks. Monitoring costs are thus relatively high in the regional West African trade given the small scale of operations. Notwithstanding the high level of risks and monitoring costs, the traders are able to check opportunism by building long-term relations and by organizing policing trade associations. The authors also made an important distinction between the traditional traders who take advantage of small market opportunities compatible with their operational capabilities for the motive of survival as against growth-oriented producers

who seek to expand their firms by exporting via network relations and by developing operational routines to enable them minimize opportunistic inclinations. This distinction and other observations by the authors regarding monitoring difficulties and trade risks are of particular significance to this current research. These provide snapshots of the circumstances in which the enterprises of the chosen sector operate in as well as the institutional responses to the coordination difficulties they face. The problematic aspect of these authors' study is that it failed to recognize the dynamic aspect of the firm's development i.e. how inter-personal ties and networks may enable a surviving small export trader to evolve and become an expanding producer. Such a gap is not surprising, because it is consistent with the general view held in the literature that micro-enterprises or small traders rarely "graduate" to become medium or large firms, especially in Sub-Saharan Africa (see discussion in section 2.5). The strength of this study, however, is that it points to the relevance of transaction cost framework and network analysis to the study of the Ghanaian non-traditional export sector whether it is to be understood in terms of the rudimentary regional trade dominated by small traders relying on informal ties in their trading transactions or producers with routinized operational arrangements in-house. Large parts of the African markets are generally regarded as rudimentary, uncertain and risky compared with Western markets but these markets do not lack institutions (though of different kinds) that support their operations. Thus an attempt to understand these markets and institutions cannot escape being interpreted within the framework of the new institutional economics (Fafchamps, 2004; see section 2.5).

The choice of this sector is not only appropriate to enable us to broaden our understanding of the ways and extent to which the institutional responses by the small-scale exporters enable them to address local constraints to production and high transaction costs but also help us to gain an insight into how the coordination mechanisms adopted by these small firms fare in terms of meeting end market requirements and the specifications of international buyers in the absence of formal institutional mechanisms that are responsive to small-scale firms. The integration of the craft industry into the export market is observed to have been made possible through various forms of inter-personal subcontracting relations (AFE/DFID, 2004). The sector of choice thus provides us with the microcosmic platform for examining the extent to which small-scale exporters are able to overcome transaction uncertainties and address trade complexities e.g. quality standard requirements by relying on inter-firm contractual relations and informal mechanisms.

3.4 The Actual Field Data Collection Process

3.4.1 Geographical Location of the Study

Interviews were conducted in Accra and Kumasi the capital and the second largest city in Ghana respectively. The initial fieldwork plan was designed to concentrate the interviews in Accra. However, it became apparent during the course of the interviews that Kumasi and two surrounding villages, namely Foase Atwima (about 10km from Kumasi) and Ahiwaa could not be excluded because of the strong backward linkages the craft industry has with producers in these areas. These villages are endowed with master-craftsmen and raw materials and almost all the handicraft exporters in Accra interviewed either

subcontract orders to the craftsmen or source inputs (labour and raw materials) from these two craft villages. While the majority of the artisan subcontractors are in the villages, the exporters, traders and the intermediaries are mostly found in Accra. Out of the 38 active exporters of wood-based craft products listed under the Government of Ghana Craft Initiative Programme (CIP), 30 are in Accra, 6 in Kumasi and 2 in Takoradi and Central regions. The major export agents under CIP who also represent international buyers locally are all in Accra. This is a reflection of the closeness of Accra to the craft market and the availability of relatively better trade facilities.

3.4.2 The Search and Selection of Interviewees

Forty-seven interviewees and informants were selected for one-one-one interviews. This included interviews with exporters/producers, export agents and other informants. The distribution (see appendix 1) of the interviews was as follows: Export agents 6, Subcontractors/Producers from Foase Atwima and Ahwiaa 4, mainstream machine furniture exporter/producers 4, Informants 6 (all from the craft industry). Twenty-seven focal exporters were interviewed and their distribution was as follows: large-scale producers (8); craft workshops/designers (4); export vendors (10); and traders (5). The list of the exporters was obtained from Aid to Artisans Ghana (ATAG) and was corroborated with exporters on the books of Ghana Export Promotion Council (GEPC). The initial fieldwork plan envisaged the use of firm size i.e. the number of employees to ensure the inclusiveness of the different types of the exporting firms operating in the industry in the study. The use of this criterion was found to be problematic in that the artisans and craftsmen are employed on piece-rate basis and their engagement by the

exporters vary depending on the quantity of the orders to be executed, which makes it difficult to determine with certainty the numbers of workers engaged by the exporters. The employment relationships between the exporters and the workers are fluid and the exporters do not claim responsibility over the crafts people they hire as their workers. The categorization used by the Government of Ghana Craft Initiative Programme (CIP) was instead adopted for the selection of the interviewees in an attempt to ensure that the main stakeholders are not excluded. The enterprises were classified as large scale craft producers, niche market producers and firms working with agents (export vendors) (the list of exporters obtained from ATAG was also categorized in a similar fashion). Whilst these seemingly reflect some kind of the different firms operating vertically along the craft industry chain, the criteria for the categorization were not explicitly explained. The criteria used could have been based on the specialties and internal production capacities of the enterprises.

The list obtained from ATAG contained only the active exporters in the craft industry. The hundreds of upstream subcontractors who supply finished or unfinished products to the exporters and many artisans were not captured in the list neither could it be obtained from other sources. The exporters who in this case are the focal enterprises of the study were asked to identify these other actors in their production. They were asked to identify their suppliers or subcontractors upstream, who either execute orders or source raw materials for them. From this, four main artisan subcontractors in the two craft villages visited were identified and selected for one-on-one interviews. They were selected for interviews because they represent the cream of artisan subcontractors who possess good

knowledge about craft production in the villages. Prior to the visit to the villages, it became apparent after a series of interviews with the respondents in Accra that these subcontractors who maintain a large pool of craftsmen in the craft villages frequently execute orders for the exporters in Accra. The responses from many of the exporters converged on these selected artisans as their main subcontractors.

Even though, the key export agents/intermediaries were on the list obtained from ATAG, to confirm the trade relations between the exporters and the agents, however, the exporters were asked to identify the trade agents and buyers they usually transact business with.

Personal interaction with key actors in the craft export industry by this researcher received a boost with an opportunity to attend a trade seminar organised by the Trade Facilitation Office of Canada (TFOC) in collaboration with the Ghana Export Promotion Council on 20th July 2007 at M'Plaza Hotel. TFOC's Design Africa initiative sought to create market linkages in Canada for African producers of home décor items and also to help the participants of the initiative to develop their capacity to move into the high-end of the home décor export market. Interactions with some of the exporters at the seminar revealed that most of them were disinterested in the high-end Canadian market for a number of reasons. They were interested in producing items for the mass market as they are easy to produce and required little effort, consisting of relatively regular high volume orders from buyers as against irregular, low volume orders and difficult to produce premium items for the high end of the market to which they do not have the production

capacity to undertake. The exporters who have the capacity to produce the middle-ranked quality products prefer to remain loyal¹ to their buyers and would not want to sell their designs, at least in the short-term, to their buyers' competitors. It was therefore not surprising that only one Ghanaian craft exporter was selected in 2006 to participate in Design Africa trade show in Canada.

3.4.3 Interviews with Key Private Actors in the Industry

The interviews were unstructured and open-ended. They took the form of a one-on-one conversation with the respondents. The type of interview technique adopted to seek qualitative information from the firms is described by Yin (2003) as guided conversation entailing the pursuance of a consistent line of inquiry (using the case study guide) but the stream of questions under consideration were fluid rather than rigid. The interviews were less structured than conventional interviews but more guided than the word conversation might also suggest (IDD and Planafic, 1998). The underlying reason is to satisfy “the needs of [one’s] line of inquiry while simultaneously putting forth ‘friendly’ and ‘nonthreatening’ questions in [an] open-ended [manner]” (Yin, 2003, p90).

The owners/managers of the exporting enterprises and the export agents were the individuals who were interviewed. The informants were mainly officials from public and private organizations knowledgeable about the activities of the craft and furniture industry. The subcontractors from the carving village interviewed were master-craftsmen

¹ This does not mean the exporters maintain single and exclusive buyer relationships. It would be demonstrated later in the empirical chapters that indeed the exporters maintain multiple buyer relationships. The lack of capacity on the part of the majority of the exporters to produce high quality products seems to account for their disinterest and not the fact that they don't want to betray their loyalty with their buyers.

with many years of experience as carvers. The interviews were carried out at the production sites or places where the exporters and the production subcontractors undertake their activities. It was a difficult task physically locating some of the production sites of the exporters. These exporters are scattered all over Accra with some of them operating in unmarked and difficult to locate premises. Visiting the exporters' premises for interviews was time-consuming and entailed a lot of travelling to some very remote areas and the periphery of Accra. This researcher, in the early stage of the data collection, was fortunate to be taken around to few production sites in Accra by one key informant; employed as quality inspection officer by the American buyer; AMC.

Most of the interview sections lasted between 45minutes and 2hrs using a conversation guide (see appendix 3). The interviews were carried out at the premises of the exporters or the offices of the informants. The specific items in the guide included the profile and histories of the exporting or the producing enterprises, business linkages between the exporters and subcontractors, buyers, export agents, horizontal linkages between the producing firms and issues bordering on quality standards and monitoring. The various items in the guide were not mechanically followed through to the letter in all the interview sections. It had to be adapted in certain instances to suit the specific circumstances of the industry, which could not be anticipated during the design stage. For instance the distinction of different buyers and that of arm's-length subcontractual production arrangements and in-house production systems were realized in the early stage of the interviews to be significant features in the industry and so were prioritized in the subsequent interviews. Again, the initial research question was concerned with the

architecture of inter-firm relations utilized by the exporters in accessing critical resources for their production activities. It also became evident in the course of the data collection that the form and the extent to which inter-firm subcontractual relations enable the exporters to coordinate their production activities could not be disentangled from soft issues such as trust or mistrust and the context of the socio-economic environment. It became apparent that issues of enforcing contractual obligations and the uncertain local socio-economic environment do have implications for how the small-scale firms organize their production activities for export. These issues were given attention in the course of the data collection, which in the end influenced the reframing of the conceptual framework and ultimately the research objectives.

Again, the fieldwork plan did not envisage a separate interview guide for the export agents and the other informants from the private and public organisations. What was done, instead, was to engage this category of respondents in much more unstructured conversations in an attempt to gain an insight into their role in the craft industry and more importantly to corroborate some of the issues raised by the exporters. The export agents were used as proxies for buyers since this researcher lacked the capacity and resources to contact the buyers directly for interviews. The export agents who represent international buyers locally were in a better position to know the minds of the buyers and market trends. The buyers were not the prime focus of the study though their perspectives would have helped to understand how their activities influence the commodity chains of Ghanaian crafts.

The data collection was undertaken at a time when most of the exporters were executing orders for AMC group of buyers from the USA. This afforded the researcher the opportunity to observe the production activities at the various links in the domestic chain from carving at the production sites to packaging and final shipment at the port. The timing, in other words, was right for an investigation into such an industry that is market-driven. Some of the interviews were audio-taped with the consent of the respondents.

The study encountered two main difficulties. The first centred on data on the performance of the individual exporters in the craft industry. The common indicators often used to measure the performance or growth of small firms are the number of employees employed overtime, profit margins, output, sales and assets (Mead and Liedholm, 1998). What is lost in this set is the measurement of the influence of the industry on poverty reduction. As should be expected, there was the general apprehension by the craft exporters to give figures on their profit margins, neither were they able to supply information on production output since they hardly keep good records of these a except few who were able to give an indication of their annual production capacity. They sometimes chose to give impressionistic statements such as “business is good or bad”; “margins are good or falling”. The study, however, relies on secondary data (export sales) to give some indication of the performance of the different exporters vis-à-vis the production strategies adopted by the exporters. The study relies on narratives instead of hard figures to describe the influence of the industry on poverty reduction.

The second was that the mainstream furniture producers who were contacted for interviews were “too busy” to grant interviews. It also came to the realization of the researcher that a majority of the mainstream furniture producers were indeed not into active export. The office of Furniture and Wood Products Association of Ghana (FAWAG) was visited three times with the view to construct a list of producers or exporters of machined furniture. In all three occasions the office was found closed. It was later gathered that FAWAG had been operationally inactive for several months; casting a shadow on what was to be expected. The Association of Ghana Industries (AGI) was instead contacted for a list of manufacturers or exporters of machined wood furniture. Seven producers were contacted but four granted the request for interviews and out of this only one manufacturer produce high quality furniture for export. The other three firms produce furniture for the high end of the domestic market. These companies are large and vertically integrated firms that produce furniture for the local Ghanaian market. The implication of this to the study is that the traditional mainstream furniture producers are largely under-represented in this study. However, the few that were interviewed had had occasional or one-off encounters with clients beyond the borders of the Ghanaian market and gave hints about some of the difficulties they face and the barriers that prevent them from becoming active players in the export market. The problems encompass the lack of technical and managerial capacity to meeting quality and delivery requirements of mainstream furniture at competitive prices. European buyers, for instance, require suppliers to prove that the wood products they buy come from a sustainably managed and independently certified sources. Ghanaian forests have not been independently certified, except in a few cases of sawmilling firms whose forest

consignments have been certified by an independent body (e.g. Samartex has its consignment certified by SGS South Africa). In response to the question of why they have not been able to export to the international market one respondent identified their inability to procure raw materials from certified and sustainably managed sources as a major impediment to their access to the export market. A respondent had this to say in connection with this issue:

The problem that we face is getting the market. I think the reason why we are not getting it is partly due to our inability to get certified forest consignment. Because any buyer who would want to do business with you would ask: “can you get the raw materials from sustainable source?” They want to be sure that the moment they start business with you, you can produce and meet their volume requirement every time. I have had encounters with a lot of buyers over there and most of the time the requirements we can’t meet them (Irokko company).

3.5 Conclusion

The chapter dealt with theoretical foundations of case-study research as a scientific inquiry and its appropriateness for studying informal trade networks and relationships. The chapter was also devoted to the recounting of the techniques and procedures applied to the data collection process. In-depth case study approach was adopted to help explore the extent to which inter-firm subcontractual relations and other informal mechanisms enable the case study firms to overcome resource constraints and production uncertainties and risks. Suitable for investigations into hard to quantify historical and contemporary phenomena, qualitative case-study research with its inherent emphasis on in-depth naturalistic understanding, is often branded too open-ended, subjective and entailing the biases of the researcher and the researched, which are far cry from objective scientific

inquiry. But the proponents of case study methodology argues that the rigour and the quality of case studies can be assured when investigators set out to address their research problem by following a clearly defined and transparent research trajectory. The correct specification of units of analysis and the operational measures that seek information from multiple sources helps to increase the construct validity of case-study research, whilst generalization is made possible by relating the case study findings to the relevant theoretical ideas. These theoretical understanding of case-study approach influenced the actual data collection process. The in-depth interviews that were conducted using conversational guide to gather information about the structural and instrumental aspects of inter-firm relations did not only target the focal enterprises but also other key actors who are linked to the production chains of the focal firms as well as key stakeholders operating outside the production chains. The underlying aim was to seek information from different possible sources for the purpose of data triangulation as well as seeking divergent views. By relying largely on official list of exporters, the study seemingly focused on the relatively successful exporters to the exclusion of other least visible exporters. The intention during the data collection process was to interview sizeable number of the different actors on the craft production chain. However, the use of few proxies (identifiable and key master artisans in two craft villages) meant that the actual views and insights of the numerous artisan and artisan subcontractors operating upstream either individually or in groups are under-represented in this study. There was the practical difficulty of physically locating some of these itinerant artisans and subcontractors. One interviewee recognized the danger of under-representing the views of some of the exporters by constructing selection frame based solely on official list:

when anybody comes for these feasibility studies, they give you some specific people, isn't it? We are about fifty people. Did they give you all the fifty names? They give you people who have a set-up, a showroom and an office. Most of the exporters don't have these. They do their work in the bush. They don't have warehouse, they don't have any premises. I think you should have the opinion of those who even don't have offices. You should interview them also.

The message here is simple; one should always seek multiple opinions from multiple sources to help broaden the findings of the research. The inability to contact and interview the mass of the artisans and artisan subcontractors who in a sense are considered the main workers in the industry is one main limitation of this study. What this also means is that there is a lack of sufficient evidence to properly gauge the implications of the craft export industry on employment levels, environment and poverty as perceived by the mass of the artisans operating in the craft villages. The anecdotal evidence (perceptual) gathered from the few artisan subcontractors interviewed showed a positive impact of the industry on the material conditions of the artisans (see section 6.6 for the narrative of the poverty impact of the subcontracting relations on the artisan subcontractors).

Another downside of this study is the failure to determine how the trade regulatory regime, in this case the African Growth and Opportunity Act (AGOA) impacts on the relative success of the industry in integrating into the US market.

Timing of the data collection is of great significance especially when the phenomena under study are time sensitive. Most of the exporters at the time of the fieldwork were in the season of executing orders for export. Another experience during the course of the

data collection is the need to be flexible and adjust the process accordingly to take advantage of emerging trends and issues as was the case with this study. Again, rushing to the field for data collection is not a perfect substitute for good pre-data collection preparation, particularly, if the researcher is not familiar with the chosen case study sector. No matter how well one gets prepared, there are bound to be some “reality checks” and disappointments as not all intended issues are likely to be resolved in the course of the data collection.

CHAPTER FOUR

THE BACKGROUND TO THE GHANAIAN NON-TRADITIONAL EXPORT SECTOR

4.1 Introduction

This chapter presents the background information on the Ghanaian non-traditional export (NTE) sector in general, narrowing down to the chosen case study sector i.e. the craft industry, which is a subsector of the NTE. This introductory section is followed by the presentation of policy initiatives and government support towards the non-traditional export sector; demonstrating the activist role of the government of Ghana in promoting the NTE sector, especially, during the SAP-era. Section 4.3 follows with descriptive background information on the craft export industry; in its historical and contemporary contexts. The character of the various actors involved in the vertical production chain of the craft export industry is presented in Section 4.4; showing the myriad of different private actors in the industry. Section 4.5 entails background information on the exporters who are considered the focal actors for this analysis. Section 4.6 concludes the chapter with a summary of the main themes. The government of Ghana played a very active role in promoting the craft export industry in the early years of the industry's development but current evidence demonstrates the assumption of the dominant role by a myriad of private actors who drive the industry.

4.2 Non-traditional Export Sector

For almost a century, the Ghanaian export sector was dominated by the traditional primary products of cocoa, timber, gold and other minerals until the 1980s when the

government of Ghana intensified its effort to diversify the export sector to include non-traditional export products as part of the economic recovery programme. Non-traditional exports are defined by the government of Ghana as any export products other than the traditional export products of cocoa beans, logs and timber, and gold (Buatsi, 2002). They include horticultural products, fish and seafood, processed and semi-processed products including furniture and furniture parts, aluminum products, prepared foods and beverages, and craft products.

Teal's (2003) analysis of the Ghanaian export sector growth revealed a picture of erratic performance throughout the twentieth century. For instance, he observed that the export per capita in 1907-1910 was US\$100 and after decades of steep decline, the effort to diversify and improve the performance of the export sector in the '80s and the '90s could only return export growth at the end of the twentieth century to the levels recorded at the beginning of the century. The export sector during this period was also dominated by cocoa exports with the attendant problems of volume and price fluctuations, which affected export earnings; "the history of Ghana's trade performance in the twentieth century is the history of its cocoa exports" (p125). The contribution of non-cocoa export to total export during this period was negligible.

The diversification of the export base through the addition of non-traditional products to the export basket was thus an agenda designed by the government of Ghana in an attempt to reverse this trend. The goal of promoting non-traditional exports was to boost and diversify export earnings, generate employment and reduce poverty (World Bank, 2001).

The government of Ghana set itself the target of ensuring the non-traditional export sector contributes about US\$ 16 billion to the total export revenue as part of a broader agenda to ensure that Ghana achieves a middle income status by the year 2020 (Buatsi, 2002). The production of the main primary exports is concentrated in the relatively rich southern regions leaving other deprived parts of the country virtually out of the export trade. The promotion of non-traditional products for export was viewed as a way of enabling poor regions in Ghana to participate and to share in the gains of the export trade (Konadu-Agyemang and Adanu, 2003).

Notwithstanding the insignificant increases in export growth over the decades, the contribution of the non-traditional export to total export revenue is very visible. The earnings of non-traditional export grew from a modest value of US\$119.3 million in 1994 to US\$705.4 million in 2004 and as at 2003 about 3000 individual exporters participated in the industry (see table 1). What is still not clear is the total number of workers engaged in this sector.

The identification of the need to diversify the export sector was given effect in 1969 by the government of Ghana through the establishment of the Ghana Export Promotion Council (GEPC) and the introduction of import surcharges and export promotion packages to support non-traditional exports. But as Addo and Marshall (2000) observed firms established in the '70s to start large-scale production for export of non-traditional products did not receive any government support. The 1980s, however, marked a renewed interest on the part of the government of Ghana to revive the non-traditional

export sector by introducing new policies and programmes with the intent to remove some of the constraints in the sector. These constraints were identified to include weak production base, high domestic production costs, inadequate export incentives, difficult bureaucratic procedures associated with export transactions and the lack of knowledge about export procedures. The government's effort manifested itself in the areas of fiscal policy incentives and restructuring of the existing formal trade support agencies. The major fiscal incentives introduced by the government to boost the export sector included a retention by the exporters of 35 per cent of export earnings in foreign exchange, corporate tax rebate allowing the exporters of non-traditional products to claim 30-75 per cent of their tax liability, customs duty draw back allowing exporters to draw back up to 100 per cent of duties paid on materials imported to produce goods for export. There were also attempts to modernize the existing trade support institutions such as the Ghana Export Promotion Council (GEPC) and the Ministry of Trade and Tourism (now Ministry of Trade and Industry). This was done through retraining of personnel and staff in international trade practices and provision of modern office equipments to these agencies. Regional offices were also established to expand the reach of trade promotion services to rural producers and exporters (Addo and Marshall, 2000). To improve the production capacity base of rural communities for export, the government initiated the development of export production villages (EPV) with the objectives to; develop effective institutional mechanisms for the coordination of rural export production, to ensure availability of supplies for sustainable export markets, to improve production efficiency and quality consciousness among rural producers. According to Addo and Marshall (2000), UNDP and government of Ghana jointly financed the EPV projects and by early 1990s, five of

them had been established. The International Trade Centre (ITC) in 2001 reported on the success of an EPV in the Ghanaian village of Aburi as follows:

Started with 35 woodcarvers in 1990, this EPV has grown to over 300 woodcarvers. It now employs nearly 700 persons...its annual export turnover has risen from US\$160,000 to US\$3,250,000 in 1997. It has become a reliable supplier to Getrade [a local export agent] and Pier One (cited in Wolff, 2004, p124).

The policy initiatives and the renewed interest by the government of Ghana (GOG) to strengthen trade support institutions since the '80 could be described as appropriate to the development of NTE, yet a lot of constraints continue to persist both at the institutional and the microeconomic levels. The GEPC faces the problem of inadequate funding, which limits its ability to fully address the constraints facing the exporters fully. A major critique of the government of Ghana's intervention in the development of the non-traditional sector is that it has overly been concentrated on the macroeconomic environment to the detriment of tackling the microeconomic constraints (Addo and Marshall, 2000; World Bank, 2001). As it will be shown later in chapter five, the difficulties at the microeconomic level presents major challenges for the case study sector and the extent to which the craft exporters respond in terms of institutional arrangements to overcome these constraints is important for their success in the export market.

TABLE 1: TRENDS OF NON-TRADITIONAL EXPORTS (1994-2004)

ITEM	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Agricultural Products											
Value(US\$m)	39.2	24.4	50.3	57.4	77.8	84.5	74.5	82.5	85.7	138.1	159.9
Number of Exporters	1206	1280	1714	1654	1344	1232	1520	1570	1442	1546	NA
(Semi) processed Prod											
Value(US\$m)	77.8	130.2	223	267	317.5	313.3	321.1	362.7	407.2	446.6	540.4
Number of Exporters	1154	1333	1424	1430	1256	1228	1518	1401	1491	1492	NA
Handicraft											
Value(US\$m)	2.3	2.1	2.9	4.72	6.4	6.7	5.0	14.9	11.3	4.2	5.2
Number of Exporters	169	192	201	194	160	137	165	146	150	143	NA
Total											
Value(US\$m)	119.3	159.7	276.2	329	401.7	404.4	400.7	459.6	504.3	588.9	705.4
Number of Exporters	2529	2802	3339	3278	2760	2597	3203	3117	3083	3181	NA

Source: Konadu- Agyemang and Adanu (2003) and “The State of the Ghanaian Economy 2004”

4.3 The Organization of Ghanaian Craft: The Case Studies Sector

This section looks at the organization of Ghanaian crafts prior to the implementation of SAPs and during the SAP-era. The craft industry during the pre-SAP era was driven by domestic consumption (e.g. specialist crafts) and the tourists market. The SAP regimes encouraged a direct integration of the Ghanaian craft industries into the international market where the industries’ growth is linked to, the ability on the part of the exporters to adapt to, international demand and pressures (World Bank, 2001).

The Craft Industry during the Pre-SAP regime

Earlier studies on the Ghanaian craft industry associated the genesis of some craft production with the development of the Ashanti court system in the eighteenth century (Johnson, 1979, Browne, 1981b):

...in the early eighteenth century, the strong and wealthy centralized government of Ashanti established certain settlements as craft villages to supply the pots, stools, drums, cloth, goldwork, state swords and other paraphernalia of the Ashanti court”(Browne, 1981, p313).

Johnson’s (1979) rich account of the organization of Ashanti craft talked of an elaborate product specialization among the craft villages² that surrounded Kumasi, the Ashanti capital, and the dynamism of the sector in adapting to changing internal market circumstances. Craftsmen made stools, staffs of office, umbrellas, drums and wooden utensils for the royal kitchens. Though this craft production was originally tied to the traditional court system, the artisans had the freedom to make and sell some of their wares to outsiders but not the designs reserved for the palace. Beyond making crafts for the chief’s court, Johnson observed that, some of the craftsmen earned a living through craft production: “...they [the craftsmen] could...earn enough by craft production to buy such things as salt, which they could not themselves produce...” (ibid, p78). Some of the craft villages, according to Johnson (ibid), specialized in producing for the tourist market (the exact period when this emerged is not known but it was in existence in 1975 when Johnson undertook her fieldwork)³ and adapted their product forms to the taste of the tourists:

² Johnson (1979) named the product specialties of the villages as follows: Kente (Bonwire, Wono; now Sakrawono, Adangmoase and Besease), Beads (Daaba), State shields (Wawasi), Basketry (Wawasi), Umbrella making (Banko, near Mampong Akrofonso, Nsuta and Wawasi), Adinkra Cloth (Asokwa and Ntonso), Pottery (Pankronu and Old Tafo), Gold weights and Brassware (Kurofofrom), Blacksmithing (Adwumakase Kese and Wawasi). It is important to note that most of these villages, which Johnson described as “more than three hours’ easy walk from Kumasi”(p78) are now suburbs of Kumasi demonstrating that “the map of the craft villages is certainly not static today, nor was it evidently static in the past (ibid, p78). A map of the craft villages surrounding Kumasi can be found in Browne (1981b, figure 1, p314).

³ According to Wolff (2004) the Ashanti fertility dolls were popular as tourist and export art forms in the late 1960s.

At Ntonso, it has become something of a tourist industry, developing interesting new forms in combination with tie-dye techniques, and non-traditional colours...Bonwire has lost much of its traditional character by catering to tourists, though the town is still one large workshop (p78).

The tourist market served as important source of demand for the Ghanaian decorative craft products when court crafts declined in importance. Johnson (ibid) described the emergence of a tourist market as follows: “The court crafts [were] in a more precarious situation...In many cases the tourists...stepped in...Meanwhile the craftsmen [were] ready enough to oblige”(p82). She described the booming tourist demand for Ashanti craft in this manner:

The crafts of Ashanti are flourishing as never before. Every year, busloads of tourists arrive in the better-known villages, eager to return home with ‘authentic’ African works (ibid, p81).

The craftsmen catered to the new sources of tourist demand by introducing new product designs, copied from other West African countries, into their product mix:

Masks are not part of Ashanti tradition, but since many tourists think that all African art ought to include masks, Ashanti carvers cheerfully make copies of Ivory Coast masks with ‘legs’ or the Chi Wara antelope masks...of...Mali (ibid, p82).

Besides the tourist market, domestic consumption of decorative craft products also grew in importance. Curio shops emerged on the streets of major cities in Ghana and the stocks of small traders grew. Johnson (ibid) reported the growth of the domestic market for the works of craftsmen for “...items not aimed solely at the foreigner, and of course the demand for domestic necessities always exists” (p 82). The sophistication of decorative

craft production became elaborated through the production systems that evolved in line with the existing market segments. These production systems could be described as “mass production” for the tourist market and niche production for a small number of individual clients locally. Some specialist villages, according to Johnson, produced items for the tourist market using entirely so-called traditional techniques, but in fact containing elements of mass production but lacked “the subtlety of the best traditional work and at worst produce[d] rather crude results” (p80). However, other craftsmen who produced to the orders of clients “were able to maintain a higher standard of workmanship than [was] possible by mass-production for the tourist market” (p80).

Browne’s study (1981a), which dealt with the internal dynamics of kente weaving among the Ashanti, looked at the ways kente cloths were marketed locally, the nature of employment in the industry, and the question of whether or not the attempt made by external agents to “modernize” traditional technology of craft production in the 1970s was an appropriate intervention. In her study of kente weavers in Sakorawono, a village near Kumasi, Browne (ibid) observed three ways in which finished products from the village were marketed. Women traders from the village who taking cloths to other parts of Ghana; the artisans themselves taking cloths to the markets in Kumasi and elsewhere; and by selling direct to customers, from whom the kente had been ordered. Because the craftsmen in this village did not produce for the tourist market, they lost out on the advantage of increased sales and revenue from the tourist market. However, they gained from having a year-round demand and a more consistent price structure for their output (Browne, ibid). Browne also categorized the workers in the craft village into self-

employed and those she regarded as “employees”. The employees were hired by people such as master artisans, women traders and individuals who had capital with which to buy raw materials. The employees were given the raw materials to make the products and they were paid on a piece-work basis according to the value (quality) of the product. The self-employed bought their own raw materials, made their designs and marketed the finished products for profit. According to Browne, most of the artisans and the employees aspired to the status of self-employment but there were cost barriers to achieving this status. To achieve this status required the artisans to work long years in order to accumulate enough capital. The employee status was a “temporary status...albeit, a prolonged period for some” (ibid, p35).

There were attempts as far back as the seventies to “modernize” or “improve” Ashanti crafts. Notable intervention, for instance, was initiated by the Technology Consultancy Centre of the University of Science and Technology (UST, now Kwame Nkrumah University of Science and Technology), and the National Cultural Centre in Kumasi to improve the efficiency of craft production through technology improvements (Johnson, 1979, Browne, 1981a). According to Johnson (1979⁴, p82), some technical problems were resolved through this effort but “in some cases the idea of increased efficiency [was] applied...in a somewhat insensitive way, often by people who have not taken the trouble to find out the consequences of the technical changes they advocate”. The supposed improvement that was achieved (e.g. the hybrid mock-kente loom) was “neither efficient nor traditional...they [gave] the poorest impression of Ashanti technology” (ibid, p82). In

⁴ Johnson’s fieldwork was conducted in August 1975 with a research grant from the Centre of West African Studies, The University of Birmingham.

particular, the effort by UST to improve the technical efficiency of kente weaving in 1973 yielded little success (Browne, 1981a). The craftsmen who participated in the project were neither interested in using the “new” technology nor willing to introduce it in the village—the cost of acquiring it was a major obstacle. She further observed:

It is difficult to see what relevance such a project would have had...even had the [technology] been cheaper. The amount of capital available to artisans and the likely demand for new products are critical considerations when considering technological change, particularly in a rural setting (Brown, 1981a, p36).

The size of market is emphasized by Fafchamps (1994) and Murphy et al. (1989) as an important element for technological adaptation (see section 2.6). Whilst simple and handmade products suit small niche markets, mass production technology is sustained by large market size. Johnson (1979) was not particularly against the modernization of Ashanti craft: she argued that the “...worst enemies of Ashanti crafts may well be those who are most anxious to preserve them” (ibid, p82). She summed up her stance on the mechanization of, for example, kente weaving as follows:

Neither traditional narrow looms nor any other form of handloom can provide the quantities of cheap cloth demanded in Ghana, and the answer must ultimately lie in mechanized manufacture...similar considerations apply to any goods in mass demand (ibid, p82).

She, however, maintained that traditional Ashanti crafts could survive in sophisticated societies by exploiting local and export niche markets that cannot be cheaply and efficiently be exploited by mechanized production systems. Basu (1995) draws our attention to the fact that technical change driven by external demand may not necessarily have a benign effect on original craft production—for it may lead to the “destruction of

the very authenticity that formed the basis for its genuine appreciation in external cultures”(p259).

The debate in the seventies and subsequently was not so much against technical change in the organization of Ashanti craft production rather it was about the idea that effective technological improvements are achieved with the support and participation of the artisans themselves (Brown, 1981a).

The Craft Export Industry since SAP

The contemporary craft export industry is described as a success story in Ghana. As the above analysis illustrates, craft production has been part of Ghanaians culture for many years, and its birth as direct earner of export revenue coincided with government policy to promote non-traditional export during the implementation of Structural Adjustment Programmes (SAPs) in the 1980s and 1990s (Pageau 2004; World Bank, 2001). Export earnings from the craft sector (as evident in table 1) rose from the modest figure of US\$2.3million in 1994 and peaked at US\$14.9million in 2001 but this has been achieved within a volatile competitive environment. This success according to Pageau (2004) is partly due to the fact that Ghana is a new source of authentic ethnic craft products. Export earnings from the sector, however, declined from US\$14.9million in 2001 to US\$5.2million in 2004. The uniqueness and authenticity of Ghanaian crafts are obviously regarded as insufficient to sustain the growth trend in the craft industry if the producers fail to match the quality and price of their global competitors (Pageau, 2004).

The Ghanaian craft export sector is a market-led industry and its original integration into the international market was spear-headed by international buyers, especially those from the USA. The role of government has been concentrated in the areas of trade promotion and facilitation activities, which are done through the agency of Ghana Export Promotion Council (GEPC). This government agency sometimes with financial support from international development agencies has been instrumental in linking the local exporters to international buyers. Initially, most craft export went to Europe, albeit, in small quantities mainly as a result of participation in European trade fairs. The entry into the US market of Ghanaian craft products in relatively large quantities started in 1993 when Pier 1 began sourcing products from Ghana. The maiden contact between Pier 1 Import and the craft exporters, for instance, was initially facilitated by the GEPC.

In 1992, the GEPC with financial support from the Commonwealth Secretariat organized a trade mission to the North America in search of buyers. Following this mission, Pier 1 entered the Ghanaian market as the first key international buyer. Because of the instrumental role played by GEPC in bringing Pier 1 to Ghana, the expectation was that the Pier 1 buyers would rely on GEPC to coordinate export orders on their behalf. But because of their general apprehension in doing business with government officials, especially in Sub-Saharan Africa, they chose instead to rely on a non-state channel by appointing a private agent on a commission basis, Kraft Export Consult, to be their local agent to coordinate export orders locally on their behalf. Incidentally, the owner of this agency was also on the staff of GEPC and was part of the team that helped to bring Pier 1 to Ghana but later resigned to establish Kraft Export Consult. The owner of this export

agency had this to say in connection with the reluctance of Pier 1 buyers to deal with the public agency:

They [buyers] selected a number of items. They ordered from about 23 different producers to the tune of US\$900,000...they gave us the orders ...the vice president of Pier 1 then asked me if I can recommend somebody for them to coordinate their export orders for them. But I reminded him that they were brought into the country by GEPC and that the council would coordinate for them successfully. They replied that US companies do not want to work with government institutions and that they prefer working with privately-owned companies. I indicated to them that I have already registered a private company and if they wanted I could use my company to do for them. The man said OK, at least we are familiar with you; we have known you for sometime if only your office would give you the blessing to do it, if it wouldn't have any conflict of interest.

The initial moderate success chalked up by Pier 1 in doing business in unfamiliar business territories such as Ghana in the early 1990s caught the attention of other US buyers under the umbrella of the Associated Merchandise Corporation (AMC) to enter the Ghanaian market. This development stimulated the emergence of myriad local traders, local export agents and other intermediaries to fill an institutional vacuum between the small artisan producers and the international buyers (World Bank, 2001). The theoretical explanation for the emergence of the plethora of commercial intermediaries and traders in trade mediation is often seen as a coordination response to information problems, high transaction risks and imperfect contract enforcement (Fafchamps, 2004).

The policy initiative designed by the Government of Ghana under its Presidential Special Initiative (PSI) of the Ministry of Trade and Industry has sought to implement programmes with the aim of transforming the industry from its cottage-like, unorganized and subsistence-focused activities into a modern production platform capable of meeting

large orders and expectations in terms of standards of the international craft trade. A number of exporters were selected to benefit from specific initiatives under this government programme. The programme aptly recognizes the organizational difficulties facing the craft export industry and therefore sought to;

- re-orient the minds of the selected companies to adopt best practices in production organization and marketing and also undertake re-conditioning exercises to develop positive production attitudes towards exports;
- expose the selected enterprises to global best practices by organizing study tours to other craft exporting countries that have succeeded in “mass-production” techniques of craft products with the ultimate goal of learning how such enterprises in those countries handle large export orders and enforce standards and quality (six key actors were actually sponsored to visit Morocco, Philippines and Honduras);
- engage in product development initiative by fielding external and local consultants in addition to individual efforts in developing new products for export and also relying on the existing institutions of innovations.

Much as the government’s policy initiative offered appropriate response to the challenges bedevilling the industry, some of the exporters interviewed expressed very little confidence in the policy, regarding it as one of those bureaucratic processes that would only remain on paper and would not see the light of implementation.

4.3.1 Ghanaian Craft Export Products

The craft products that are imported from Ghana include baskets, traditional musical instruments, drums, wooden masks and figures, Ashanti stools, furniture and home accessories, beads and jewellerys, ceramic wares, textiles i.e. Kente products and other

cloth products. This study looked in particular at wood-based Ghanaian crafts. The export of wood-based crafts constitutes about 80 per cent of all craft exports earnings according to export figures from GEPC, thus considered fairly representative of the craft export industry (Pageau, 2004). Basket exports, which were next to wooden craft exports in terms of revenue, fell drastically from about US\$4.7million in 2001 to US\$550,000 in 2002 (GEPC) as a result of stiff competition from Vietnam—with better organised production systems to produce high quality baskets at cheaper prices for the international market. In view of the wide assortment of Ghanaian craft products, it is still possible to categorise them into the traditional/simple decorative pieces and middle-ranked utilitarian home accessories; products that have use in Western homes but designed with Ghanaian decorative designs.

4.3.2 Destination of Ghanaian Craft Export

Most of the Ghanaian craft exports are destined for the USA, Holland, Italy, Germany and Japan. The US with a huge African-focus market provides major demand for Ghanaian craft export and most of the products christened as “mass products” are for this market. There are smaller American niche market buyers who buy functional and the relatively high quality home decor from the few exporters capable of producing these types of products. It became evident in the course of the interviews that the craft products that are exported to the European market are of low volume; high quality functional products that the majority of Ghanaian exporters interviewed did not yet have the capability to undertake.

4.3.3 Raw material supplies

The main raw material for the craft industry is wood. Wood once regarded as in abundance in Ghana is increasingly becoming scarce due to forest depletion. The craft industry relies mostly on informal sources for wood supply, mainly through chain saw operators and “lumber dealers” who supply it with wood off-cuts from sawmills. The ban on chainsaw operators by the Government of Ghana since 1998 to curtail forest degradation has made it difficult for the exporters to obtain wood from informal sources. This, however, has not reduced the reliance of the craft exporters and the small producers on clandestine sources of wood supplies from distant villages though they often face harassment from forestry officials and the police and end up paying bribes in their bid to transport the logs. Most of the small producers cannot afford the high cost of sawn lumber that the millers are only prepared to sell at export price. Again fiscal incentives, such as tax rebates on volumes exported and the export earnings retention fund instituted by the government of Ghana encourages the millers to export instead of supplying the domestic market (Owusu, 2001). In the face of these difficulties, the exporters are resorting to lesser-utilised wood species instead of the fast depleting traditional hardwoods. Again some of the craft firms and producers have secured lands and embarked on tree plantation projects to ensure sustained supply of raw materials. A case in point is the Foase craft village where the artisans have come together, secured land and begun a tree plantation.

4.4 Background to the Key Private Actors in the Craft Production Chain

There are a number of actors in the production chain of the craft industry in Ghana and a brief description of the actors along the chain follows here, beginning with the actors involved in upstream activities and moving to those in downstream activities. The classification is derived from researcher's fieldwork data and other studies by Action for Enterprise (2004) and Pageau (2004). The actors in the vertical chains of the craft industry include the individual artisans and craftspeople, exporters, traders, export agents and international buyers. These are the actors along the commodity chains that link the Ghanaian craft products to the ultimate clients in the West and the roles they play are important in determining the success or failure of the art industries (Wolff, 2004). They are regarded as "gatekeepers" in the sense that they "play a role in controlling the commodity flow...and are essential actors in the feedback process that guides future production behaviours of artisan[s] ...who strive to remain active in a highly competitive market (ibid, p132). Wolff (ibid) identified the domestic gatekeepers at the supply end of the craft commodity chains in Ghana to include master craftsmen, entrepreneurial individuals (the exporters who form the central focus of this study), and export agents. At the demand end of the transnational craft production chain are the US and European buyers for small and large retail outlets. According to Wolff (ibid) an exploration of the activities of the different actors along the commodity chains that link African artisans to the Western market can be useful for understanding the nature of commodity flow, product change in cross-cultural context, and explaining success or failure of artisan industries in tapping the resources of global market. In addition to the various activities and influences of the various gatekeepers in the Ghanaian craft commodity chains, this

study also looks at how the nature of the *relationships* and institutional mechanisms utilized by the “exporters” in transnational craft commodity chains enable them to effectively coordinate their activities.

4.4.1 The Craftspeople and Artisan Subcontractors

These are the craftspeople with the indigenous skills who are directly involved in manually producing craft products for mainly the lead exporters and export agents on a subcontractual basis. They also sell directly, though on a limited scale, to regional buyers and small international buyers. Typically, the artisans and the craftsmen produce in groups independently in the craft villages⁵ and peri-urban areas in southern Ghana. The artisans and the craftspeople may also be contracted to produce at the workshops or the premises of the exporters. The master craftspeople, acting as lead subcontractors, hire other artisans and craftspeople to execute orders on a piece rate basis either in the workshops of their hirers or in groups in the craft villages. They are highly mobile occupationally and can easily switch from one lead exporter to another depending on who offers the highest bid. However, some of the artisans and craftspeople have established special relationships with some of the exporters and thus work regularly for them. They perform specialized and discrete activities such as designing and carving, sanding, polishing, finishing and sometimes packaging. There are gender and age divisions of labour in the craft production. The men undertake the designing and the carving functions while the women and children do the sanding and polishing of the products. Wolff (2004, p127) succinctly captured the nature of these divisions of labour in this way:

⁵ Foase Atwima and Ahiawaa in Ashanti region, Aburi in Eastern and other villages in Volta and Central Regions.

The [male carvers] make the raw piece and incised decorations and contract their wives, sisters, friends and kids for polishing. So mainly women sandpaper the pieces, put on finishing touches with the sharp knife and then apply the polish...The pieces however belong to the man, she is just a contractor and is paid her fee, if not she keeps the pieces and gives it only back after ...being paid. She also trains younger ones and her children to help her with the work after school. There are already 12 year old boys who hide, when the school teacher goes round the town to ring and bell and call them for afternoon classes, they prefer the polishing work.

The lead exporters may buy the raw materials and pay the artisan subcontractors for their labour or may subcontract the whole order to the artisan subcontractors and leave them with the charge to procure raw materials. In this instance, the artisans negotiate the price of each item to be produced with the lead exporters and receive advance payment to execute the order. Most of the exporters prefer the latter arrangement and give price incentives to artisans who procure their own raw materials to execute export orders. In this way, the exporters push the responsibility of procuring raw materials to the artisans. Since the exporters carry the financial burden and the risks associated with production pre-financing, they only subcontract to artisan producers they can trust not to abscond with their monies. Cheating by artisans and craftspeople is endemic in the industry; this is dealt with in more detail later in our discussion. The artisans and craftspeople also engage in transactions with multiple lead exporters to maximize their chances of getting export orders.

4.4.2 The Export Agents

They are the domestic representatives of international buyers in Ghana. They perform different functions and some of their activities overlap with the activities of the exporters.

There are seven of them playing significant intermediary roles between the exporters and the buyers. They include Getrade, Kraft Export Consult, Fritete, Afripeche, Delata, SPB Unicommerz and Sankofa. The intermediation functions of these export agents and their subcontracting relationship with some of the lead exporters are dealt with in detail later in chapter 5, section 5.4.

4.4.3 The Buyers/Market

There are different kinds of buyers who patronise craft products in Ghana. They can be segmented along the lines of volume of export orders, the product type, quality and the nature of the end market. They are the big and the small international buyers. The big international buyers with long standing trade relationship with Ghanaian craft exporters are from the USA. They include Pier 1 import and AMC group of buyers.

There are also international small buyers who deal directly with the producers or the exporters, let's call them the middle-ranked quality product buyers. They order small product quantities consisting of relatively complex products i.e. functional craft products. Unlike the big buyers, the interaction between the small buyers and the exporters is qualitative in nature. It entails exchange of market information and support for product development. Buyer demands regarding product quality and standards are high requiring more intensive interaction between the buyers and exporters. Some of the small buyers sometimes send their consultants to develop new products together with the exporters. The empirical evidence suggests though order volumes from individual small buyers are

low and infrequent, profit margins are relatively high (see quotations in sections 6.2.3 and 6.2.4).

There is also the category of small buyers who order small quantities of products similar to those patronised by the big buyers directly from the producers and the exporters. From historical accounts, these small buyers dominated the Ghanaian market until the early 1990s when the big buyers entered the market and almost forced them out of the trade, though some of them occasionally give orders to the artisan producers. Two of the producers interviewed at the export villages were executing orders for small Ghanaian buyers resident in the US at the time of the visit. The common defining factors for the international small buyers are that they offer better prices, make upfront payments to the producers to pre-finance production, and sometimes are more involved in developing new products with the exporters.

There are also other traders who travel from neighbouring countries to buy craft products from Ghana and re-export them. Tourists and one-time international buyers occasionally buy craft products from street-side shops and designated craft shops such as the Art Centre in Accra. Here the transaction is spot-like, one-off and entails a lot of price jostling and haggling between the vendors and the buyer.

The growth of the Ghanaian crafts products since the early 1990s has largely been driven by international demand. However there is an emerging domestic market— the expatriate workers, Ghanaian returnees from Europe and USA, hotels and restaurants— that offers a

great market potential for the high quality hand-made home products. One exporter interviewed had actually retreated from exporting and is now producing for this market and other exporters also indicated their willingness to diversify their market base to include the high-end domestic market. This segment of the Ghanaian market is quite demanding and also has tastes and preferences similar to the international market and can serve as a source of pressure for innovation and improvements.

This study though takes the local exporters as its focal actors in the Ghanaian craft commodity chain; it also recognizes the role of international buyers in controlling the chain. By specializing in marketing activities, the Western retailers and wholesalers are able to exert considerable influence on transnational trade in African craft products. The literature on global production network teaches us that international buyers tend to control the commodity chain they feed into by virtue of possessing market knowledge and marketing infrastructure. By occupying strategic positions in the chains they are able to exert pressure on their suppliers to ensure timely delivery of orders at specified quality without having to own the production infrastructure of the suppliers. The American retailers and wholesalers through their marketing strategies manipulate the meanings of African craft products based on their deep understanding of the tastes and preferences of American consumers to boost demand (Wolff, 2004). The success of Ghanaian akua ba (fertility) dolls in the American market, according to Wolff (ibid), has been achieved through the Americanization of the traditional meanings of the dolls by the US retailers:

The retailer, driven by economic concerns, modifies and inserts information based on their knowledge of the American audience. A good example is the

firm that expands the meaning of “fertility” to include success in business...the retailers convey an aura of authenticity and functionality around their goods to encourage consumers to “use” the dolls as home décor”(ibid, p136)

By specializing in marketing at the end of the commodity chains, the retailers are able to control the economic value of the African craft products (Wolff, 2004). It will also be demonstrated in chapter five that by occupying special position in the commodity chains, the buyers are able to achieve compliance with quality and timely delivery through financial penalties for non-compliance with product specifications and delivery timelines.

4.5 The Focal Craft Export Enterprises

Defining who the exporter is in the Ghanaian craft industry is a bit problematic. There are a plethora of firms and individuals who consider themselves as exporters. The common variable that seems to hold true for all the individuals and firms calling themselves exporters is that they are “business people” or entrepreneurs who are motivated by profits to take business risks. They secure production orders from the buyers, take responsibility of the final products and ultimately bear all the risks associated with the execution of the export orders. One key role of the lead exporters is to seek resources e.g. trade credit and make advance payments to the craftspeople for the execution of export orders. Thus delays, non-execution of orders and cheating by artisans and subcontractors increase the risk burden on the lead exporters. These exporters are the focal actors in the network of private actors operating in the craft industry.

On the classification of industrial activities, McCormick et al. (1997) argued that the organization of production is not only a function of technology but also should be seen as entrepreneurial strategy that matches available resources to market relations. Following from this, they developed a typology for Nairobi's garment firms based on their differing interaction with the input market, capital and the product markets. Action for Enterprise also used similar criteria to classify Haitian craft industry (USAID, 2006). This study adopts similar criteria to categorize the focal enterprises according to their differing interaction with export agents/buyers, product type, the input market and production strategies. The focal enterprises fall into four main categories: traders, export vendors, craft workshops/designers, and craft factories. The characterization of these enterprises is preceded with brief historical background of some the enterprises.

4.5.1 Characteristics and Types of the lead Export Enterprises

Most of the craft exporting enterprises were established in the early 1990s to meet growing demand from US retailers and wholesalers. The ownership structure of the majority of the firms is either sole proprietorship or "husband-wife" family business and almost all are wholly Ghanaian-owned. The educational background of the owners varies with enterprise. Generally, those firms that are described as traders and possess no or minimal production capacity are run by individuals with very little formal education. The relatively successful exporting companies are owned by entrepreneurs with formal education up to the tertiary level and in certain instances have been associated with the craft industry in some other ways before deciding to establish their own firms. The formal training of the entrepreneurs and their past experiences are regarded by most of them as

useful to the craft export industry. Also worth noting is the significant role played by the NGO, Aid to Artisans Ghana in grooming (wittingly or unwittingly) some of the entrepreneurs who later established their own exporting firms. The table below highlights the training background and date of some establishment of some the exporters interviewed.

Background of some Selected Craft Exporters

Afrikan-Dream Studios Ltd started as a sole proprietorship in 1993 by Ralph Ashong and grew to become a limited liability enterprise in 1996. Ralph Ashong is a professional sculptor and African Art graduate of the Kwame Nkrumah University of Science and Technology and his association with Aid to Artisans (USA and Ghana) greatly contributed to his understanding of the export market.
Mr. Ofoli is the proprietor of Kottage Originals, which was established in 1999. Mr. Ofoli is very talented and has the flair for innovative African designs. He is a product of Kwame Nkrumah University of Science and Technology (KNUST) where he studied rural art and industry. Upon completion of his university education, he worked with Aid to Artisans Ghana until he resigned to establish his own export firms, though he continues to deal with ATAG. Likewise, the owner of Delhouse enterprise, Mr. Del Boampong, studied Art for his undergraduate and recently completed his MBA studies at KNUST.
Wild Gecko was established in 1993 by the company’s partners Poem van Landewijk and Kingsley Sarfo. Poem has always been interested in beads and had practiced bead making as a hobby until she teamed up with Kingsley who was then exporting beads to Germany. Her Father, a geologist and a lecturer with scientific interest in bead materials inspired her to take up a career in that direction and she is always motivated to be creative and always thinking of doing something different. Wild Gecko recently produces a wide range of high quality furniture and other home accessories for both the export and the domestic markets.
Ms. Grace Mensah, the owner of Hide-Out enterprise, has been in the craft trade since the late 1970s. She started by selling craft products at Accra Art centre to tourists. She was introduced into this trade by her late husband who was an artist and sign writer. Unlike other exporters, she has very limited formal education. Ms Grace was introduced to the export market by the boss of ATAG. She started exporting decorative craft products as a vendor in 1999 and specializes mainly in traditional crafts with very little functionality.

Source: Field Interviews 2007

4.5.2 Traders and Export Vendors

The export vendors are “businesspeople” who liaise between domestic export agents and local artisans/craftspeople. They may not have the artisanal skills themselves but instead

rely on skills of the craftspeople and artisans. In certain instances they operate as traders who possess no production capacity and wholly subcontract their orders to artisan subcontractors. The export vendors possess some minimal production capacity and may subcontract whole or the early stage of production i.e. sourcing of raw materials and carving to artisan subcontractors but undertake later stage activities such as drying, product finishing, packaging and labeling in their small workshops.

The export vendors usually take product samples designed by the artisans and craftspeople and present them at buyers' exhibitions organized by the export agents. When they are fortunate enough to secure orders, they subcontract the orders to the artisan designers after the price of each piece is negotiated. When an agreement is reached, the vendor then makes an advance payment to the artisan contractor or the craftspeople to execute the orders. The contractual relationship between the vendors and the craftspeople lasts as long as the orders last but the relationship is reciprocal. The artisans give their product samples to vendors for buyers' exhibitions and the vendors must reciprocate by subcontracting the orders to the artisans and trust remains a key ingredient in this relationship. The vendors specialize in typical craft products such as masks, figurines, drums, dolls, trays; products that could be describe as lacking greater functionality and are mostly produced for the lower end of the mass market. Apparently, the order volumes that are executed through these individual vendors are small but when the individual orders are consolidated by the export agents or put together they constitute large volumes, which enable them to economize on shipping costs.

The vendors lack the capacity to undertake their own export processing arrangements neither are they able to attract buyers directly. They mostly rely on local export agents to perform logistical and other shipping arrangements for them as well as depending on export agents for orders.

The craft workshops and the large-scale producers began as vendors with very minimal or no production capacity in the formative years of the industry. When the US buyers first entered the Ghanaian market in the early 1990s, the organizational response of the craft exporters were reported as follows:

“...the suppliers have responded with speed and have demonstrated flexibility. This rapid supply response has been possible, in large part, because the traditional nature of most of the products ordered has not called for new skill development. Many suppliers are themselves middlemen and have enjoyed the flexibility of sourcing from a large pool of smaller, often rurally based, production groups. Some suppliers have also had to set up production units to complement these sources, if only for finishing products to specification” (Biggs et al. 1994, p35).

4.5.3 Craft Workshops/Designer Producers

The craft workshops or the designer producers have integrated greater part of the production process in their workshops. They have been described by Biggs et al. (1994) as “boutique” producers who produce smaller volumes for quality conscious consumers who are less price-sensitive. This category of exporters produce a relatively high quality range of products including garden furniture, cabinets, chest of drawers, bedside and floor lamps, mirrors, magazine and CD racks, coasters, jewellery/treasure boxes and picture frames; mostly functional products, which are of middle-ranked status.

They contract a few experienced and skilful artisans with whom they have built a long-term relationship to work in-house. They maintain a skeleton administrative staff that performs the normal secretarial as well as sales functions.

The craft workshops also produce the typical traditional figures, wall hangings and masks mostly patronized by volume buyers. They subcontract the early stage of these products meant for the low-end mass market to independent contractors and artisans and undertake finishing and packaging in their workshops. Like the vendors, the craft workshops make advance payments to the independent contractors and artisans to execute their orders whether or not they produce outside or inside their workshops. When the artisans work within the premises of the exporter, not only are they provided with the space and the equipment to work but they are also provided with raw materials.

The craft workshops or the designer producers maintain two main market channels i.e. the domestic and the international market. The domestic market comprises mainly expatriate workers and Ghanaian returnees from the West. The export market encompasses boutique shops and small quantity niche buyers as well as the mass market controlled by high volume buyers. The craft workshops have not weaned themselves completely off the services of domestic export agents. They continue to rely on the domestic export agents for markets services such as securing export orders, especially from big buyers, and shipping arrangements. They construct differing relations with the buyers. Characteristically this group of exporters maintains two streams of interaction with buyers. While the interaction with the large international buyers is impersonal, that

with small quantity international buyers is more personal and entails qualitative flow of information and other hands-on support.

Kottage Originals Enterprise

Kottage originals is a case that typifies what has been described above as craft workshops or designer producers. Currently the owner employs three carpenters, two finishers at his workshop and he doubles as the designer of the company. Kottage Originals also has a showroom situated within the Premises of Artist Alliance Gallery on La Beach road in Accra. Whilst the firm centralizes the production of its furniture orders in its workshop, it subcontracts the early stage of production of its products meant for the US mass market to subcontractors in the craft villages (such as Foase, Asamang and Aburi) and the finishing is done in the firm's workshop in Accra. It is difficult to estimate the precise size of the mobile subcontractors that the firm works with, this is because when the firm contracts out the orders to its main production contractors (master craftspeople), they in turn subcontract to other artisans and craftspeople, the number of which is difficult for the firm to estimate. The firm claimed that other companies use the same strategy to execute export orders for big American buyers such as Marmaxx, Cost-Plus and Pier 1 Import.

According to Mr. Ofoli, the owner of Kottage Originals, the main area of specialization of his company is the production of unique African furniture and other home décor accessories, the production of which is done in his company workshop in Accra where his contractors are assembled to undertake production activities. He claims his furniture is too expensive for the big American buyers. The company exports the furniture to a host of buyers in Italy through a buyer, Mysha, who consolidates the orders and ships to Italy. The company also supplies to other European buyers such as Art Works of Africa, UK; Made-in-Africa Collection in Germany; and Swahili Import in USA. The company equally values its local customers who are mainly expatriate workers in Ghana. The price tags on some of his products displayed at the company's showroom ranged from \$400 to \$900. Regarding the furniture, the company has few local competitors and Mr. Ofoli could count five companies that are into quality furniture production as his competitors.

Kottage Originals considers its creative African product designs as its strength and something that distinguishes the company from its competitors. When asked what the buyers like about his products, Mr. Ofoli replied: "I think it is the uniqueness. They are unique. You can go round the whole country you will see only one of this products (*pointing to a particular product in the course of the interview*). I don't produce too many pieces. You see this table console, that is about the third one and I can do this for this year and stop it. I couldn't replicate the original design. You hardly find two of this in my shop". Mr. Ofoli strictly protects his designs from being copied and the centralization of the furniture production within his company's workshop is actually meant to achieve this purpose.

Source: Field interviews 2007

4.5.4 Large-scale Exporters/Factories

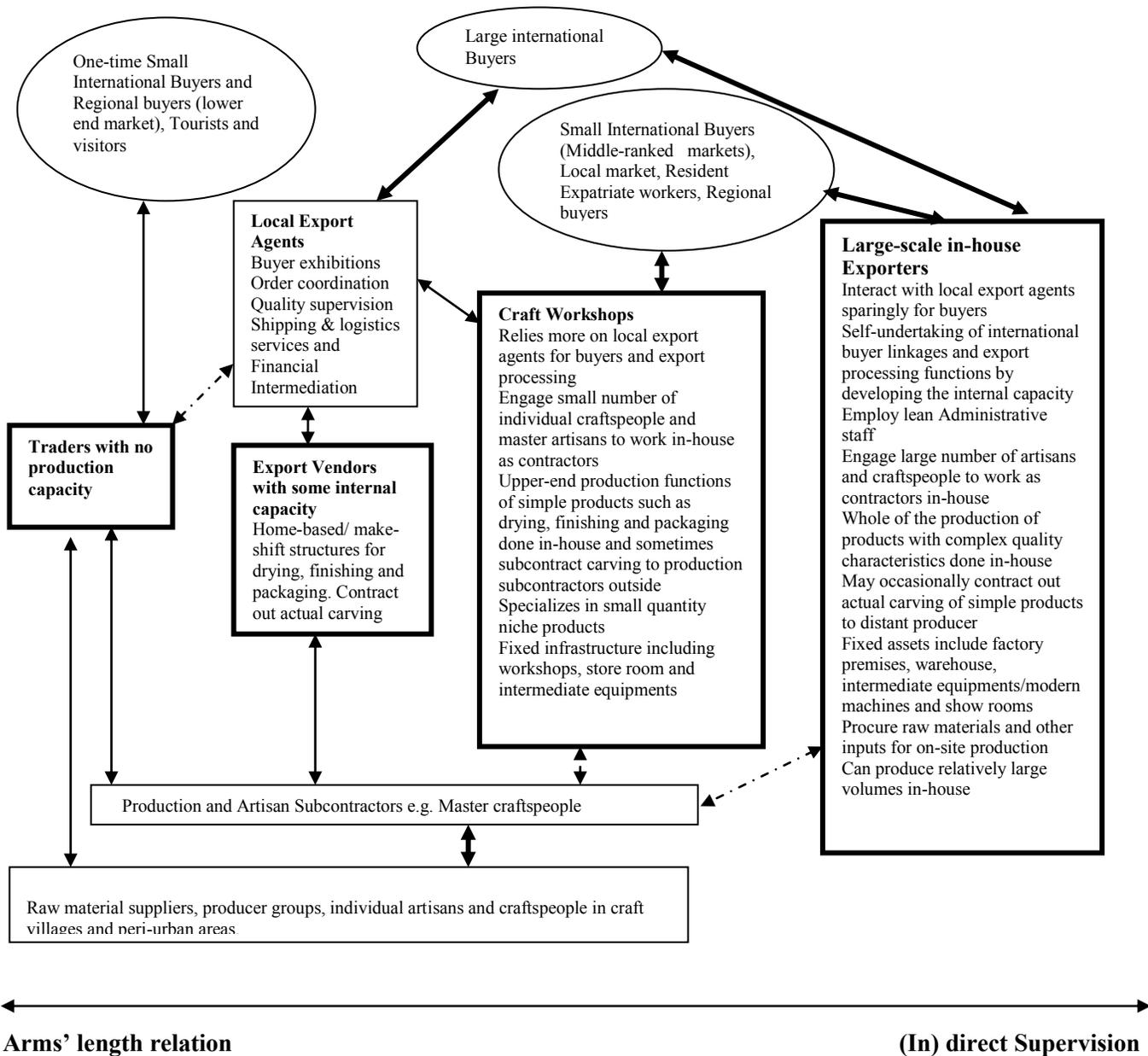
The craft factories in one sense are similar to the craft workshops in that they have integrated most of the production processes in-house. In another sense, they are different

because they are able to execute high volume export orders using intermediate equipment or modern machines. In addition to production in-house, these exporters occasionally subcontract early stages of the production processes of relatively simple products to independent artisan subcontractors. They produce to meet rigid cost, quality and volume requirements. The large-scale enterprises produce a broad mix of products in large volumes including gift items, home accessories, traditional African figures and statuettes, traditional stools, drums and furniture. The products with less functionality dominate the products content of these in-house exporters but are of higher quality and finishing compare with the vendors with minimal production capabilities. Their functional products in terms of design and aesthetic beauty are less appealing compared with the craft workshops or the boutique producers. They have significantly weaned themselves off the services of the domestic export agents and have developed internal capacity to undertake their export and shipping arrangements. The exporters in this category have the capacity to execute orders from US\$100,000 to US\$500,000 per annum (e.g. Fritete and Tekura).

Figure 2 is an attempted pictorial representation of the Ghanaian craft export industry, which is conceptualized within the transaction cost framework presented in chapter two (fig.1). The bold boxes represent the various categories of the focal exporters in the craft industry; showing their internal production capacities and production functions. The vertical and diagonal double-arrowed lines represent the forward and backward linkages. The thickness of the lines represents the intensity of the business interactions between the actors. The broken arrows signify occasional interactions. The long horizontal double-arrowed line represents the continuum on the transaction costs axis. The traders are

engaged in trade transactions that are synonymous with the auction regime characterized by one-off interaction and price jostling. This is followed by the export vendors who possess minimal internal production capacity and predominantly rely on subcontracting relations to execute export orders. At the extreme right of the diagram are the exporters in the category of craft workshop and large-scale producers whose transaction regimes correspond to “in-house” subcontracting, which is not specifically represented in the transaction cost framework conceptualized by Knorringa (fig.1). The inside contracting regime as practiced by the Ghanaian exporters is more rigid than the traditional subcontracting relations but less rigid than the vertically integrated firm. It occupies a space that is the intersection of the subcontracting, network and direct control regimes depicted in fig 1.

MAPPING THE GHANAIAAN CRAFT EXPORT CHAIN



(Fig 2, Constructed From Fieldwork Data)

4.6 Conclusion

The discussion in this chapter centred around general background information on the Ghanaian non-traditional export sector as well as specific information on the craft export subsector. For a century, Ghana did not register any significant change in export revenue as well as the components of the export sector. The government of Ghana realizing this unacceptable trend intensified its activist role as part of SAP to diversify the export sector through the promotion of non-traditional exports. Fiscal incentives and initiatives to strengthen meso-level trade support institution were designed to boost the export of non-traditional products. The reality is that the good intentions of the government of Ghana have not sufficiently been translated into removing constraints facing the NTE sector at the meso and micro levels. The craft exporters benefitted from government buyer linkages programmes in the early years of the industry.

The craft villages with historical links to Ashanti culture remain important “workshops” for the production of crafts for the domestic, tourist and export markets but the geography of the production sites has change; new centres of production have emerged in peri-urban areas that had no historical links with craft production. The craftsmen from the craft villages operate as production subcontractors either from their village workshops or may be contracted to produce from the production workshops of their hirers in the urban centres. Different agents such as traders, export agents and exporters based in the cities i.e. Kumasi and Accra assumed dominant roles in the organization of craft production for export. The roles of these actors occupying specific links in the craft commodity chains influence the flow of craft products from the artisans operating in the craft villages to the final consumers in the West. The majority of these agents have no social or historical

relationships with the craft villages, unlike the craftspeople who are bonded together by a common cultural identities and family ties in the craft villages. This has implications for the nature of the relationships existing between, for instance, the artisan subcontractors and the export agents/exporters, which take the form of commercial relationships often characterized by opportunism (see empirical analysis in the next chapter).

The development of the industry in the post-SAP era is driven largely by foreign buyers, which has led to the spontaneous emergence of local private actors to fill coordination gaps in the industry. The exporters who are singled out as focal enterprises for the purpose of this study are the entrepreneurs who are motivated by profit to take risks and also play pivotal role in coordinating craft production for export. These exporters are not uniform; they are segmented according to their capacity base, the market segment or buyer and the product type. The next chapter looks at the contractual relations between these focal enterprises and the other private actors in the craft industry. The analysis looks at the relationships between the exporters and their trading partners to include subcontracting and inside-contracting and their differing strengths in enabling the exporters to overcome their production constrains and export market requirements. This is preceded with a discussion on the local market risks, uncertain production environment and export market forces that affect the activities of the exporters.

CHAPTER FIVE

COMPETITIVE AND IMPERFECT PRODUCTION ENVIRONMENTS OF THE CRAFT EXPORT SECTOR AND SUBCONTRACTUAL RELATIONS

5.1 Introduction

This chapter looks at the extent to which reliance on subcontracting relations enable the craft exporters to overcome microeconomic and environmental constraints to production for export. The chapter is structured around two main themes. The first is concerned with the presentation of local microeconomic and socio-cultural factors, international competition and end market forces impinging on the activities of the exporters. Biggs et al. (1994) summed up the coordination challenges that the Ghanaian craft export industry faced during the embryonic stage of the industry's development to include:

- the difficulty of accurately estimating the production capabilities of far-flung artisans in order to avoid over committing on quantities and timing; for cultural and other indigenous practices could interrupt production schedules;
- managing the quality standards applied to each item produced by workers who are unaccustomed to such rigid specifications on colour, measurement and consistency of design.

The second looks at market coordination via subcontracting relations and informal institutional arrangements, which are adopted by the exporters in response to addressing some of the constraints placed on them by the uncertain local economic environment and external market forces. On one hand, the organizational paths adopted by the exporters are a response to their attempt to overcome external market requirements and local specific supply-side constraints. On the other hand, the scope of coordination of craft production for export via subcontractual relations and other informal mechanism is constrained by other forms of market failures and imperfections. Capacity constraints,

lack of access to relevant market information, opportunistic risks and socio-cultural practices are the domestic factors that impede the ability of the exporters to meet market requirements. Section 5.2 follows the introductory section with the analysis of competition from Asia. Section 5.3 looks at the microeconomic environment and supply-side constraints to production. Section 5.4 is about subcontracting relationship between export intermediaries and the exporters and the benefits that are derived from these relationships. Section 5.5 concludes the chapter.

5.2 International Competition from Asia

International competition from Asia had had the implications of putting some Ghanaian craft producers out of business while at the same time forcing other producers to improve their production practices and product quality in order to be competitive. Not only have these countries succeeded in copying typical Ghanaian designs and mass producing them but are also able to produce high quality products with good finishing at lower cost than their Ghanaian competitors, a processes which is gradually eroding the competitive advantage of the Ghanaian craft exporters. The Ghanaian exporters increasingly face the challenge of producing authentic craft products efficiently to reduce production cost in order to be able to compete favourably in the international market. Konadu-Agyemang and Adanu (2003) for instance have observed the success of Korean firms in mass producing Ghanaian craft designs and selling them in the international market at much lower prices. They queried whether Ghanaian producers can turn some of their art forms into mechanized mass products and compete with the Asian countries.

First, some of the small-scale producers are increasingly being squeezed out of the export market because of the superior finishing and the lower prices of the products by the Asian producers. Current trends, however, show that consumers are getting fed-up with the mass-produced African craft products from China and buyers are responding to this by shifting their procurement strategy to source of origin⁶. Jenkins and Edward (2006) in their analysis of the economic impact of China and India on the economies of Sub-Saharan Africa observed the indirect competitive pressures from these Asian countries on African exports in the international market. When some of the exporters were asked about the challenges they face in the export market, they frequently mentioned competition from Asia, especially China, as their main source of worry as evident in the quotes below:

The Chinese people are our main competitors...we produce mirror frames and the Chinese also sell similar things to these American buyers and they sell them so cheap that we cannot compete... (L'Afrique Concept)

I think the second issue is the competition from the Far East. You may for instance have an Akuaba doll, a typical traditional African/Ghanaian product produced by Taiwanese and sometimes whether we like it or not these people have better finishing than we have...when it comes to modernisation, they have the machinery, although is hand-made, they do a lot of finishing with machines...(Getrade).

The buyers can buy a mask in China for \$2 or even \$1 but the same quality and even better quality... well, the issue of handcrafting, which makes us distinct and unique is losing out; because most of our products are for the open market and some of them they fix the "made-in-Ghana" labels on them...(Afripech).

I have seen Akuaba dolls produced in Chinese factories and they are made from plastics but they look better than ebony wood and they are being sold everywhere. I have seen Vietnamese baskets labeled Bolga Basket... (Adu Mensah)

⁶ Chain Store Age, June 22, 2007.

Second the Asian competition is inducing some of the local producers to adjust their production practices and capacities in the bid to match the quality product finishing from the Asian producers. In the face of competitive pressures from Asia, some of the Ghanaian producers interviewed believed that their competitive strength comes from product “origin and authenticity” and what they needed to do in order to compete favourably was to improve product quality and finishing.

The keen competition among the global buyers has consequently led to the depressing of prices in the international market. Some commentators have observed that large U.S retailers and buyers of craft products operate in markets with extreme price competitiveness (Biggs et al.1994). A review of retail bulletins⁷ in the US showed intense competition and losses among the major retailers or the buyers of Ghanaian craft. The dipping of prices that follows are, in turn, passed on along the chain to the producers upstream. Price negotiation with U.S retailers is therefore crucial to achieving some reasonable margins within the context of global price depression and competition. This places additional responsibility on the exporters to understand all elements of their production cost to position them to be able to negotiate effectively with the buyers. The impression gleaned from the interviews suggests that price undercutting is also endemic in the craft industry. A respondent recounted an instance where a particular exporter quoted \$16 for a product that could cost twice that amount to produce, all in the bid to out-compete rivals in procuring orders. The export agent in this case had to step in and negotiate with the buyer to secured \$32 for the same product but at this price the exporter in question failed to execute the export order successfully. Some of the exporters argued

⁷Chain Store Age May 25 and June, Home Channel News, June 2007, DNL Retailing today Nov.22 2006.

that when those individual exporters fail to execute their orders, it is the reputation of the whole Ghanaian craft industry that suffers and therefore argue for a regulatory mechanism potentially through the trade association to ensure that new entrants into the industry do have some basic understanding of export practices and product pricing.

5.3 Imperfect Environment of Craft Export Production

The reality pertaining to the craft industry is that most of the artisan producers and the craftspeople are unaccustomed to the stringent export market requirements relating to product quality dimensions such as colour, size, health and safety, labeling and packaging. The independent artisans and craftspeople who are subcontracted to execute export orders very often do not appreciate the consequences of non-compliance to buyers' standards and product specifications due to attitudinal and cultural factors. They are also ill-equipped technically to respond to the export market demands and also lack the relevant market information to help design sellable products.

5.3.1 Lack of Access to Market Information by Artisan Subcontractors

It is often said that the Western market is a buyers' market and that to succeed in the export market demands that the producers and exporters adhere to complex market requirements pertaining to large order volumes, stringent product specifications, quality standards and tight delivery timelines. These requirements present unique challenges to the majority of the indigenous Ghanaian artisans and producers directly involved in the actual production process. The artisans generally lack information regarding buyer

specifications, product standards and products that are in demand. The quote below exemplifies the challenge of accessing the appropriate market information by the indigenous artisans in order to come out with product designs that meet the tastes and preferences of international buyers. Kofi is an itinerant master artisan from Foase; a craft village 10km from Kumasi who at the time of the interview was executing orders as a subcontractor for an export vendor in a suburban area of Accra. This is what Kofi had to say regarding the problem of access to export market information relevant to product development:

...We don't often know what the buyers want when they come to the exhibitions so we use our imagination to create designs for them. When the buyers come they complain that the designs we present to the exhibitions they still have some in stock. But we hardly get to know whether those products have been bought or not. We produce almost similar products with little modifications. So when they come they don't select those items that are similar to those they have on stock...

The conversation continued and Kofi was asked how he thinks this information problem could be resolved so as to avoid repeating designs the buyers have in stock. He pointed to the export vendors and the traders as actors who could help bridge this information gap. But he was also aware of the attempt by the export agents to sometimes frustrate any direct contact between the export vendors and the international buyers:

I think it is the dealers that have to interact or communicate with the buyers and ask them what particular products that they want. I think the buyers would tell them...in fact the [export agent] would not allow them to interact personally with the buyers...it is the [agent's] officials who are in the position to interact and talk to the buyers to know exactly what the buyers want...

So if the agents communicate with the buyers, don't they also channel the information acquired to you? (Interviewer)

Yes, they do communicate but it depends on your closeness with the agents and that you are the one who always executes his orders for him. He would for instance ask you to bring [a particular type of product] for him to present at the exhibition but he would not tell exactly what the buyer wants...sometimes they tell you the buyers are interested in “shadows” or “unity” or furniture or stool. You may not be able to tell the exact type of furniture or stool that they like or the type of “unity” they like. And the furniture or the stool you can’t tell if the buyer wants Adinkra symbol or what. So we create our own symbols to see if the buyers would select them...

5.3.2 Literacy and Technical Know-how of the Artisan Subcontractors

The technical know-how of the artisans and the craftspeople is mainly knowledge acquired through the traditional apprenticeship system. The know-how of the artisans is increasingly proving to be inadequate in meeting the buyers’ exacting quality standards and specifications. The majority of the artisan producers have no or minimal formal education, very conservative and less receptive to new ideas. The owner of Neocraft Ventures, which operates in the craft village of Ahwiaa, told of the advice that a Canadian consultant gave him and his colleague exporters to be innovative in order to be able to keep the craft industry going. This researcher then asked him whether he has the capability to innovate. His answer was that:

I am but there are some buyers in the US who are giants and their requirements and specifications are difficult to achieve. Recently one such buyer came to Ghana and out of about 120 exporters, only one exporter’s product suited them. Even that they had to sit with that exporter and made modifications. So you see, still in Ghana we are unable to meet their requirements. There was also one buyer; Target, they came and the standard they wanted was a bit difficult for us. I executed orders for them in all the years that they came to Ghana...you see the craft work face a lot of challenges because the education of our people is not all that good. For example if this product is to be cut at say 6×4 inches, the craftsman will cut it at 6.2× 3.8 inches and if you give it to Target, they won’t accept it. They prefer uniformity or consistency in the products. In some companies the products are passed through a single machine. But for us the products pass

through about 10 or 15 different carvers or hands. So at the end of the day, you get lots of variations in the quality... their standards were a bit difficult for us the Ghanaian producers. They (Target) would have come this year but we haven't heard from them again.

The training of craftsmen in production for export is considered important for bridging the knowledge/capability gaps between them and market requirements. The question is who should bear the cost of training? The exporters who hire the artisans are reluctant to invest in the training of the artisans for the reason that they can easily lose them to their competitors overnight. The exporters regard training of the artisans as a “public good” and therefore there is little private incentives to invest in artisans' training. An exporter had this to say in connection to his frustration over training the artisans and later losing them:

...my experience has been that each time that I try had to train them [artisans] and use them to produce that is when they always take advantage and decide to leave and make it on their own...so we eventually lose them. In fact, for some time it was very difficult for me to train new hands. I have come to realise that no matter what I do, I would lose them because these are guys are so ambitious...there have been instances where other exporters have approached me and suggested that we put resources together and train artisans and then put them in a pool so that we can share. There is also equal evidence that, I know ATAG has tried it before, they had training camps at Kokobeng and another one at Kpando but at the end of the day controlling them became difficult.. (Interview with Fritete, 2007).

It is, however, worthy to note that ATAG has been instrumental in helping to upgrade the skills of the local artisans. Wolff (2004) summarized ATAG's roles in training Ghanaian craft artisans and also helping them to develop new products that can compete successfully in local and global markets to include the following:

- ATAG trains field advisors who help to identify individuals who display entrepreneurial skills and invite them to participate in workshops in product development and best business practices;
- Artisans who demonstrate promise of success are sent to Aid to Artisans, USA for further training and opportunity to attend the American gift and craft shows. At the shows the artisans not only get a sense of market trends but also internalize ideas for adapting Ghanaian products to American market;
- Some of the artisans play entrepreneurial roles as leaders of artisan groups, while others become ATAG field advisors who work with producer artisans to encourage innovations in response to market trends. The advisors work both in village-based artisan groups and contemporary urban workshops by entrepreneurs in the cities.

5.3.3 Unstructured Export Production or Lack of Production Scheduling

Most of the independent artisan subcontractors are oblivious of the advantages of production scheduling. Their production activities are not structured according to any time schedule, even though the export market to which they produce for is time-sensitive. Exporters who produce for large volume buyers normally have three months to ship their order from the date the order contract is sealed. Speed is a necessary ingredient to success in the export market and delays are least tolerated by buyers;

Most of them [artisans] are illiterate and their understanding about time and action, production scheduling etc is very low. He doesn't see the reason why he should carve 10pieces today and then another 10pieces tomorrow and finish 100 pieces in 10days. They would decide to play around today and attempt to finish 100pieces tomorrow. Their production schedule is not well structured and so sometimes you go to the field and realise that they had just started producing at a time when you expect them to have gone far with production (Interview with Marcus, 2007).

5.3.4 Artisan Subcontractors Lack of Appropriate "Export culture"

As indicated earlier, time is a precious commodity in the export market. The buyers operate in a market that is highly seasonal and therefore have minimal tolerance for

delays in fulfilling orders. The business culture of indigenous producers permits “contractual flexibility” in local business transactions to insure parties against delays caused by infrastructural problems, input sourcing difficulties and other social obligations (Biggs et al. 1994; Fafchamps 1996). Fafchamps (1996) succinctly describes this problem as follows:

The need for contractual flexibility is ...probably accentuated in Ghana by the low level of economic development. ...the respect of contractual terms regarding consistent quality [and] rapid delivery ...is difficult. Markets for raw materials, intermediate goods, specialized services, and capital equipment are thin or nonexistent....Whenever technical difficulties or shortages of [inputs] arise, they cannot easily be circumvented and tend to ripple through downstream economic activities. These factors combine to create delivery [and] quality problems. Ghanaian businesses adapt to the situation by displaying a high degree of contractual flexibility (Fafchamps 1996, p444).

The lack of respect for time is attributed in part to socio-cultural factors. The artisans have very little appreciation for scheduling their production activities or even to work overtime in order to meet export deadlines. An exporter queried: *what is it about to meet deadlines that they have to work 16hours daily for two months because the autumn collection has been determined in America? What is that for?* (Interview with Wild Gecko, 2007). The incident of artisans stopping work halfway through production to perform farming activities, attend a funeral or other social functions is widespread. In this circumstance, export orders that are subcontracted to artisans in these communities are bound to suffer serious delay setbacks during the farming seasons.

The cultural stereotype of some craft communities is that it is the lazy people who go into

craft production. In other cases, it is considered a taboo for a section of the community dwellers to engage in the production of certain craft production. A key informant recounted the cultural impediment to craft export this way:

We undertook a contact promotion programme to the North America in 1990 and that took us to Atlanta Georgia to participate in the international house-ware show. That was the first exposure for Ghanaian craft companies abroad. After that show, we got some orders mainly for baskets and we were to do it for one of the biggest US companies for US\$ 600,000. Unfortunately three months into the production of a six month period order we had not done 5% of the orders. So when we got back to the buyer; Avon Cosmetics they offered to bring two consultants from Preston University to hold orientation workshops in Bolgatanga and its environs for 200 women in basket weaving (Interview with an informant, 2007).

The informant specifically attributed the initial difficulties to the execution of this order to local cultural barriers:

We didn't select men because at that time it was considered a taboo for men to be weaving baskets. So the fact was that when the women got the money to buy raw materials for commercial production, the husbands were not in favour of their wives getting that good money and it resulted in a lot of people beating their wives and taking the money from them (Interview with an informant, 2007).

The business culture that accepts excuses for delays in the execution of export orders is at odds or dichotomous to the demands of the export market. The work ethics of the artisan producers do not reflect the sense of urgency that is required by the export market. The attitudes of the local producers and their business practices are discordant with the culture of the export market that requires subcontractors to execute orders speedily and diligently to meet seasonal demands. These factors together limit the competitiveness of the Ghanaian craft export. Some of the stakeholders in the industry recognize this:

...If we continue to do things the way our forefathers did, we would really not be able to compete enough with these products coming from Asia (Getrade).

5.3.5 Export Risks, Opportunistic Behaviour and Supervision Difficulties

The main sources of risks identified in the craft export industry included what is referred to as buyers' "charge-backs", which emanate from non-compliance to product standards and specifications, penalties for delays in meeting delivery deadlines and the risk associated with artisans and craftspeople either absconding with advance payments, delays in executing export orders, and more importantly the fluctuations of demand in the export market. Most of the exporters are not able to predict the purchasing behaviours of the buyers nor are they able to determine the changing market trends, which are always in the state of flux. A buyer may change his sourcing strategy without giving prior notice.

In the context of falling product prices and dwindling margins, the exporters have very little room to gamble with any of these sources of transaction risks. There is the general sense of zero-tolerance for any of the above risks among the exporters; however, the large exporters in relative terms are better able to deal with these sources of risks. It would become evident later in the subsequent discussion in chapter six that the craft factories that have control over production, well-connected, possessing rich and multiple supplier and buyer base are better able to respond to changes in export demand and adapt to product changes fairly well than many of the small export vendors.

5.3.5.1 Export Risks

The artisans and the craftspeople contracted to execute export orders almost always receive advance payments from the exporters to execute their orders without having to make any substantial financial commitments in the production. The financial arrangements the exporters have with some private banks enable them to secure private loans, which are then advanced to the artisans and the craftspeople as working capital. The independent artisan subcontractors bear virtually no risks when it comes to the financing of production. The repayment of the loan is often tied to the receipt of payments from the buyers. What this means is that should there be huge buyers' "Charge-backs" and penalties resulting from the delivery of sub-standard products and delays, the exporters' margins may be eroded or they may incur losses which would make loan repayment difficult. Also some of the exporters indicated that they are made to pay 10% penalty of the order value if they fail to meet delivery deadlines. These risks are very much related to the work ethics and lack of professionalism on the part of the artisans and artisan subcontractors—behaviour which is at variance with the demands of the export market, lack of understanding of, and lack of production capability to meet, buyer specifications and quality standards. The two quotes below are views expressed by a leading local export agent and an exporter, which echo the risks and the liabilities the exporters face in the craft export industry:

The issue of late shipment and the issue of sub-standard goods and therefore the buyer coming back with charge-backs.... that would be one of the ways that the buyer punishes the vendor [exporter] for non adherence to quality and product specification If you look at the face value, the artisans and the craftspeople might not even have any sort of liability in this industry. There could be the liability of the items getting mouldy and the vendor is charged.....If there is a charge back, it doesn't go to the artisans; it instead goes to the vendors. It is the vendor who bears the risk; the artisans would have taken all his money. In this

particular situation the craftspeople have absolutely no risks for whatsoever. There are very few vendors who are at the same time craftsmen (Getrade).

Another respondent corroborated the risks involved in the export trade by recounting his own experience of having to pay charge-backs for shipping sub-standard products to a buyer:

Let me tell you one of my experiences. I executed some orders for export sometimes ago. The buyer came to tell us that the products were wet. They sent to us charge-backs for the reason that our products were wet. I had to pay US\$15000. Imagine that I have gone for a bank loan, the items produced and the craftspeople paid off and in the end I had to pay so much.... The export entails a lot of risks. Some of the vendors have run into serious debts and have become fugitives. I heard some of them have had their properties seized because they defaulted in paying their bank loans. So if you don't organise yourself well you can run into serious problems (Acarve Enterprise)

It is important to stress that the use of financial penalties for late delivery and sub-standard products are employed by the buyers, though harsh but effective, to elicit compliance. This is largely employed by the large international buyers who frequently seek impersonal relationships with the exporters. This is not the case with the small international buyers who establishes more informal and intensive relationships with the exporters.

The other risk pertaining to the export market is the situation whereby the buyers switch from sourcing products from the suppliers or the country as a whole. This mostly happens when there are changes in consumer tastes and preferences and when the suppliers fail to fulfill orders consistently to meet buyers' requirements or exogenous factors, for example,

the September 11th attacks in the US, the main source of market for Ghanaian craft products, caused demand to dip in 2001⁸.

5.3.5.2 Opportunistic Behaviour and Supervision

There are other forms of transaction risks that are local in nature and touch on lack of candour and contract indiscipline on the part of the independent artisans and craftspeople contracted by the exporters to execute production orders. These take the form of artisans taking advance payment and absconding with it or failing to deliver the required quality and quantity on time. Most of the exporters interviewed complained about these as major obstacles to organizing local production for export.

There were stories of artisans in the villages taking orders and running away with advance payments, using raw materials procured for them to execute orders of other clients. This is a human problem, which increases the cost of supervision and monitoring. Some of the exporters appoint agents, usually the master craftsmen, in the villages to supervise production on their behalf, yet the physical presence of the export vendors at the production sites to monitor production is considered important in ensuring that orders are executed speedily and at the required quantity and quality. The majority of exporters in Accra, for instance, frequently complained about the negative effects of the deceitful behaviours of the artisans on their businesses. These vendors in Accra frequently have to travel tens of kilometres to Kumasi and other craft producing communities, book hotel rooms for days and personally monitor the production process to ensure that their orders

⁸ See appendix 4 for a story carried by the Washington Post on the cascading impact of the global economic recession on the craft export industry in Ghana.

are executed to meet the required product specifications; all adding to the cost of transacting. These costs ultimately eat into their dwindling margins. Among the exporters interviewed, the export vendors were those who persistently complained about the high supervision costs. In the quote below it is evident that spatial proximity may help in terms of supervision to reduce deceit and meet other contractual obligations but in other cases, it may not necessarily be an antidote to dealing with supervision difficulties (see section 6.4). This interviewee who is the only exporter in the craft village, Foase, indicted how his geographical closeness to the craftsmen facilitates monitoring and enforcement unlike his Accra counterparts. He also recognizes the deceit on the part of the exporters who sometimes fail to fully finish payments for orders executed by the artisans and the craftspeople.

One of the problems that the vendors face with some of the craftsmen is that some of them are not reliable. You give them your work, they will take your money and in the process of executing your orders, they would stop your orders and take somebody's orders. That is why I was saying that the fact that I reside in this village is an advantage because the carver cannot take my money and run away with it because I monitor them. But if you are in Accra and you give orders to somebody in this village, how do you monitor the person. If you are not lucky he would cause you to incur a lot of debt. Some of the vendors also do not treat some of the carvers well. Some of the vendors sometimes fail to complete the order payments to the carvers. These two problems apply both to the carvers and the vendors. If you are a new entrant into the industry you may be deceived. Some of the carvers are not honest so are some of the vendors (Acarve enterprise).

5.3.6 Modest increase in Trade Volumes and the Risk of Deceit

The volumes of production orders that are subcontracted to the craftspeople in recent times are relatively large as well as the working capital required to execute production orders compared with orders that they used to get in the early days of the industry's development. The exporters are therefore very apprehensive to advance large sums of

monies to the independent artisans and craftspeople, especially, if they have doubts about their competence and cannot trust them to adhere to the contract terms. The export value of the industry during its formative years in the early 1990s was a little above \$1million but this figure for instance increased to over \$10million in early 2001. This increase has translated into relatively large transactions, raising the risks that the exporters are exposed to should their subcontracted artisans behaves opportunistically:

Now the monies involved are large and nobody would want to advance large sum of money to the artisans but the other problem is that when you give 50% advance payment it has been proven to be insufficient to enable them to finish the job so we end up paying the 100% before he even finishes the work and this actually increases the risks should the artisan abscond with your money (Celebate Services).

This does not in any way suggest that the other actors such as the export agents and the artisan subcontractors do not bear any risks in the industry. It is an issue, which borders on who makes direct investment in the actual production process and takes ownership of the final product and is therefore more likely to suffer from the risk of deceit. In most instances, it is the exporters who commit financial resources into the actual execution of export orders and take ownership of the final product. The artisan subcontractors may design the initial product samples and the export agents may facilitate financial resources for the exporters yet none of them lay claim to the ownership of the final products. However, the evidence also suggests that there are some export agents who combine intermediation roles with actual production and thus make direct investment by way of making advance payments to the artisan subcontractors to finance production. In this sense they are also more likely to suffer from losses from opportunistic artisan subcontractors.

5.4 Subcontracting Relations between Export Agents and Export Vendors/Artisan Subcontractors

This section analyses the subcontracting relationship between the export agents and the export vendors/craftspeople. The role of the export agents fills an important link between the myriad of export vendors/artisan subcontractors operating in peri-urban areas/villages and international buyers. The export agents provide market channels for the small-scale exporters to the international market; an activity that is almost impossible for majority of the individual export vendors to undertake. The analysis in this section looks at the benefits and constraints embedded in the relationships between the export agents and the export producers. Qualitative services such as product development/design, quality control and monitoring, financial intermediation, shipping and export processing, and the organization of trade exhibitions embedded in the subcontracting relationships are discussed. To the buyers, coordinating production from the disparate vendors and artisan in an unfamiliar terrain of high transaction costs and uncertainties is a cumbersome and expensive exercise. The role of the export agents significantly helps to take this burden off the shoulders of, especially, large volume international buyers. One significant theme in this analysis is that whilst the intermediary services provided by the export agents are crucial in enabling the small-scale exporters to enter the export market, the export agents lack the capacity to raise or improve on the current levels of their services that is required for greater competition. In addition, there are limited incentives to invest in creating high order services because of various forms of externality.

According to AFE (2004), two export agents handle about 40% of Ghanaian craft export sales for large US buyers. They charge commission on marketing, monitoring and the logistical services they provide to the exporters. There are other export agents who do not necessarily charge commission for the services rendered to the export producers but this cannot be regarded as altruistic since the cost is taken care of during price negotiations with the export vendors. The export agents provide these services to the export vendors who in turn pass them on to the small artisan subcontractors and the craftspeople. The intermediary functions of the export agents sometimes overlap with production activities of the export vendors. Some export agents have moved a step beyond brokering to undertake certain production functions such as finishing and packaging in-house.

Characteristically, each export agent has built a special relationship with groups of exporters. Some of the export agents have up to 100 different export vendors operating under their umbrella who in turn subcontract to hundreds of small artisan subcontractors. It is through these subcontracting arrangements that the services of the export agents trickle down to the other subcontractors and craftspeople. The export agents possess rich information about the trustworthiness of the export vendors and non-performing members are excluded from the group.

5.4.1 Organization of Trade Exhibitions and Buyer Contact Functions

The export agents organize local exhibitions for international buyers in Ghana. Export vendors take product samples from the artisans and present them at the fairs and when an order is secured, it is then subcontracted back to the artisan subcontractors and

craftspeople who designed the samples. The Ghanaian export agents/brokers have designed an exhibition model that enables the buyers to do one-stop-shopping of a variety of Ghanaian craft products.

The exhibition model of the Export Brokers

...Under the model they [export agents] have developed, they invite the large buyers to come to Ghana two times per year for 5-day product exhibition (they play an important role in communicating with these buyers and entice them to attend the exhibitions). During each visit they organize fifty to eighty “production export companies” to do a presentation of their products (usually at a well known facility). Part of this process is the selection and screening of companies to participate in the show (they will only choose those with a capacity to produce). The buyers go to the stands of each production company, select products, and negotiate prices directly with the owners of the company. Once they finish, all orders are consolidated with the export agent—who assumes responsibility for monitoring production, packaging and shipping...

Action for Enterprise & DFID (2004)

This arrangement fills an important gap in bringing the numerous export vendors together on one platform in order to meet the volume requirement of the large volume buyers. This exhibition platform is also responsive to the sourcing strategy of the large home product buyers who frequently seek to find a wide range of craft products from the small producers who individually do not have the capacity to produce the range of products and the volumes required by the buyers;

The large home product buyer is driven by the need to find a wide assortment of product. Individual firms are typically too small and narrow focused to provide a range of products. Home product buyers typically source from a number of producers. Home product buyers, thus shop in a country the way consumers shop in a department...but buyers are short of time and resources; they prefer to buy products from destinations that offer a wide range of potentially marketable products and cost of transportation low (Biggs et al. 1994, pp30-31)

The relationship, under this arrangement, between the exporters and the artisan subcontractors are reciprocal. When an order is secured from the buyers, through the

instrumentality of the agents, the exporters are then obliged to subcontract the orders to the artisans who designed the samples. It must be indicated that this relationship is under threat due to mistrust and dishonest behaviours on both sides of the relationship. The exporters may divert orders to other artisan subcontractors other than those who designed them. Likewise, artisan subcontractors may divert resources procured for them to execute orders of other client exporters.

The open bargaining of prices, whilst it promotes transparency, leads to a situation whereby the exporters try to out-compete each for orders and thereby undercut each other on prices. The buyers also take advantage of this situation and play the exporters against each other in order to beat down prices.

The current trend is that the export vendors do not interact directly with the large buyers let alone to negotiate prices with them at the exhibition hall. An export agent had this to say in connection to an exhibition he organized for the American buyer Cost-Plus; “...they [the buyers] just walked into the exhibition, selected whatever that they wanted, the buyers offered their prices...it was like a barter trade; no interaction but it was smooth”. In this situation of anonymous interaction, the export vendors miss out on qualitative information exchanges with the big international buyers.

In addition to local exhibitions, some exporters and the export agents occasionally take product samples from their subcontractors and present them at international trade fairs. To the majority of the vendors participating in international fairs, it is an expensive

venture and the prospects of generating orders from international buyers cannot always be assured. The export vendors, unlike the moderately well endowed craft factories and workshops, patronize mainly retail international fairs instead of the lucrative buyer fairs. The incentive to attend retail fairs is that it affords the export vendors the opportunity to sell their wares to meet their traveling expenses at the same time that they seek to attract orders from buyers. The general perception is that retail fairs are not the appropriate forum for attracting lucrative buyers and orders compared with buyers' fairs—attending buyers' fairs is however much more expensive and the risks are high. The ability of the few craft factories and workshops to attend international buyers' exhibitions in Europe is taken to be a measure of their capability to meet or match the requirements of the buyers.

Privately I have undertaken or attended exhibitions abroad but it is very expensive. Sometimes you may have to spend about US\$3000-4000. Though I learned but to be able to cover the expenses was difficult...In Germany we have what we call retail exhibition and buyer exhibition. We normally attend the retail exhibitions because we are not in the position to spend US\$4000 on buyer's exhibitions and at the end of the day don't get immediate financial returns. So we normally attend the retail exhibitions where we can sell some of our products and say get about US\$2000 to defray our travelling expenses (Neocraft Ventures).

This respondent recognized the benefits of attending international buyers' exhibitions and went further to explain the dynamics involved as follows;

But with the retail exhibition it is difficult to get orders unless you attend the buyer fairs, which we are not allowed to sell our wares; your sample may be selected but sometimes this happens after you have consecutively attended the fair for about three times. This year you will go, the second year you will, third year they would say that this producer has been here three times so if we give him orders he would be able to execute them. This most of us in Ghana cannot undertake. For buyers' fair I can say that about 5-6 exporters are able to participate. The bank also used to give us loans for the

fairs but because we were not getting the expected returns they advised us to stop (Neocraft ventures).

In addition to private efforts at organizing trade exhibitions locally and participating in international fairs, the government of Ghana occasionally sponsor the exporters to attend international fairs; very often with financial assistance from donors who pay for exhibition stands abroad. But this is not without difficulties as there were complaints of government officials favouring their friends and relatives who are not necessarily connected to the craft industry in any particular way to attend trade missions abroad who at the end of the exhibition would abscond and never return to Ghana.

...you realize that the support normally goes to the industry leaders and those of us in the field are left out...recently there was a fair at Japan. Those of us who are exporters did not get the chance to go to Japan. Instead those individuals who are not in the craft business got the chance because they had the money to pay. What I am saying is that they organized a fair through MOTI (Ministry of Trade and Industry) for craft exporters in Japan. The money they demanded before you could attend the fair, there was no way I could afford. So if you are connected to a big man, even though, you may not be a practitioner in the craft industry, you just have to look around and buy some craft products from the open market, pay your way through and join the group.

Another craft producer narrated a similar pattern of official under-hand dealings when it comes to government-sponsored trade missions abroad:

...recently at Mampong District Assembly, there was a guy who is not even a resident of the district, there was an exhibition in Switzerland, they requested this district to bring one representative from the craft business. What happened was that this guy came around got some samples and they bought ticket for him. In fact he never returned. These are some of the things that impede the progress of the business.

5.4.2 Shipping and Export Processing Functions

The individual export vendors lack the volumes or the economies of scale to undertake their own shipping arrangements in a more cost effective manner to international markets.

The export agents deal with these by assembling the executed orders from the various export vendors and consolidate them into single shipments to international destinations.

Getrade consolidates export orders from about seventy export vendors and ship them to big American buyer AMC/Marmaxx. The agent has a warehouse at Tema port where the export vendors who are scattered all over the country converge and present their finished products for inspection and on-ward shipment. The products from the various exporters go through a quality screening process at the port before they are packed into sea containers. During the boom era, the agent was consolidating export orders up to hundred 40-footer sea containers per annum. Currently, the agent consolidates about sixty 40-footer containers for shipment. Getrade prepares all the export documents and deals with freight forwarding and customs issues on behalf of the export vendors.

Source: Fieldwork interviews, 2007.

The big American retail and wholesale firms almost always source Ghanaian craft products through the local export agents. They source mainly simple and traditional decorative craft piece in large volumes. The exporters interviewed frequently made references to orders from these big international buyers as “mass products”—alluding to the large order volumes of relatively simple and unique traditional craft products for the large American buyers. This scale of production is beyond the capacities of the individual small artisans and artisan groups. The factory space that achieves this scale of production is constructed as a subcontracting arrangement encompassing interconnected enterprises specializing in some aspect of the craft production process, including the small producers from the craft villages such as Foase, Ahwiaa, Aburi, Asamang and Kokobeng to the export vendors and agents in Accra who undertake finishing, labeling, packaging, shipping and logistic functions to ensure that the products reach the shop floors of the retail stores such as T.K Maxx, Home Goods, Cost Plus and Pier 1 in the USA in good condition. If not the intermediary role that is being played by the export agents, the task of sourcing and coordinating products from small scale producer groups scattered all over

the country would have been very daunting for the buyers to undertake considering the fact the buyers have limited time to stay in a single country to shop for a range of products.

5.4.3 Quality Monitoring and Control

The export agents and some of the export vendors appoint supervisors; leaders of the craft producers or master craftspeople to monitor performance to ensure that the craftspeople and the artisans conform to quality standards, product specifications and to ensure timely delivery. Often the export vendors and the master craftspeople are given some training in quality management techniques and they in turn pass on the knowledge to their subordinate artisans and craftspeople. During the execution of orders, some of the agents and the export vendors personally visit the production sites to monitor the progress of production, though they do so infrequently because of time and cost constraints involved in frequent travels. The responsibility for quality assurance is often left on the shoulders of designated field supervisors who sometimes fail to strictly enforce adherence to quality standards and product specifications. The literacy levels of the majority of the artisans as indicated previously are very low and therefore adjusting to new quality demands and buyer specifications is always problematic. Even though it is stressful and costly to manage quality, some of the export vendors realize that meeting the buyers' quality demands enables them to get good price for their products and reduce the incidence of product rejection.

When the AMC buyers were experiencing a decline in the quality of Ghanaian craft products they employed quality inspector somewhere in 2002 to monitor and control the product quality of all the export vendors and producers who operate under the agent; Getrade. The quality inspector,

Mr. Marcus, prior to his employment by AMC buyers worked for the Centre of National Culture (now Art Centre) in charge of the craft sector. He holds a degree in industrial management and wood technology and received all his training in quality assurance from the AMC buyers.

Mr. Marcus undertakes two forms of quality inspection anytime that there are orders to be executed for the AMC buyers, which he called as DUPRO (Inspection done DURING PROduction) and FRAI (Final Random Inspection, which is done at the port). During the fulfillment of export orders, Mr. Marcus visits the sites of the exporters to assess their performance and where necessary offers corrective support to improve compliance to quality requirements and specifications.

At the port of exit, Mr. Marcus inspects every single piece that is brought to the port for shipment. He matches the products with a check-list written by the buyers detailing the product specifications such as colour, dimensions, design and price labeling that needs to be met by the export vendors. Also he randomly checks the moisture content of the products presented by the vendors using moisture tester. When he is satisfied with the quality and the specifications of the products, they are then packed into boxes and loaded into 40-footer sea containers for shipments.

Mr. Marcus recognizes the insufficiency of the reach and intensity of the quality management services that he offers to about seventy export vendors operating under Getrade/AMC. He indicated that in the final analysis the ultimate responsibility lies on the individual exporters to manage quality internally. Mr. Marcus had this to say in response to whether or not the service offered by AMC is enough: “I think in reality, AMC is doing its best. The main issue has to do with the individual factories. They would have to augment the control process because for AMC, if you are told to do things in a particular way and you deliver at fault or fall below the standard, your items would not be shipped...as far as AMC is concerned, it is a lot of work though, maybe an additional QA person would do. But I believe that the bulk of the responsibility or the job lies with the individual factories”.

Marcus makes a distinction between exporters who believe that they are selling an image and carving a niche for themselves through product quality and are pursuing this by instituting internal systems to improve quality compared with other exporters who are in the industry just to make quick money with no recourse to quality and image. In response to the new exigencies confronting the craft industry such as meeting the quality requirements of buyers, Getrade has trimmed down the number of export vendors operating under its umbrella from 120 to 70 aimed at getting rid of those exporters who are having difficulties adapting to the basic quality demands of the buyers.

Source: Fieldwork interview, 2007.

5.4.4 Product Development and Design

Product development and design remain critical to sustaining the craft export industry.

Almost all the exporters interviewed pointed to the Ghanaian design concepts and the authenticity of Ghanaian products as their competitive strengths. However, the range and

the product types have remained significantly unchanged over the years. An exporter had this to say regarding buyers' fatigue of the traditional craft products; "...the buyers have become saturated with some of these old designs; they need something new but we are also not able to create new designs" (Getrade). The quotation from a World Bank report brings to the fore two fundamental factors that impede product development. A gap exists in assembling relevant market information for developing new products and the lack of local capacity to adapt to changes in design trends even if the information is available (see the presentation in section 5.3.1 about the information problems that the artisan subcontractors often face).

Lack of design skills is a big handicap. Traditional, authentic designs are often enough to penetrate new markets, but functional ethnic designs (typically products of Western origin which have African decorative features) are needed to become a middle-ranked handicraft exporter. Buyers increasingly seek functional products which Ghanaian producers have difficulty designing and producing mainly because they are not familiar with Western lifestyle and the use of handicraft in Western homes... wood is often not sufficiently dry, hence, it can warp and crack, making it unsuited for most practical applications in Western markets. Even when managers are familiar with market requirements, they cannot transfer the information effectively to the local artisan producers" (2001, p 39).

There is an overarching need to create new product designs that do not narrowly target the African-focused market but also appeal to the broader Western market for sustainable growth and profitability. The literature reports of product development and design process whereby international buyers provide innovative ideas and design information to their suppliers or may directly develop new products in tandem with their suppliers. Unlike in Asia, the story of Africa and in this case Ghana is that the local exporters(vendors) and buyers seldom engage in intensive inter-personal trade

interactions that could serve as source of product design innovations(see the analysis of African markets and institutions under the theoretical chapter). The evidence gathered in the field clearly supports this claim especially when we consider the trading relationship between the export vendors and the big international buyers that source products through local export agents. The manager of one leading export agent had this to say in connection to the lack of direct upgrading support from international big buyers:

They [big international buyers] are not here to help you to develop your products. They can tell you I am interested in stools or this time around I think the market is good for drums so let have a lot of variety of drums or a lot of variety of stools. But they are not here to have time for you to develop your products. They have very few days to stay in this country and go so if you are talking about design, then it is another area where maybe you decide on how to get other people to come and design. Individually, the people might not be able to afford the design too (interview with Getrade 2007).

However, the evidence also points to a situation where certain type of exporters i.e. the visible craft workshops and the craft factories do maintain collaborative relationship with the international buyers, especially the small international buyers. The craft factories and workshops have accumulated over the years the reputation of having the capacity and competence to meet the standards and specifications of middle-ranked functional craft products. Thus the buyers are willing to deal directly with them. The qualitative relationship between the craft workshop/factories and the buyers will be returned to in the next chapter.

- Exporters are hesitant to invest in new product design as they fear that products will be quickly copied by local competitors. Some keep their “fresh” designs in-house as long as possible and only provide new designs to suppliers when production can no longer be done internally.
- Export companies limit their investment in product design as the return on investment is not always immediate.
- Most export companies lack professional design training.

- Some export companies consider product design to be a public service and therefore do not invest themselves.
- Most of the Ghanaian export companies do not attempt to innovate products on regular basis—while some of their international competitors come up with new collection developed by professional designers twice a year.

Source: AFE/DFID, 2004

Some of the exporters are professional designers who when given the right incentive conditions could frequently come up with new product designs to feed the craft industry. These professional designers even though seek to control their designs by producing in-house yet they find it difficult to protect their designs from being copied by their competitors and artisan subcontractors. Excessive design copying is a disincentive for future investment in innovative designs. Some of the professional designers interviewed were prepared to forgo actual production and focus solely on product designs, if their effort would be rewarded in financial terms. The potential for professional product designs exist in the industry for it to be harnessed given that there are sufficient economic incentives in place.

Robert Ashong and Del Boamong are both professional designers and about ten of their colleague exporters who produce similar products like them, are appalled by the extent to which their product designs are constantly being copied by their local and international competitors, which damages the competitiveness of the craft industry. According to Ashong, “the practice of people copying from others affects us because when a buyer sees this product at Wild Gecko and the same product at Unique ceramics, naturally, they get fed-up. So the way out is to motivate the designers”

They are willing to come up with new designs to feed the industry only if the other exporters are ready to pay a fee for their services. Mr. Ashong indicated that he has a lot of designs but do not have the capacity to produce them. He had this to say: “if somebody is ready to pay for my design services, I can sell those designs; we will enter into an agreement... help to develop samples. If you sell you pay me a commission of 2% on each one. This happens abroad but here people don’t understand”. Contract as an institutional tool to curtail design copying and provides the incentive for undertaking productive activity in this case by investing effort in design is absent. Ashong further attributes the problem to non-existence of copyright laws or if they exist they are not properly enforced: “They would rather copy because the copy right laws are not well implemented. It is only in the music industry that they are enforcing it but with the visual

arts...also textiles that are produced in China, there are anti-piracy people that go around arresting people in the market for selling pirated textiles from China. Because the textile companies have invested a lot in human resource training and equipment only for people to be ripping them off. They just copy the designs and send them through emails to companies in China, produce them and sell them at about a quarter of the price. So in our industry nobody is enforcing anything. So people are copying left, right and centre”.

Likewise, Del Boamong main concern is about dishonesty in the craft business: “I would prefer working as a designer. That is my background... So if I create and another person takes and I know that with every piece that is produced I am getting a certain amount on it, I don't have any problem with that. But the risk is that there is dishonesty in the business. If the first order comes say 10,000 pieces, he would say we had this order of 10,000, how about repeat orders, how about hybrid products?”

Source: Fieldwork interviews, 2007

It is important to note that the more technologically-centred benefits (i.e. quality management and product designs) unlike other market services are least addressed by the subcontracting arrangements between the export agents and the exporters due to negative market externality. A report by UNCTAD in 2007 highlighted similar market failures and imperfections that constrains the Ghanaian craft industry to include limited skills, lack of capacity on the part of the firms, lack of economic incentives to invest resources and time in developing new product designs as well as training of artisans.

By the early 2000s, it was evident that, although they were important, these services that were embedded in the transactions of the value chain were falling far short of achieving their full potential. In particular the more ‘technology-centred’ services were seriously constrained by a combination of limited skills in firms and limited incentives to invest in creating or hiring them—because of various forms of externality. This can be illustrated, for example, by the case of product design. Exporters sometimes passed on to their suppliers ideas about new product designs they receive from importers. However, this was a relatively ‘passive’ process’. The importers seldom had the design skills or time required to work with exporters on more purposeful product development. Also, besides lacking design capabilities, the exporters were hesitant to invest in new product designs because these would be rapidly copied by competitors.

Source: UNCTAD, 2007

A case that was often cited by many of the exporters interviewed was in the early 2000s when a key US buyer (Pier 1 import); stopped buying Ghanaian craft products and switched to China and other Asian countries. This led to a decline in the volume of export orders in the early 2000. The buyers' switch was partly attributed to the lack of new product designs. The Government of Ghana report on the craft industry, for example, attributed the looming crisis of the declining interest by major American buyer to field more in-country buying missions (Pier 1 One Import and AMC/MARMAX) to the lack of capacity by the exporters to come out with innovative products (PSI on craft, 2005). The extreme design copying in the absence of patenting laws is not only a disincentive for inducing private actors to come out with more innovative designs but may also be a source that discourages buyers from buying from the country as was indicated by this exporter:

One thing that makes Cost-Plus and other big buyers that offer better prices not to trade actively with Ghana is that here in Ghana we don't have copyright and patenting laws or brand the crafts we produce. If you design a product and give to a buyer at a higher price, somebody else would copy the design and sell it at a cheaper price to another buyer. At the end of the day the same product type somebody is selling at a low price and the other high price, though the quality may not be the same. That I believe cause the buyers to stop from buying from Ghana. I think if they should have exclusive rights to specific products, they would continue to come to Ghana because when they come to Ghana they always say that they don't want the things that have been sent to this or that particular buyer...sometimes our designs are one way. We don't create new designs. All come back to this issue of patenting. I have a background in rural art and sculpture from the university but if you spend time and effort to come out with new designs and after trading it once, twice somebody else picks it and that is that for me. (Katalvic Enterprise).

5.4.5 Financial Intermediation

The Ghanaian small craft exporters benefit from trade arrangement that enables them to access formal financial resources, thus setting them apart from many other small enterprises operating in the informal sector. Here the export agents and the National Association of Handicraft Exporters (NAHE) play crucial roles in this financial arrangement. The local private commercial bank, Prudential Bank, has been the major financier of the craft export since 1997. The bank has a special relationship with NAHE, the trading association that represent craft exporters in Ghana. For any craft exporter to qualify for a loan that individual must first be a registered member of the association and the association has to confirm to the bank the membership of the exporter as having a good standing as exporter.

Once the buyer places the export orders after the exhibitions, the export agent puts them together and present to the private bank to facilitate the acquisition of loans for the individual exporters. Even though the loan facilities are processed under the group name of the agents, the final responsibility of repayment solely lies with the individual exporters. The exporters are not required to provide physical collateral for any amount that is less than €100million. When the loan application is approved, it is then disbursed in tranches to the exporters at the prevailing interest rate. The bank initially lends out about 60%-70% of the order value to the exporters to begin production and the remaining percentage release to them towards the end of production. It is out of these loans that the exporters make advance payments to the craftspeople and the production subcontractors to pre-finance production.

When payment is received from the buyers, the bank then deducts the loan and other charges including the commission to be paid to the agents and the remainder deposited into the accounts of the individual exporters. For one leading export agent who consolidated export orders worth \$15.5million dollars between 2000 and 2007, the bank granted a loan of \$7million to the exporters operating under this agent.

The bank has also instituted certain “safeguards” against possible default or to minimize default in the absence of movable collateral. The bank charges a three percent fee on total loan amount to the exporters to use as an “insurance pool” against possible default (AFE/DFID, 2004). The major source of loan default comes about when the exporters fail to adhere to the buyers’ quality standards and specifications. The exporters may fail to repay their loans if their products fall below the required quality standards and specifications and therefore the buyer refusing to pay them. This makes effective monitoring to enforce compliance with buyers specification and quality standards critical for loan repayment.

There are limits to the use of intangible or soft safeguards as guarantees for securing high risk loans. The exporters are required by the bank, for instance, to provide movable collateral for any amount exceeding €100million. Many of the exporters with the ambitions to invest in production infrastructure and equipment in order to meet new and challenging buyer demands raised concerns about their inability to raise such investment capital from the banks for lack of collateral. It is estimated that about 80% of the craft exporters are small-scale enterprises whose capital base per annum rarely exceeds

US\$100,000 meaning that many of them cannot provide the needed collateral securities for long-term commercial loans (Government of Ghana/PSI on Craft, 2005).

Neither the export agent nor the trade association (i.e. NAHE) bears the risks of loan repayment, yet their reputation may be on the line if their members fail to repay loans—the loan repayment is solely bore by the exporters. The success by the export agents in facilitating future loans for its “members” is linked to how well their members performed in executing previous orders. The agents would have to monitor their members to ensure that they are producing exactly to specifications and sometimes confirm to the bank the stages of production its members have reached. By granting loans to the exporters under the umbrellas of the trade association and the export agents, the bank seeks to use group pressure to enforce compliance and loan repayment. The members feel that they are “in it together” and therefore encourage their colleagues to be always mindful to deliver according to the terms of the order agreement in order to be able to pay their loans. Besides, the bank maintains a closer and informal relationship with the exporters, which helps it to minimize transaction costs. In a response to a question about what is unique about the bank’s financing of the craft export sector to the extent to that the exporters continue to deal with it, the bank official had this to say: “There is a closer bond between us and it is more informal...some of them if you come and see us talking you may think that we are talking about family issues; that sort of closer relationship between us...the relationship to which we have reached at the moment, I would call it more or less risk free, and the risks are minimal”. This quote and the one below further reinforce how the commercial bank relies on inter-personal relations, group dynamics and reputation effects

as guarantees or intangible safeguards to minimize risks of loan defaults in the absence of other forms of physical collateral:

Every member in the group qualifies for loan. The only thing you need to do is to be a member of the group, obtain an order and their name confirmed by the agent or the group. Immediately they enter into the contract that is where the group pressure works. Because the group has certified that the applicant is a member and can deliver, when the other members are moving and the member in question is not doing well the group tries to impress upon the member to perform as well... Each member of the group bears its own risk but we have this group dynamism, because of the idea that they all belong to the same group and that if one does not perform it affects all the group members and you know how group pressure works. It is some sort of shared-responsibility; they wouldn't want their name to suffer. But when it comes to the repayment of the facility, it is individual risks executed under the umbrella of the export agents and the association (Interview with Prudential Bank Official, 2007).

Although the bank relies on the rich knowledge the export agents/trade association possess about the exporters, and their enforcing powers, it also undertakes its own monitoring and adopts other enforcement arrangement to ensure loan repayment. The producers and the exporters are scattered throughout the country and therefore monitoring them to ensure that they use the credit to execute their orders is time consuming and very expensive. However, the bank reckons it is less expensive to monitor than to recover loans from the small-scale exporters—for the loan recovery process is much more expensive and frustrating.

In the event of default (due to sub-standard products or unanticipated production cost overruns), the bank sometimes defer repayments subject to future export orders instead of adopting the conventional court actions to retrieve loans from the exporters—the reason

being that using court action is cumbersome and also it could strain its future relationship with the exporters. They only issue threats of court actions:

It is less expensive to monitor than to recover loans. The recovering process in Ghana is very difficult. You go to court and for about two years you would still be going to court. So if you have the means and the opportunity to monitor and achieve perfection than to recover it is better to do that...When they default for them we only threaten them with court actions and letters because going to court would be too difficult and we also don't want to break their backs...and the point is also [about] our security...when you take them to court one, two, three and somebody in the judiciary hints them that there is no collateral...they would be stubborn. By letters, communication we try to convince them to try and get orders and then deduct the loan in small amounts (interview with an official of Prudential bank, 2007).

Also embedded in the above quote is the idea that resolving commercial dispute using the court may not only be due to the financial cost and cumbersome bureaucratic process but also by the fact that the informal contractual relationship may make it difficult to resolve contractual disputes in legalistic manner. The court system requires litigants to tender in evidence of written agreements specifying the conditions of default and guarantees (i.e. physical collateral) that could be used to service default. The implication here is that even if the court system is effective, the use of informal contracting (contract lacking hard evidence) would discourage litigants to use the courts. In this instance, partners would continue to engage in on-going inter-personal discussions to resolve informal contract disputes (Lorenz, 2000).

5.4.6 Mistrust between Agents and Exporters

As much as these services provided by the export intermediaries enable many of the small-scale firms to participate in the international market, contrary evidence indicates that the intermediation role play by the export agents is far from ideal. The export vendors persistently complained about the situation where some officials of the export agents are unofficially engaging in export production. These officials who are well positioned in terms of access to important market information from buyers sometimes use this information to their advantage without passing them on to the other export vendors. Besides, repeat orders from the buyers are often withheld and executed by these officials (some of these officials have their small firms operating “underground”) without the knowledge of the rightful exporters who designed those products. The analogy below was used by an exporter to illustrate how the perceived mistrust in the industry stifles specialization in the industry:

I believe that the agents, exporters, producers, carvers and finishers should play their individual roles as such so that there would be transparency in the industry. We expect an agent to play the role of an agent. If you are a player we expect you to play the game as a player and if you are a referee, we expect you to play that role. But if you play the role of a player, a coach and a referee at the same time, it raises a lot of problems. There is a lot of mistrust in the system. The situation whereby one (this refers to the export vendors who are next to the export agents in a hierarchical order) gets information from the carvers whenever a buyer is visiting is not the best. Why do we hear the buyer’s visit from the carvers? It means that the referee (the export agents) is involved in the game because he goes to the carvers at the villages to create his samples (Celebate Services)

It is noteworthy that mistrust though impedes the subcontracting relationship between the export intermediaries and the exporters; it does not largely negate the positive

commercial role that is being played by the agents in linking many of the small exporters to the lower end of the export market. The issue here is more than mistrust. It also has the undertone of power relationships between the actors, which are shaped by who controls what resource along the production chain. The powerful position of the export agents in the local value chain is derived from the special relationships they have established with international buying agents and their relatively rich access to market knowledge. It is therefore not surprising that the agents closely guard this relationship to deprive the export producers (those without the capacity to undertake buyer search abroad) any direct interaction with buyers during in-country trade exhibitions. In the hierarchy of power relations, the international buyers are on top followed by the local agents. This is how one official of an export agent constructed the power relationships along the Ghanaian craft chain:

...these are the issues that we have looked at and talked to the buyer about, but the relationship is like master-servant relationship. If you talk too much the buyer would say I am not coming [back to buy again], so we...in fact what the [agent] has actually tried to do is to dance to the tune of the buyer. So for 10 years it has been so...let me say it in this way. There is this chain. You look at the buyer at the top, then comes [the agents] and the export vendors; the two are tied together because [the agent] doesn't have a say in whatever the buyer is giving the exporter (apparently referring to prices buyers offer). But from the exporters to the artisans the chain is broken...the artisans have more power than the export vendors...so you have the export vendors in there with less power even though they come next after [the agent]...

In the view of this interviewee, in the natural sequence of things, the artisan subcontractors at the bottom of the chain should wedge less power than the export vendors but the opposite is the case in this instance. The strong bargaining power of the artisan subcontractors in the chain is attributed to the fact that they possess unique artisanal

skills, which majority of the export vendors does not have. This “broken chain” between the export vendors and the artisan subcontractors makes it difficult for the former to control the latter with implications for enforcement of contract obligations.

5.5 Conclusion

The object of this chapter has been to highlight the external market forces and local economic and environmental conditions, which influence the general performance of the craft export industries and the subcontracting relations/informal mechanisms deployed by the exporters in coordinating craft production for export. On the global front, the Asian countries have succeeded in copying Ghanaian products and mass produce at high quality and finishing thereby pushing the frontiers of competition from price to issues of quality. These coupled with buyers’ specifications and requirements place competitive pressures on the local exporters to adjust organizationally and materially in order to stay afloat in the export market. Factors pertaining to the local environment also present unique set of challenges to the exporters. The artisan subcontractors often lack the technical capacity to execute orders to meet the required buyers’ demands. Unstructured production schedules, socio-cultural factors and the lack of understanding of export culture on the part of many local producers could cause undue delays in executing and shipping orders. Also endemic in the local environment is the risk of opportunism that the exporters have to grapple with in their transactions with the artisan subcontractors. The relative increase in the volume of trade makes the threat of opportunistic behaviour and supervision even more costly. Through subcontracting relationship with export agents and artisan

producers, the export vendors are able to access certain critical resources, which they would have otherwise found it difficult to generate internally such as working capital, labour and market information.

Many of the exporters described in chapter 4 as “export vendors” depend predominately on the export agents for market access and other trade intermediation services such as quality inspection, shipping and export processing services. This enables the numerous export vendors to overcome their own capacity limitation to generate some of these activities by themselves. However, the subcontracting arrangement via the export agents are restricted to low-order activities regarding quality management and product development; factors considered critical for greater success in the export markets. The export agents are less enthused to invest in product development and design either because they do not have the skills and the capacity to undertake those activities or due to negative market externalities. The export agents consider product development and design as “public good” because of the lack of excludability to the use of these activities and the fact that it is difficult for the export agents to prevent other actors in the industry from free riding. Specialized firms that provide quality management and product development services are not popular phenomenon in Ghana. ATAG can expand its third party service provision on a fee-paying basis to the artisans since its dependence on donor support makes it difficult to provide such services in a consistent manner.

The other limitation regarding the marriage between the export agents and the vendors is that, while informal mechanisms are used as intangible safeguards to minimize the risks

of loan defaults, it is however not enough to enable the export vendors to secure long-term loan for capital investment to meet more difficult production challenges. The banks always demand formal and movable guarantees, which the majority of the small-scale export vendors do not possess thus limiting their prospect of improving their production capacity for greater success. The lack of finance for capital investment tends to confine majority of the exporters to simple and traditional products, which are sellable at the low-end of the export market. This implies that intangible assets or informal systems are not sufficient to insulate the banks against high risk loans.

The subcontracting relations both with the local artisan producers and the export agents have been instrumental in enabling the exporter to integrate into the export market. However, these relationships are increasingly being undermined by opportunism, mistrust, cultural constraints and capacity difficulties; factors that make it difficult for the export vendors to meet the requirements of the export market. Trust as important prerequisite for sustaining subcontracting relations for coordinating production activities even for simple cultural products is being eroded through opportunism and lack of contract discipline.

The next chapter discusses how some large-scale producers and craft workshops organize their production functions and seek to overcome some of these environmental uncertainties and production challenges through inside-contracting arrangement. The character of the inside-contracting as it pertains to the export industry and the motivations underlying this system is explored in detail in the next chapter.

CHAPTER SIX

INSIDE-CONTRACTING: “NEW” RESPONSE TO UNCERTAIN PRODUCTION ENVIRONMENT AND MARKET IMPERFECTIONS

6.1 Introduction

This chapter discusses the production strategy of the “in-house” craft exporters. The thrust of the discussion in the chapter is that the exporters with in-house facilities are relatively successful in meeting quality specifications, speed and volumes compared with the export vendors who mainly subcontract their production orders to outsiders. Noting that external subcontracting had been the main channel for coordinating craft production for export in the industry, partial production in-house (inside-contracting) is a “new” and modest response to the increases in the complexity of the export transactions, risks and uncertainties. It is an institutional arrangement that is adopted by the exporters to gain control over the production processes in order to reduce agency problems. In other words, the move to overcome coordination difficulties and extreme risks pertaining to the local environment and export market pressure are the motivations underlying the trend towards the *partial internalization* of production activities in-house by some of the craft exporters. Given the uncertain production environment and opportunistic risks, the loose market-like subcontracting arrangement seems a weak approach for organizing craft production for export. This production arrangement adopted by some of the exporters does not strictly fit into the typical vertical integration mode of production prescribed in the transaction cost literature. It is a *partial* in-house production arrangement in that the owner of the firm engages artisans on *contract basis* to produce inside his workshop or production premises instead of the more formalized employment relations. It is an

arrangement that mixes an *external subcontracting* regime where trust plays an important lubricating role and an *internal contracting* regime—in which the essence is to gain control over the production process in order to address the different exigencies of the domestic environment and export market requirements. Not only does this category of exporters maintain multiple relations with suppliers but also with international buyers. This characterization of the complexity of inside contracting strategy as adopted by exporters also demonstrates a change process where the arm's length subcontracting relation served as the basis for the development of the in-house contracting system.

6.2 Inside-Contracting Production Arrangement: Character and Dynamics

The historical accounts given by the in-house producers indicate that they began mainly as exporters who operated mainly as traders without any on-site production facilities and used to subcontract whole of production functions to independent artisans and craftspeople. This is a “new” mode of production i.e. from non-factory environment to a seeming in-situ factory production organization in the industry.

These exporters/producers have invested in in-house production facilities with some of them going a step further to mechanize certain stages of the production processes using modern or intermediate equipment. These producers are integrating upstream and downstream in the local production chain. The core area of activity of these exporters was to secure export orders from international buyers by participating in buyer exhibitions organised by the domestic export agents and subsequently subcontract them to the craftspeople in the craft villages that possess the artisanal skills. But now these exporters

are loosely integrating production functions in-house to the extent of undertaking their own shipping and export processing functions without having to rely on export agents.

They have organized production lines that mimic the discrete specialized activities performed by artisan groups in the craft villages. Each specialized activity, including carving, designing, finishing and packaging, is supervised by experienced and skilful group leaders or master artisans. Most often the masters who act as subcontractors negotiate the price of each piece to be produced with the owner of the enterprise and in turn pay the artisans working under them by the piece.

Some exporters who have on-site or in-house facilities have offended so many people. By getting the good craftsman to stay in-house you step on some toes. The guy was working for some other people and you have taken him, which means you deprive other people from utilizing the guy and that breeds bad feelings among the exporters (Celebrate Services).

Engaging the skilful artisans to produce from the premises of their hirers is not without controversy in the industry as depicted in the above quote. There is an indirect employment relation between the craftspeople/artisans and the enterprise owner. The owners provide the factory space, the equipment and the raw materials for the artisans to execute the orders. This is not to say that they have completely abandoned the use of simple tools; there are certain aspects of the production process such as the initial carving that continue to rely on the use of simple tools. Even though the craftspeople are independent contractors, producing within the confines of the factory or workshop space provided by the lead exporter enables him or her to closely monitor the artisans to ensure compliance with quality standards, product specification and prevent opportunistic risks.

The owners of the principal enterprises are not themselves artisans or craftspeople but are knowledgeable about the requirements of the export market and therefore transmit their acquired market information internally to the artisans they contract to work for them.

The narratives below are the stories of two leading craft exporters who were just traders but have developed their businesses to become successful in-house producers with a well organized production set-up; typical of the inside-contracting regime being discussed in this chapter. These narratives provide a prelude to the thematic discussion of the inside-contracting system as it relates to the craft industry. The narratives demonstrate the learning process and adaptability of the enterprises in question to changes in export market demand and local-specific challenges. The case firms; Tekura Enterprise and Fritete African Art Works together have the capacity to produce about US\$700,000 worth of export orders annually. The narratives are constructed based on information obtained from fieldwork interviews and secondary data sources (Webber et al. 2007).

Case: 1 Tekura Enterprise

The origins of the company: It is a craft export company that specializes in simple traditional craft products, home décor and furniture. Josephine Forson, the owner of Tekura Enterprise Ltd started her career as an employee with Aid to Artisan Ghana, an NGO that helps to build the capacity of craft businesses in Ghana. She carried with her the experience gained from, and the buyer contacts made at, ATAG to establish Tekura Enterprise Ltd in 2000. Tekura started as an export vendor with minimal on-site production capacity and initially relied entirely on individual subcontractors to execute her export orders. Josephine runs the company with her husband, who resigned as an account with Red Cross Society in 2003 to join the company. Tekura has about 44 craftspeople as subcontractors who operate from the company's production premises located in Adenta, a suburb in the outskirts of Accra. The company has over the years invested in machines such as band saws, mitre saw, planing equipment, drying oven etc. In addition, the company has a showroom and a warehouse where samples of various crafts products and finished products are displayed and stored respectively. According to Josephine, she occasionally subcontracts some of her traditional items to subcontractors to carve outside her production premises and the finishing, incisions, sanding and

polishing completed in-house. However, all the production processes relating to the high premium home décor and furniture are performed within the company's production premises in order to control quality. From modest export sales of \$35,000 in its embryonic stage, Tekura increased its export sales to \$180,000 in 2004, and \$200,000 in 2005. The year 2006 witness a decline in export sales because one of the company's big buyers did not place export orders.

Declining Margins due to demand changes and competition: Tekura began selling traditional animal and human figurines and masks to the high volume US buyer; Pier 1 Imports. Early year sales were good, which resulted in good margins. In the early years, a 12-inche wooden mask had an average sale price of \$8-9. However, in 2003, for almost a decade in sourcing craft products, Pier 1 began reducing sourcing from Ghana partly because its clients started developing interests in functional products and increasing disinterest in traditionally based ethnic craft products. It was also partly due to the fact that other retailers such TJ Maxx and Marshall's, which compete on price and had entered the Ghanaian market virtually out-competed Pier 1 Import in the US market for Ghanaian craft products on price. Order volumes began to decline in 2003 and buyers started to squeeze more margins from their orders. Masks that Tekura used to sell for \$8-9 in 2002 were later sold for an average price of \$3.50 by 2003.

Horizontal Collaboration to raise capacity to enter up-end market and meet increase in order volumes: In 2004, West African Trade Hub (WATH) linked Tekura and other exporters to the US retailer Target, Inc. Target was sourcing home décor products from Africa, Asia, Latin America and the Middle East for its "Global Bazaar". Target placed 27,000-piece order (US\$365,000) for Getrade Ghana Ltd, Fritete African Works and Tekura to produce for its Global Bazaar in 2004. Tekura was successful in producing some of the items ordered by Target, but there were equally other unique items that Tekura had no experience in producing. In the end Tekura was able to complete 70% of the 9000 order pieces due to capability problems. Likewise, Fritete also failed to fulfill his order completely. Regardless of this shortfall, Target expressed the willingness to place another order in 2005. In view of the capacity problems Tekura encountered in executing the previous orders, Tekura sought additional resources and capacity improvement in anticipation of the orders promised by Target in 2005. Tekura teamed up with Fritete (the other company, which failed to complete previous years orders but possesses reasonable production capacity), to form a joint venture; Premium Export. Also a German-based handicraft expert was brought in through the assistance of WATH to analyze the production systems of Tekura and helped implement some changes in the areas of building templates and jigs for woodcutting to reduce waste and ensure uniformity in size and also improving drying techniques of wood products to reduce warping, cracking and moulding during transit. Tekura secured loans through local financial institutions to make capital investments. Band and mitre saws were purchased between the first and second Target orders.

In 2005, Target returned with an order of 48,000 pieces to which Tekura was responsible for producing 13,000 pieces of items, including masks, wooden figurines, candle stands etc. The production difficulty encountered here was how to obtain the necessary funds to

finance these huge orders. Tekura had in previous occasions relied on an informal arrangement with a local private bank to secure loans to finance production but this time around the bank would not grant huge loan request without a solid guarantee. She lacked the collateral then but the joint ventureship with Fritete enabled her to obtain an Exim Guarantee (attracts 3% interest rate), which enable her to obtain private loans from local banks. The collaboration between Tekura and Fritete yielded good results. They were able to complete the orders at the required quality and quantity.

Changes in Buyers' Behaviour: As it pertained to Pier 1 Import, the tastes of Target customers changed and so Target responded by shifting its focus within its Global Bazaar product offerings from country of origin and artisan uniqueness to emphasis on affordability, colour theme, category and item dominance. Instead of the broad mix of product purchases, Target focused its 2006 African home décor purchases to woven baskets from women's groups in Ghana. Pier 1 imports returned to Ghana in August 2007 and Tekura is expected to secure orders. The return of Pier 1 is linked to the losses that the buyer has been incurring in recent years. Its new recruited buyers have been directed to purchase merchandise "that is more akin to Pier 1's historic roots rather than the modern craftsman approach the company dabbled in unsuccessfully"⁹ in sourcing from Asia. This shift in buying focus seemingly favours countries like Ghana where Pier 1 has traditionally been sourcing authentic African products.

Diversifying client base as a response to sporadic buyer switch: With the vacuum that was created by the loss of Target in 2006, Tekura, has learnt to anticipate the sporadic buying habits from large "big-box buyers" and now constantly seeks new niche markets. The big buyers can stop buying without giving any notice and so an exporter relying on a single big buyer faces the danger of going out of business if the buyer switches.

Tekura continues to produce and sell home décor item to Marmaxx and has sought to expand into other markets by joining a consortium of Ghanaian artisans and manufacturers called "living Ghana", which is comprised of 15 Ghanaian companies, and started by attending trade fairs in Berlin and also work with German designers to improve their product offerings. The consortium sells to the European market through a variety of German and Swiss boutiques. Tekura also teamed up with African Heritage Collection to launch exclusive, higher-value home décor products. In 2006, Tekura was selected as part of the Design Africa Initiative, sponsored by Trade Facilitation Office of Canada, to participate in the Montreal International Interior Design Show and the prospect of getting buyers from this show looks good.

In addition, Tekura sells to other smaller and niche market buyers such Swahili Imports and Bambolla both in USA. The order quantities from these buyers are small and may be up to US\$ 10,000. The benefit derives from these buyers is that they send down their designers to Ghana to work with Tekura to develop new product samples. When these buyers get orders for the samples they give them back to Tekura to produce. Unlike, many other exporters, Tekura do not have a problem communicating with the big buyers; however, the frustration that she sometimes faces is the bureaucratic channels that she has

⁹ Chain Store Age, June 22, 2007.

to go through in communicating with the buyers' Africa regional agents stationed in South Africa. Mrs. Forson believes that the direct communication and the visits to the production premises by the buyers are as a result of the confidence the buyers have in her company. She had this to say: "The buyers come down to us. They have agents in the country and when you are well organized they bring the buyer to your workplace. When the buyers come they see products that are different and they are excited and if they want some of them, they ask for some changes and if you are able to organize and quickly effect the changes they tend to feel more comfortable with you".

Seeking reputation through quality: Tekura believes she is not just selling products but also reputation and therefore do not compromise on quality. Apart from personally getting involved in quality control, payments done for work are tied to the level of quality achieved by the craftspeople. One of her big buyers; Marshall has a local quality control officer who visits her premises during production to undertake quality inspection; a process Tekura learns from.

Teaming up with Fritete allowed Tekura to take advantage of the economies of scale and the resources necessary to complete their orders with Target. As margins, continue to decline, Tekura needs to adapt to new production techniques and input sources to lower their costs. Tekura use wood from trees left lying in the forests as a result of reforestation. In an effort to improve their market position Tekura has continued to improve the designs of its home décor products to appeal to different tastes.

Case 2: Fritete African Art

The origins and company's profile: This Company is one of the pioneers in the craft industry. It was established in 1987 by Mr. Robert Ellis who started as a vendor or a collector of African Art works. Until he began collecting craft products, Mr. Ellis worked as an IT officer at Ghana's Drivers and Vehicle License Authority (DVLA). Fritete was initially established to produce and export crafts products, however, the company has acquired a new function as an export agent. The company has the capacity to produce \$500,000 worth of export orders annually. The company is sited at Agbpgba-Haatso, a suburb of Accra and it boasts of investment in modern machines, and other infrastructure including, storage facilities, production sheds, haulage vans, showrooms, drying ovens among others. The company produces and exports a wide range of craft products including documented African figurines and museum reproduction, traditional and contemporary furniture, mirrors, frames, musical instruments and the like. Its production space can accommodate 150 workers whom he engages on piece rate basis and also subcontract orders to hundreds of production subcontractors in the craft villages. The company negotiates the price of each piece with the artisans; this in most cases is done between the masters under whose direct supervision the craftspeople and the artisans work. Engaging the artisans on piece-rate basis enables the company to adjust to fluctuations in export orders. Mr. Ellis indicated that the company used to engage the artisans on permanent basis, even when there were no export orders, to produce for stock; in an attempt to fully utilize the artisans and not to lose them to its competitors. This was however discontinued because keeping product stocks always played into the hands of

the buyers to beat down prices and loans were also “locked up in the stocks”, which needed to be serviced (the storage rooms of a number of exporters visited by this researcher revealed huge piles of stocks of unpolished carved products). During off-seasons the company only keeps a handful of artisans in-house to create new product samples for trade exhibitions.

Learning about market trends through private/sponsored participation in international fairs: Mr. Ellis has participated in both local and very lucrative international trade fairs and missions. Between 1987 and 2007, Mr. Ellis participated in nine major international fairs in Europe. In a particular instance, he repeatedly participated in these fairs every year from 1999 to 2007¹⁰. In terms of fair participation, he stands out among all the craft exporters. Two decades ago, the craft industry was regarded by many Ghanaians as a cottage industry reserved for school drop-outs and as a pioneer craft exporter who always place emphasis on good product presentation, it was easy for him to catch the eyes of government authorities and be selected to participate in government and donor sponsored international fairs. Unlike many of the scale-scale export vendors, he does not primarily measure his success at the fairs by how much sales he makes, instead he goes to these international fairs with the prime objective to learn about trends in the export market, tests his new products, seek the views of the buyers and the consumers on pricing, finishing and presentation and the feedbacks incorporated into his final product designs. Mr Ellis always returns from international fairs with a dossier of information, which enable him to improve on his designs and product range. Fritete always seeks to diversify its product designs and the functionality of the products in line with trends in the export market.

According to Mr. Ellis, his first major exposure to international trade mission was somewhere in 1992, when he was selected among other companies by the Ghana Export Promotion Council through the sponsorship of the Commonwealth Secretariat to undertake trade mission to North America to explore the market for buyers. This happened at the stage in his company’s life when raising the money even for air ticket was a major hurdle for him. This mission, according to Mr. Ellis, was successful because in the end they were able to secure export orders from a major American buyer. The success of the trade mission to the North America became a springboard for him to sell his company for slots in future government sponsored international fairs.

Multiple clients from different countries: Fritete has been dealing with rich and multiple buyers. This, according Mr. Ellis, is the result of his approach to participations in international trade fairs. Fritete has been exporting almost to all the big US buyers including Cost-Plus World Market, Pier 1 Imports, Marmaxx, Target Corporation. The company also transacts or has transacted business with a number of buyers from countries such as Peru, Mexico, the Netherlands, Italy, Spain, Germany, Cyprus and Norway. Mr.

¹⁰ Ambiente fair, Germany from 1999 to 2007; Birmingham Spring Fair, 1999 and 2000; Bordeaux International trade fair, France 1989; AMK Berlin Trade fair, Germany 1990, 1991 and 1993; Import Shop, Berlin, Germany 1998-2003; Paris International trade fair, 1987-1990; Premier Trade fair, Germany 1995; Tendence Trade fair, Germany 1996, 1998 Trieste International trade fair, Italy.

Ellis indicated that orders from Germany where he plies most of his trade fair participation has been growing in recent years.

Functional upgrading and learning through intensive relationship with a big buyer: Fritete typifies a company that has upgraded its functions as craft producer by adding to its activities the role of an export agency. When Mr Ellis was approached by the American buyer; Cost Plus to be its local agent, he was initially reluctant to take up the offer because he felt he did not have enough experience and understanding of the operations of an export agent. Notwithstanding, his experience in production and exposure to the export market was considered enough initial prerequisites by the buyer to take up the new role as an export agent. His in-depth understanding of the needs of buyers and the investment he has made in production facilities were enough to convince the buyer of his capability to deliver as its local representative. The buyer also offered to give the company some assistance. This is how Mr Ellis expressed this concern: “the experience I had was in production and export and not agency work. These big buyers, they have different documentation issues that you need to understand. At the moment I am working with about 13 different desks and you have to be able to understand them. I have a buyer, assistant buyer, purchase order management team, changes team, shipping team, distribution team; all in the US who work with me. Sometimes when it becomes necessary we organize telephone conference where we can explain things to the understanding of two or three people. Then I didn’t understand those means of communication and I needed to understand so many things which were not within my abilities but they offered to give me guidance and direction. In fact as at now, most of the vendors went against most of the strict regulations and normally when you do that they slap you with charge-backs but because of the special dispensation to use this relationship as a learning platform for my agency we are normally given waivers”.

Fritete currently operates as an export agent and is in the process of reorganizing in order to cede the organization of actual production to another company; Treasures of Africa (owned by Tina the wife of Mr Ellis). Fritete is also the regional representative of Cost-Plus and coordinates export orders from Burkina Faso and other West African countries for the buyer.

Just when the company had started to do business with Cost Plus, Fritete was fortunate to get involved in a training programme organised for craft vendors on export guidelines by WATH. He received training on product development, order negotiations and executions, and export procedures including; packaging, labeling and post-shipping trust and confidence buildings with buyers. The knowledge gained at this training programme was in turn imparted to most of the craftspeople and artisans working under Fritete; majority of whom do not have formal education.

Informal-formal credit arrangements with private bank to meet large export orders: According to Fritete, the first exhibition organized for his new buyer in Accra was a great success. The obstacle that immediately confronted Fritete and its vendors was the lack of finance needed to execute their export orders. When the orders for Fritete and its vendors

were finally sealed by the buyer, the company used its influence to facilitate bank loans for the vendors. The order volumes were huge and as such required huge working capital; the kind of money the private bank i.e. Prudential Bank, was reluctant to advance to the vendors without a secure guarantee and as it is the case with many small enterprises, the vendors lacked the requisite physical collateral as guarantee to back their loan requests¹¹. So Fritete had to design a monitoring and a guarantee system to ensure full loan repayment. First, Fritete visited the production sites of the vendor applicants to assess their levels of preparedness or the level of investment that they have made in their production infrastructure. Based on this assessment, the company then recommended to the bank to advance the loans to the vendor that is commensurate to the value of the vendor's production infrastructure. The loan disbursement was done in tranches and the initial loan installment was made to commensurate how much the vendors have invested in production facilities. Fritete took the responsibility to monitor the recipients and reported back to the bank on the progress of work of the individual vendors. Further loan disbursement was based on the performance of the individual vendors in successfully using the loan to execute the previous stages in the production process. Mr. Ellis had this to say in this connection: "The bank was giving the money in tranches, so if it gives €50million to the vendor, I should be able to report back to the bank to convince them that the money has actually been used in production and that the individual is on track and I should also be able to tell how much more money the individual needs or that the individual is having problems with production and that the bank should slow down on monies to that individual". This arrangement, according to Fritete, was so effective that they succeeded in full repayment to the bank. Following from this, the bank has decided not to deal directly with the individual producers or vendors but instead write all loan agreements for the export orders in the name of a subsidiary company of Fritete. As a key exporter with a better understanding of the industry, the bank was confident Fritete was well positioned to know who the real performers in the industry are and is less likely to advance monies to under-performing producers or vendors. Making the company to bear the foremost risks was also meant to induce Fritete to further tighten the monitoring of its subcontractors to ensure that its vendors are always on track. To the bank, dealing with an umbrella exporter such as Fritete meant a reduction in transaction cost (monitoring and enforcement) in dealing with myriad of producers or vendors who are scattered throughout the country and also overcame the information problem regarding the ability of the exporters to execute orders diligently.

Internal quality control checks to meet quality requirements: Mr. Ellis understands the changes that have taken place in the craft export industry over the years in terms of consumers' tastes, product quality standards and the need to respond to these changes appropriately in order to stay in business. With this understanding, Fritete has responded to these changes by investing in modern machines, which enables him to achieve consistency in product quality and also ensures that product quality is controlled right from production to packaging. At the start of the production of each order, the company internally transmits information on product specifications to its craftspeople and artisans and design jigs and templates for achieving the required product sizes and dimensions.

¹¹ The interviewee mentioned that some of his vendors needed financial request or loan in excess of €300million from the private bank, an amount that requires fixed collateral by the bank.

Every craftsman is obliged to ensure that each product produced fits very well into the jigs before they can move to the next stage. According to Mr. Ellis the leaders of the craftspeople acts as supervisors who check product quality and enforce compliance at every stage of the production process. Crafted items are then taken to the drying base for oven drying. Mr. Ellis prefers oven drying to air drying or kiln drying because it is quick and enables him to meet deadlines. On the issue of product quality this how he puts it; “the quality issue is not the concern of the manager and the supervisors only, it is as well the concern of the individual producers and artisans from the beginning to the end of production”. He told of his experience of some difficulties he encountered in executing export orders for Target Corporation because of some lapses in quality control during the production process; the quality control personnel engaged by Target undertook the quality checks at the port of exit instead of during production. He felt that checking product quality at the Port was flawed and therefore refused to allow that arrangement to go on. The buyer agreed to allow the officer to offer the quality control services during production. This according to Mr. Ellis made the quality control officer to appreciate some of the practical challenges that they often face during production.

6.2.1 Bipolar Contractual Arrangement

The fact that these producers are building internal capacity and integrating production activities in-house does not in any way suggests complete abandonment of their traditional subcontracting to independent artisans operating in the craft villages. The craft factories and workshops combine *internal contracting* within their production premises with *external subcontracting* to independent artisan subcontractors operating outside their production premises. This approach can perhaps be referred to as a “Bipolar” contractual or production strategy whereby the entrepreneurs decide to outsource certain activities to their *trusted* independent subcontractors and at the same time decide to perform some other activities in-house. The decision to adopt internal or external contracting is influenced by the product type or the complexity of the product, issues of buyer standards and specifications, order volumes, delivery deadlines, the extent of exposure to opportunistic behaviour and whether the artisan subcontractors can be trusted to execute the orders diligently. The relatively complex and difficult to produce products are hardly

outsourced to independent artisans operating from the craft villages. Where they choose to contract out externally, it is normally the simple or the traditional crafts, which are produced for the mass market but where order volumes are huge and quality could easily be compromised, production is then centralized in-house to enforce compliance to product quality and specification. Also in-house production has the potential of limiting the range and variety of products, which are often required by large international buyers. The motive to subcontract externally, in addition to in-house production, is also meant to ensure that they are able to broaden the base of their product range.

6.2.2 Trust and Subcontracting relationship with Artisan Subcontractors

These exporters possessing in-house production capacity were relatively comfortable in subcontracting their simple craft orders to their distance subcontractors and able to assemble skilful artisans to produce from their production premises with relative ease. On the contrary, the vendors without in-house production facilities, especially those in Accra, who specializes in the same simple and traditional products expressed apprehension in subcontracting to independent artisan subcontractors in the craft villages because of the risk of deceit (see the analysis in the previous chapter). The most important factor explaining this difference is *trust*. The relationship between the in-house exporters and their subcontractors is characterized by trust building. The texts below by two exporters with in-house production capabilities recognize the role of trust as an important ingredient in enabling external subcontracting to be deployed with minimal supervision or helping the entrepreneurs to attract the artisans to produce in-house without having to establish formal and permanent employment relationships with them:

This is a human problem...at the end of the day controlling them (artisan subcontractors) becomes a problem. Now we don't use numbers. Now we use quality; very few reliable producers and the attraction around these quality people is that they always have influence on the new generation of producers or artisans who would want to be like them. So they get attracted and I use them as the contact point. Most of them are reliable and you can entrust them with €20million, €40million or €50million, no problems....They are so reliable and then the other thing I do is that when we have orders that need to be done in great numbers we centralize it. I bring it here, gets the materials and then I mean reaching the carvers is not difficult; because we have the networking. We get them to come and reside here and then they work (Fritete).

One of the disadvantages of working with the piece-rate is that once they are not salaried and they wait and you are not getting orders for them naturally they would not stay... But the good thing is that once you maintain a good link with them like me...once I have orders I call them, they come and help me, I pay them off and then they go back. So that is when you maintain a good relationship with them.... But if you ever treated them badly or they have course to feel that you cheated them then when they go they say good-by to you; they don't want to come back. When my wife died and I was not here, they organized the one-week celebration; I was in New York. When we brought the corpse they came to help with the funeral arrangement. There are two boys in Accra...they came to Kumasi to help us with the funerals In a way it is also good because you don't have to be paying them when they are not working. Of course it is linked to productivity (African Dream).

Trust is necessary in enabling the in-house producers to manage their relationship with the artisan subcontractor, yet it is not enough to sustain their continuous stay in-house. The economic circumstances of these artisan subcontractors and the fact that they are highly mobile occupationally make it imperative that the producers secure enough and frequent orders to engage them on a regular basis least they lose them to their competitors. One producer who specializes in good quality home décor products for the niche markets in Italy and at the same time produces for volume US buyers indicated that his motivation for securing high volume orders was to ensure that he keeps his workers busy:

The Marmaxx order is just to keep the system busy, pay my bills, pay the staff and keep the workers occupied. If you don't keep the workers occupied and

there is an order somewhere they would leave and it is difficult to get them back. So the Marmaxx orders, Cost-plus orders, the “mass” orders are just to keep the system busy (Kottage Originals).

6.2.3 Multiple Producer-Buyer Relations

The in-house producers maintain multiple trade relationships with buyers including large wholesale and retail buyers, especially from the US, and smaller quantity or niche buyers from both US and Europe. A marketing brochure obtained from a one leading exporter showed that this producer had had business interactions with ten big volume buyers from North America and eleven other small buyers from seven other countries outside North America. The type of buyer, either small or large influences the quality of interactions between the buyers and the exporters and to some extent the decision to produce in-house or to subcontract. The detailed discussion of the trade relationship and the benefits therein between the craft producers and the different type of buyers would be turned to in section 6.2.4. It must be indicated, however, that the competition for the craft products dominated by the big buyers is stiff and it is this particular segment of the market that the local competitors as well as the Asians have succeeded in copying the designs thereby depressing prices and profit margins. Conversely, and as should be expected, the competition for the good quality craft products, which are predominantly patronized by the small niche international buyers attracts higher prices and entry barriers are relatively high. However, whilst the small international niche buyers offer premium prices, the frequency of export orders from this source is low as compared to orders from high volume international buyers who visit Ghana at least twice every year. One producer, African Dreams, made a comparison between their responses to the different market

segments within the current competitive environment within which they operate and the survival responses of some University lecturers during the economic crisis that hit Ghana in the 1980s;

When Ghana was going through difficult times in the 80s, a lecturer friend from UST [University of Science and Technology] had this to say; in fact in the 80s you could find a lecturer who would come to Tech junction to pick passengers to town with his Benz and charge them some fees. So what he said was that you may need that Benz that would give you the comfort and also you can take one or two passengers and charge a few cedis or run some car hiring service with it and that one is exclusive and it is not for anybody. You can be sure not many people would come and hire your Benz so you must have a *Trotro* (mini-buses for mass transit) also which would be working everyday and would bring you the small, small pesewas and the Benz would bring the big money.

According to this respondent the lecturer was in effect: illustrating the point that when you go out into the working world you need to identify products that you can mass produce, it is good to maintain that kind of market; high volume, low margin which you usually have the capacity to produce and brings in a dollar or 50cents. And then you can have the exclusive products or the niche market where you sell smaller quantities but for higher price. They all have their advantages. When the small buyer has not brought an order and the big buyer brings you some, you know you can get something. If you are able to organize yourself well you will be able to make something from the different markets; that is the way things are in this industry.

This researcher could count 12¹² of these exporters who have developed the capacity to meet these diverse market segments. Apart from emphasizing the different market segments that the exporters target (diversification), the above quotation also buttresses the bipolar contractual strategy that is deployed by some of the Ghanaian craft producers to meet the demands of the different segments of the export market. Trading with multiple buyers puts the exporters in an advantageous position in that it to some extent insulates them against the volatile and unpredictable demand changes in the export

¹² Afripech (1997), Fritete (1987), Delata(1997), L'afrique (1992), Katalvic, Tekura (2000), Treasurers of Africa, African Dreams (1993), Kottage Originals(1999), Lorenpee African Version, Wild Gecko(1993), All-round Marketing

market and also minimizes the effects of buyer switch, which are characteristic of especially the large international buyers who sometimes decide to stop sourcing from a particular country or a firm overnight.

6.2.4 Impersonal and Informal Relationships with Buyers

The relationship between the exporters and the different buyers are constructed differently. Most of the exporters interviewed, describe their business relationship with their volume US buyers as formal and that with the small international buyers as informal.

The formal relationship is very much akin to market relationship where there is very little inter-personal interaction between the producers and the big international buyers. There is very little qualitative information flow between the producers and the big international buyers:

The other thing I would say about working with the small and the big buyers is, the small buyers tend to have a more personal relationship and more informal. The small buyers can travel all the way to my shop; they come to me in Kumasi, they know my family. I have a whole room dedicated to one of my buyers. The relationship is more informal but with the big buyers it is so formal. As I talk now, I have never spoken to the buyer of Pier 1; we had neither met nor shaken hands. The first order that I did for them; it was a product somebody picked from me and presented at their show. They work more through their agency and it is the agency who deals with us. But with the small buyers, they come with their agents to Kumasi to visit and spend 2-3 days with us, we do product development, they come with their concepts I make my input, they leave a list of things they want me to design and then they go, I do the samples and send to them, which is not what often happens with the big buyers. So it is like on-site product development and adaptation. The producer benefits because eventually you get to know exactly what the buyer needs. It is also very motivational because you get to see how committed they are to what they are doing....what helps to maintain the quality is the fact that I maintain good contacts with the buyers. They feed us with information on what has happened to our products.

For instance, if the products get there and there is a major problem they take pictures of them and send them to me. So it helps me to know what problems were they. Those kinds of feedbacks we receive from the buyers have always helped me to be quality conscious.

The lack of collaborative interaction between the producers and the buyers is in part attributed to the deliberate attempts by the export agents to frustrate direct interaction between the producers and the international buyers. The other reason is that the buyers cannot just *trust* many of the individual producers to deliver on contract terms, either because they do not have the capacity to deliver on quantity and quality or there is the high propensity for the producers to behave opportunistically if not monitored by an external agent. These generally conform to the long held view of the untrustworthiness of African producers and the lack of professionalism as constraints to building collaborative relationships with international buyers. Let us consider the response of the owner of Delata enterprise to this question that was posed to him: You said some of the international buyers like Bamboula and Swahili have been doing business with you for 13years and 15 years, so what has kept your relationship with them for such a long time?

First of all it is trust and professionalism. Because they see us Africans as people who don't know how to do business, we are not honest, we cut corners. But by my background I am open and transparent. We have that relationship based on transparency and we try to do our best. The Americans for example they want results. So it is trust and transparency. And communication is very key, even if there is a bad situation they want to know (Delata enterprise, 2007).

The observation by this respondent on one hand, confirms the general perception that “weak-ties” (Granovetter, 1983) have failed to develop between African entrepreneurs and foreign buyers because of dishonesty. On the other hand, it also shows that

investment in trust building and a good professional attitude towards work could strength collaborative trade relations between the local suppliers and international buyers.

Contrary to the earlier observation about the impersonal relationship that exists between the volume buyers and the exporters, the evidence also shows that some of the in-house producers with internal production facilities and the capacity to undertake some logistical or shipping arrangements do engage in business transactions directly with the volume international buyers and benefit from market information sharing:

So at least the big people we go to dinner with the buyers and then we ask them the problems they face with our products whether they are in competition with [other big buyers] (L'afrique concept).

The relationship with a UK buyer; Alexander Rose and the local manufacturer of high quality furniture for export also exemplifies an intensive collaborative interaction between a large foreign buyer and a local producer. Through the technical assistance that the producer receives from the buyer, it has been able to upgrade its furniture production to a world class standard. This qualitative relationship is captured in this quote:

Alexander Rose provides us with a lot of technical support in terms of design, in terms of how or what material should be used. At the same time they assist by bringing down an expatriate staffs who are responsible for the quality control. Most of the time our production managers are outsiders; expatriates and that together with the local staffs creates awareness about different dimensions of product quality...they have trained our people and the training is very important...at times they bring people down to come and tell them what exactly should be done...so that has been the strategy that enable us to achieve that high quality and they continue to give us a lot of feedback, especially, from the various shops and also what their competitors are doing(Official of Scanstyle Limited).

It ought to be indicated that the craft exporters with the performance records, good reputations in terms of organizing production to meet buyers' quality standards, quantity, and timelines, all fall into the category of (quasi)integrated producers. They are also among the few exporters capable of participating in expensive international buyers' fairs which in itself is a test of their capability as exporters to diligently meet buyer requirements. This clearly shows that possessing production capability is not only an important prerequisite for attracting foreign buyers but also for engendering collaborative trade interaction between the local producers and the international buyers. These are clearly the advantages of *size*, which in this study is largely related to the extent of investments that have been made in physical production infrastructure and human development. These firms, though relatively young with the oldest in the sample established two decades ago, have accumulated a reasonable amount of physical production infrastructure to boost their production capacities. None of these firms in the study sample were in existence prior to the implementation of trade liberalization and SAP policies in the early 1980s. The oldest among them was established in 1987 and the youngest in 2000. At the birth of their establishments they operated as export vendors who relied heavily on the rudimentary production capacities of artisan subcontractors to execute their export orders. In effect, the ability to build performance enhancing ties with external agents is a function of the economic characteristics of the in-house producers.

The trade transaction between the producers and the international small buyers is described by the producers as a family affair and very informal. The products type involved in this form of business interaction as one producer puts it: *are complex and*

beautiful... [and] I keep those products for the small buyers who pay something additional for them and order small quantities. The complexity of the product development requires some level of inter-personal relationship for information sharing between the trading partners. The small buyers provide the producers with market information relevant to product development and design; this information is provided by the small buyers without any financial cost to the producers. These buyers occasionally send their consultants down to directly get involved in developing new products with the producers. The information they provide to the exporters are sometimes more specific to the product standards of the individual buyers. Regardless of the fact that the buyers make some investments in the transactions and the product designs are tailored to their needs, the exporters are in this case not *locked into* exclusive relationship with the buyers. This could be attributed in part to the fact that the investment the buyers make in the product design and development process are not *substantial* enough to warrant such a relationship. These exporters do have good business reputations and therefore the buyers can trust them to deliver without necessarily having to lock them into exclusive relationships to increase monitoring and supervision. But should the exporters benefit from huge and specific investment from the buyers dependent relationship is inevitable, which is in keeping with the predictions of the transaction cost theory. Let us again consider the relationship between Alexander Rose and the Ghanaian furniture manufacturer (though not in the usual category of craft production) where the former makes substantial investments in the product design and development process of the latter:

We have CNC machines, which can be used for any type of design. We have the professionals who can handle them so any type of product we can design. In terms of adapting to anything with the help of our technical team in the UK is not much of a difficulty.... (Official of Scanstyle)

Noting the multi-purpose technology that is possessed by the company and the flexibility that comes with it in terms of adapting to different tastes and preferences this researcher further asked if the company has any other clients that they supply their products to apart from Alexander Rose. This was the answer given by the respondent:

We started; now we have lots of buyers in Ghana and Nigeria...when we started selling to the Nigerians the buyer was scared that maybe the people would come and buy and then re-export to Europe. It is like a marriage of convenience.

So who pays for the technical support that is provided by Alexander Rose?
(Interviewer)

It is a relationship that they try to help us. All the designs come from them. So if for instance I want to sell to another buyer I have to seek permission from them that this gentleman wants to buy so and so and they would look at it and say well...It is not colonization but it is a marriage of convenience.

Though the respondent wouldn't openly accept the locked-in relationship with the buyer, the statement that "it is not colonization but it is a marriage of convenience" implicitly suggests that such is the case.

It is worth noting that not every buyer is interested in exclusive relationships with the suppliers given the seasonal nature of export market demand, which dictates that partners maintain flexible relationships with each other. The lack of preparedness by the buyers to enter into exclusive trade relations with the exporters is in part due to the volatility of the export market within which they operate; tastes and preferences are always in state of flux. An exporter pointed out that the buyers are not interested in exclusive relationships and the reason in his opinion is that:

.....these are seasonal items, these are trendy items, they change so nobody wants to put all his money in a product and keep repeating the same product, they want to change.... every buyer wants exclusivity, it is only that they don't want to buy your entire production because they are not sure whether it would sell or not. So the middle or the midway situation is that if you are that experienced what you do is that you develop some colours, you develop styles and indeed every importer that we deal with has got the product forecast for trends and we keep receiving on very regular basis all these information from the buyers. In fact the trend for next year...they supply the information free of charge. For example, Cost-Plus will come and say this year our theme is ethnic India and then they would bring some designs or some patterns. So you take a cue from the trends or the design concepts and then you try and then find local colours that would compare favourably.

The trade relationships between the “in-house” exporters and the international buyers take two forms—they are either *market-like* or *network-like* or both. The relationship between some of the in-house exporters and, especially, large American volume buyers are impersonal or market-like and lacks one-on-one trade interactions. The interaction between the exporters and the small-scale international retailers is network-like because there is the qualitative flow of market information, and *light touch* support for product development, that are achieved through informal or trust-based trade relationship.

Noting that the exporters maintain multiple clients, the question that arises is how the producers/exporters are able to meet the idiosyncratic product standards and specifications of their different clients. This raises the question of the capacity of the supply base to flexibly adapt to the different needs of the buyers. It is an issue that borders on the alignment of the design and production capacity of the exporters or producers to the requirements of the buyers. The initial product design is always done by the producers and once a buyer expresses interest in a product sample, it is then adapted to the buyer's specification. Product adaptation is considered to be a normal practice in

the industry. Most of the firms, it is observed, *are able to cope, especially, those who have control over production; ... there are certain technical implications ...so you would have to understand all these and convince the buyer with your experience or know-how (interviewee)*. The product adaptation is always undertaken in tandem with the buyers, agents or consultants appointed by the buyers. The product adaptation process enables the producers to adjust their product designs to the standards and specifications of the buyers:

The issue about adaptation is normal with our industry.... for example if a buyer comes to me and wants to buy a Fritete brand; the buyer would start by selecting a number of items. They may not have the same finishing or colour and the buyer would say can you then give me all these as a collection in the same colour or product finishing; it is product adaptation. Now the buyer can equally select a lot of items and say for packaging reasons I want all these to be one size and price. It is a form of product adaptation. Now once you do it once, twice with buyers A and B, the next buyer who comes, you even go ahead to sell. These are some of the trade secrets that we have. Once you meet the buyer you have to assure the buyer that that is an added plus with your ability to adapt to the buyers need or specification (Interview with Fritete, 2007).

Though recent trends suggest relative increase in the complexity of craft products demanded by buyers and some exporters have responded by employing the use of intermediate equipment or machines, however, the craft products of the exporters largely remain traditional and greater part of the production process relies on the skilful hands of the artisans. The shift from traditionalism is not enormous to present greater technological and capacity challenges to the producers. As indicated earlier, the investments by the buyers in the relationship are not huge enough to call for rigid dependent relations. Hence the ability of the producers to adapt their product development process to the different client needs. It is yet to be seen if the producers can

continue to demonstrate the same capacity flexibility to meet the demand for complex and higher value products at the upper end of the export market.

6.3 Integrating Buyer linkages, Shipping and Export Processing Functions

The export agents as discussed in the previous chapter play very significant roles in export processing and shipping arrangements for most of the craft exporters. Besides internalizing actual production functions, the “in-house” producers are also developing the capacity to undertake their own shipping and other logistical arrangements without having to rely overly on the local export agents thus eliminating the constraints that the local export intermediaries place on them, in terms of the wedge they create between them and the buyers as well as the commission fees they would have to pay to the export agents. Their well organised in-house production capabilities and their history of successful execution of export orders make them more attractive to the buyers. The buyers do have confidence in them to deliver on contract terms. For a buyer to agree to do business directly with an exporter in an uncertain setting as it is the case with the Ghanaian craft industry, the buyers need to be convinced that the producer do have the required capability to deliver according to the order specifications. A local representative of a US agent (buyer AMC) emphasized the importance of building internal production capabilities as one of the prerequisites for developing a direct interaction with the buyers; short of this the roles of the export agents are regarded indispensable in linking the exporters to international buyers:

Cutting off the agent is not possible unless you are very well organised, unless you are very good and even the big ones are themselves [...] then you are talking about somebody who has a huge place and carves everything, have in-

house craftspeople, they carve everything there and produce there and therefore if a buyer comes, the buyer would want to see this person and see if he can get a variety of items from this person (Interview with Getrade, 2007)

The risks of also encroaching on the core area of activities of the international agents are high for exporters seeking to deal directly with international buyers unless again they do possess enormous resources to enable them to participate in international fairs in a bid to attract their own buyers; an exercise which is too expensive for the majority of the exporters interviewed. An exporter who attempted to bypass the US agent, AMC, and deal directly with a buyer recounted her experience as follows:

That is one of the reasons why we didn't do Target orders. I am giving you an example; Target came through AMC and then Getrade. That time we were shipping directly to Peter [the buyer]. So that is the disadvantage of dealing directly with the buyer. If you don't go through the agent, if another buyer is coming you can't exhibit for that buyer. So that is also some of the advantage of coming back through AMC. With AMC, if another buyer is coming they ask you do you have this stock or that. So they bring the buyers. AMC brings the buyers.

When this exporter was pressed further to explain her decision to return to do business with AMC, the cost involved in the distribution of her wares abroad was also given as her reasons:

That is what I was saying. If any buyer is coming you don't get the opportunity and also the expenses involved were too much. Sometimes it takes about a month for the goods to get to the buyers' country and whenever it gets there we have to go there and look for a warehouse, unload the goods and then call their transport manager who would then come and take the products to the distribution centres. The expenses on the plane ticket and the hotel bills were too much and the buyer too was not willing to pay more. So in the end we don't benefit much.

Another exporter (Lorenpee) corroborated the difficulty and the expensive nature of attending international exhibitions, carrying out one's own export processing and shipping functions; reinforcing the importance of the role of the export agents:

In those days I used to travel a lot. The problem with travelling abroad is that it makes it difficult for you to concentrate on production. I have attended a lot of international exhibitions but they are very expensive. It means that the little profit I get from this work, I would have to use it to buy plane ticket, book hotel rooms, in-country transportation expenses, pay for exhibition stands etc. At the end of the day all my profit would have gone into exhibition. So if I travel abroad and fail to get orders it means all my effort here would have come to naught.

The respondent went further to suggest ways of making the relationship between the export agents and the exporters more effective. He stressed the need for trust building as necessary precondition for bringing about specialization between the exporters and the agents:

The agents play important role in this regard. But what they needed to do is to make their functions effective. First, they have to facilitate one-on-one interaction between the exporters and the buyers. There are other areas that we would still need the agents; shipping, how to get cargo containers, loading and paper work. Are you going to combine actual production with these functions? Think about it and if you give to the agent is he going to do it the way you want it? It is a matter of trust. You trust that the agent for instance understand its role. We don't seem to understand specialization. Because at the end of the day I have to procure wood from the village, supervise production and undertake shipping activities. No! That is hectic. I have tried it and it is not wise to do that.

As discussed in the previous section, the individual export vendors do not have the volumes to enable them to ship their finished products at competitive transport cost. Through the consolidation of orders from the individual exporters, the export agents are able to achieve the volumes enough to ship at competitive transport cost. The craft

factories and workshops do possess reasonable capacity to execute order volumes larger than the other category of exporters; however, their orders are not large enough to achieve economies of scale; they pay the same freight charges for the cargo container regardless of whether it is full or not. It is also common for these producers to team up and ship their goods together in situations where they produce for the same buyer.

6.4 Inside-Contracting to gain control over the production process

This section specifically discusses the motivating factors that influence the decision by some of the craft exporters to coordinate production activities in-house, instead of contracting out entire orders to external subcontractors. It is a direct response to overcoming uncertainties surrounding the coordination of production locally and to reduce export risks associated with non-compliance with buyers' quality requirements. The craft exporters operate in an environment characterized by high transaction costs. These costs and risks provide the catalyst for those exporters who can afford to partially internalize production activities in-house to increase control over the production process in their quest to minimize those risks.

The statement below by an exporter who organizes production at her premises identified the need to control product quality and also to meet delivery deadlines as the motivations for organizing production within her production premises. According to this exporter relying on independent artisans operating outside her production premises could lead to delays and poor quality products due to the difficulty of monitoring the artisan subcontractors who may take orders from other exporters without recourse to their ability

to meet product standards and volumes within the specified delivery timelines. When she was asked whether she would prefer to subcontract production orders to outside artisans, her response was:

No! We don't subcontract much because of our quality. You won't be there to check.... If you don't use your "workers" and you go and use "outside workers"; they take money from everywhere. They won't do your work. If somebody comes and the person gives...you know these carvers are not many and these orders that come in are huge orders. So it is the same people that everyone is chasing. So if you don't bring them in-house they won't do your work. They would do small of yours, they would get money from another person...this business too we have time, we have deadlines to meet. That is why we prefer them here and then make sure they do quality work (L'afrique Concept).

Lorenpee enterprise employs about 25 artisans on a piece rate basis and they are recruited to work from the firm's workshop whenever there are orders to be executed. The owner claimed that keeping the workers on the production site helps him to physically monitor the work in order to improve on the quality of his products, something that is difficult to achieve when the workers are producing from faraway places. He believes that the improvement in his product quality over the years is as a result of his strict supervision within his production workshop. He had this to say: "what accounts for the better quality is the supervision and also being strict and don't let go certain things such as playing with the work. I am strict and if you play with the job I fire you. I don't accept "I beg you" neither do I accept excuses otherwise I won't achieve the quality that I want". In the course of the interview in his office, the interviewee requested that he be excused and asked this researcher to join him in his workshop to continue the interview there; apparently he realized that his workers have been left in the workshop unsupervised and that could compromise his product quality. The interview continued but this time in his workshop:

When you came I was at the workshop, when I left here for few minutes you see how everything has slowed down. That is the nature of this work. So most of the time if you keep most of them at a place where you don't have direct supervision, expect that if you get 10pieces, 5 of them would be faulty...that is the attitude of the ordinary Ghanaian. It is Ghanaian character...there are few places that you would go, especially in the private sector that,... the government sector is even worse; when the boss is not there the staff adopts lackadaisical attitudes, lack of seriousness, lay their heads on a table and take a nap or be reading newspapers when he is suppose to work. I don't often subcontract orders. I don't often get charge-backs, which I think is the result of my strict supervision.

A Kumasi-based in-house exporter, Katalvic industry, also indicated the need to control product quality and minimize supervision cost as the reasons for not subcontracting orders to artisan subcontractors even though his factory is spatially proximate to the craft villages and that supervision could be less of a difficulty. When the manager of Katalvic industry was asked to explain the decision to organise production activities on-site instead of subcontracting to the artisans in the villages his response was as follows:

It comes down to quality aspect of the production. When you have the carvers on-site, you are able to check the quality and they also work. Because being at the factory or on-site, distractions are also a bit less. At first we used to go to the villages to execute orders. Most of the time you realize that there may be one order in which the sample could be produced only by an Ahwiaa artisan, another sample only by Foase artisan and the other only by an Aburi artisan. This means that I had to recruit three supervisors to check on the quality of work and progress.

This respondent went further to attribute the motivation for production in-house to the need to gain control over the labour process in order to reduce supervision cost:

It was much more costly to monitor. But if the artisan is on site or factory, I can always check everything to ensure that they produce according to specification of the sample. The problem has to do with supervision. Sometimes when they produce from the villages, they get drunk and sleep instead of executing the orders and give a lot of excuses such as I am sick, I

attended a funeral etc. But when you have them on-site you are able to have some control. I have developed something like a gang; consisting of a master and he would have about 10 members under him. When the order comes I take the sample, give it to the master and negotiate the price with him and then come into an agreement that I need 500 pieces of this can you do it for me. So he picks it and then sublet it to the others. The master artisan brings the carvers to the site otherwise; it is sometimes difficult to control them.

Similarly, some of the export vendors who contract out greater part of their production to subcontractors and do not yet organize greater production function in-house also expressed the preference for investing in in-house production facilities. The appropriateness of in-house production, according to these exporters, arises from the uncertainties that surround the execution of orders by subcontracted artisans and craftspeople. Often the failure or delays in executing export orders also results from a situation where the artisan subcontractors add onto orders¹³ from other clients without full appreciation of their limited capability to execute such orders in time; they often bite off more than they can chew. As indicated by the exporters, it is difficult to control these subcontractors and the cost of monitoring them in faraway places is very high:

Until recently, when we started experiencing the down-ward trend, and those with production facilities are gaining the upper hand; I personally didn't see the need to invest in permanent structures but now I think there is the need for people to control production. The need is that if you give your money out to a carver to execute an order for you, there is no guarantee that you would get the products. The cost of even chasing the person is even more than the eh eh eh eh. If it is in-house you buy the wood for the craftsmen and then negotiate the price of each piece with them and then take the price of the wood from their money. That one you are safe... in your premises you have control over him. Initially, there wasn't the need to have all those in-house things but now there is the need for it otherwise you won't be able to meet your target. They would delay it for

¹³ The craftspeople, indeed, are not able to predict when the next order would be coming their way and so with the least opportunity they take on as many orders as possible without a good estimation of their capabilities to execute all the orders within the specified delivery time.

you. Somebody can even collect your money and runaway with it (Celebrate Services).

I would very much like to carry out all my production activities in house instead of subcontracting to craftsmen at Kumasi and other places. The reason is that it would... increase my control or monitoring over them... monitoring is a big problem, because if you give your job to them and someone also give them an order, they can leave my work and attend to that person's order. But having my production site, help the process to move faster and quality can be achieved (Agyadu Creations).

Not only does organization of production in-house enables the exporters to control product quality, it also allows the producers, within the context of high level of design imitation, to control their product designs from being copied by their competitors. This producer who specializes in the export of home décor for the niche market in Europe (Italy) and the domestic market had this to say:

Actually these are designer pieces and production in-house is actually to regulate process and products. We don't want it to be copied. It is easier for me to work at my workshop because I can control the design. Some of the finishing, I do them myself and this is a way of controlling copying (Kottage Originals).

Generally, quality control seems to be the predominant factor influencing the decision of those exporters that are integrating their production functions in-house whether it is about the production for the mass market or products for the premium market. The craft market has been shifting from basic craft products, once dominated by collectors, to product types patronized by a vast array of clients conscious of product standards and quality. Thus the use of machinery in some aspects of the production process to achieve consistency in product quality:

In the past most of these items were used or consumed by people who were collectors. Today craft is not used or consumed by any special people. The

general public, the general consumers who go into the stores and buy decorative items, they are the ones who do buy and nobody has the time to buy a piece and go and rework it for it to stand. It is my responsibility to make the product to fit the specification of the buyer (Interview with Fritete, 2007).

The use of machines is regarded as unorthodox in Ghanaian craft production but their use is necessitated by the changes in the export market and more especially the quest to meet the changes in quality demands. The investment in machines in the production of crafts is specifically to help achieve consistency in product quality, reduce waste and enhance productivity, and to meet delivery deadlines. The competitiveness of Ghanaian craft products has been derived from the cultural uniqueness of the African designs and the fact that they are hand-made. However, handcrafting alone is regarded inadequate. It is difficult to produce large volume orders with consistent product quality using simple hand-held tools. The acquisition of modern machinery is regarded by many of the exporters as a necessity to meet the new challenges facing them. The government of Ghana policy on the development of the craft industry recognizes the need to transform the industry from a cottage-based one to a modern industry based on the use modern machinery for mass production (GOG/PSI, 2005). The success of the Chinese and other Asian countries in craft export has been attributed in large part to their ability to mass produce high quality craft products at lower cost using modern machines (Konadu-Agyemang and Adanu, 2003). The general preference for organizing production in-house and the use of modern machines in craft production stems from the urgency among the exporters to match competition from the Asian countries. The use of machinery in craft production, according the exporters, is a needed production requirement to meeting export market demand for consistent and high quality products. However, few of the exporters (craft

factories and workshops) have been able to acquire intermediate technology for mass production instead of relying on the simple tools of chisels and hammers. The quote below succinctly captures the justification for investment in machinery for craft production to control quality in mass production and also enhance efficiency.

For machinery, once you get into large scale production, then you need to consider more important issues like quality control. There is no human-being who can produce thousand of these pieces and then turn them with chisel and at the end of the day put there and they would stand.machines increases productivity, it reduces waste and also allows you to meet deadlines. So the use of machinery in mass production or in export production is to ensure that the quality aspect; your target for quality you attain it... lots of production that I get outside from these premises; most of the things that I presented to my current Pier 1 importers, the importers have asked me to provide extra base because of standing problems The other important issue about this machinery thing is that most of the companies like Target etc when you go you find out that the items are displayed in planograms and these shelves have got specific measurements. When you involve mechanization, what it does is that now you control the sizes using machines (Interview with Treasures of Africa, 2007).

6.5 The Challenges to Sustaining Inside-Contracting Arrangement

Producing in-house has its own challenges. The main issues that emerged were the ability to continue to keep labour (i.e. artisans and craftspeople) who are contracted on flexible terms inside the production premises without losing them to competitors, the difficulty of continually securing export orders from buyers to justify the cost of building in-house production facilities, and the challenge to ensure that internalization does not whittle away product variety or range; something the vendors without much in-house production capacity are able to achieve by way of subcontracting production orders to their numerous subcontractors who have unique specialties.

The products mass produced by large in-house producers tend to compromise on the range and the variety that is often demanded by the buyers. The mass-produced craft products are relatively homogenous in terms of design and thus tend to lose out on uniqueness required by niche buyers; a feat that they are able to attain by sourcing their products from numerous subcontractors.

The business is becoming more and more delicate. The solution is to have the craftspeople in-house but this also has got its own problems. The issue is that we export different range of products which we source from carvers with unique specialty and hardly can one get an individual carver to produce the entire product range....in-house (Celebate Services).

Again to be able to sustain the organization of export production in-house requires more secure and frequent orders— extremely difficult to achieve in the volatile and demand-driven export market—to justify investments in fix assets:

Also building ones internal capacity would be based on what I said earlier on that if you are sure that this buyer is going to come once or twice a year, you could do that. But what if you secure a production site, you have everything in place and the buyer doesn't come? What happens to that site? It comes at a cost. So initially everybody was trying to get a production site; almost everybody. We secured this site, we had a metal workshop, we had equipments, and we do have some equipment still in there; about 6years now, brand new things, which we have not used. There was a slump or a dip in the whole industry and now you don't want to commit, you don't want to invest into it. So you see these are some of the challenges (Interview with Delhouse, 2007).

The successful in-house producers balance internalization of production functions with flexibility that is required to adjust to the export market. Even though the craftspeople and the artisans are brought in-house, they are engaged on a piece-rate basis and are not on payrolls of the exporters, enabling the exporters to adjust the size of labour to changes in export market demand. Despite the difficulty of labour control associated with the

piece-rate employment relationship, some of the in-house producers are able to extract some degree of loyalty from the artisans they have been working with over the years. Again some of the specialized producers who produce for the high end of the market claim to use “mass” orders from volume buyers as bait to attract and keep experienced artisans.

6.6 Performance of the Exporters

One major shortcoming during the fieldwork was the inability to secure primary data on the profit margins of the craft exporters in order to be able to obtain a clear picture on the performance of the of the different categories of the craft exporters. However, a study done by Pageau (2004) reported on the differences in performance between exporters with the majority of the artisans working in-house and exporters who largely subcontract to craftspeople and artisans working off-site. Using the 2003 total export sales of six exporters in each category of exporters, the study concluded that the highest production rates were achieved among exporters possessing workshops equipped with proper equipment, storing rooms and majority of the artisans working within production premises of the exporters. Conversely, the production rates of exporters, who subcontract greater part of their production orders to individual artisans and craftspeople; using mainly simple tools, tended to be lower. Generally, the extent to which the exporters address factors such as speed of production; product quality and organizational flexibility are often used as measures of success in the export market. How well the producers respond to these critical factors in many ways influences their profit margins. The tables below, adapted from Pageau/GTZ, illustrate the total export sales of exporters or

producers at the opposing ends of the scale. The total export sales for six in-house exporters in 2003 totaled US\$ 1.1million¹⁴, which was more than a quarter of the total export sales of the whole industry.

Table 2: Sale of Producers with Equipment and most Artisans On-site in 2003 (US\$ '000)

Producers	Prod 23	Prod 17	Prod 27	Prod 24	Prod18	Prod22	Total
Sales	158	240	355	60	301	30	1,144

Source Pageau (2004)

Table 3: Sale of Producers Subcontracting to Artisans working Off-site in 2003 (US\$'000)

Producers	Prod 11	Prod 10	Prod 28	Prod 3	Prod 26	Prod 15	Total
Sales	8	6	50	7	6.2	6	77

Source: Pageau (2004)

Meanwhile, these six producer/exporters constitute just about 2-3percent of firms that are into craft export. On one hand, this analysis suggests a seeming concentration of export production in the industry. On the other hand, it gives an indication of the fact the in-house producers with efficiency enhancing equipments and with most of their subcontractors working on-site; giving them control over the production process, are able to achieve higher production rates than vendors who operate within non-factory environment. Notwithstanding these differences in the sales performance of the exporters, another way of looking at the issue of success in participating in the export market is the effect of participation on poverty reduction. The villages that are linked to the craft export industry tend to benefit from the employment that is generated through the subcontracting

¹⁴ The total export sales for the whole industry was US\$ 4.2 million in 2003 aftermath of 9/11; a sharp drop from US\$14.9million in 2001. The crude estimate of producers in the craft export industry is considered to be between 200-300 producers.

relationships established with the artisans domiciled in these villages. The World Bank (2001, p41) reported that:

...the income generation impact of the handicraft sector is considerable with artisan carvers being paid as much as a skilled machine operator in a factory. In the case of one firm which employs up to 100 persons, wood carvers are paid US\$70-US\$200 per month. This is even more remarkable when one considers it is in a remote location served by dirt tracks and the owner is illiterate and non-English speaking.

The narratives below are also the perceptual illustration of the influence of the craft export industry on the living conditions of artisans at the Foase craft village. In this sense, success in the export market is not judged in terms of firm-specific indicators such as output or total sales instead it is also assessed through the influence the industry has on the living conditions of the artisans. The small-scale subcontractors or artisans may not be growing in terms of their contribution to total output but their ability to secure export orders regularly may contribute to the improvement of their poverty situation. Through subcontracting relations the benefits of integration into the global market cascade down to these remote communities. The case below on one hand demonstrates the direct impact of export on improving the material conditions and raising the social status of the village folks of Foase. On the other hand, it reveals how viable source of demand could motivate the young rural dwellers to take up occupation in craft production. Jamison (2000) made a similar observation about how the availability of market could serve as the motivating factor in attracting individuals and communities who otherwise are uninterested in the craft production to take it up as an occupation: "The perceived economic viability of the craft produced, i.e. whether a market is believed to exist for such crafts and how regular

and predictable demand for these products are outside of Africa, are important considerations in motivating people to engage in these activities”(p70).

The Poverty effects of Craft Export on Foase Village

Foase¹⁵ is one of the main craft villages where traders source craft products for exports. It is located about 10km from Kumasi; the second largest city and about 265km from Accra. Though the village is geographically remote, it is linked to Accra and beyond through the craft trade. This manifests itself in the form of subcontracting relationships that have developed since the 1980s between the artisan subcontractors operating from this village and the export traders, the majority of whom are domiciled in Accra. These trade linkages symbolize the integration of a rural community into international trade made possible through various personalized subcontracting relationships.

Prior to 1987, there wasn't a huge commercial value for the artisans' products. Carving was practised as a means for obtaining income for daily survival. The teaching of carving as a subject in the village's "continuation school" by one village teacher, Mr. Addai was not even enough to motivate the young rural folks to take up occupation in the industry in the 1970s. They did not see carving as viable occupation. Historical accounts traced the origin of the industry in the village as commercially viable export industry to the 1980s. It was during this period that the craftsmen began to get market for their products; first through the purchases made by foreign tourists who visited this village and second by small-scale buyers who bought small quantities of craft products and re-export to North America and Europe. The emergence of this market inspired the artisans to take the craft trade as a serious occupation. The expansion of craft activities during the early 1990s in the village corresponds to the entrance of more international retail and wholesale buyers into the Ghanaian craft industry.

There are about 200 master craftspeople in the village who also engage hundreds of artisans to work for them. About 10percent of the total population (5000) of the village are associated with the industry in different ways. A respondent had this to say regarding the effects of the craft industry on the village's development: "it is an occupation that has significantly contributed to the development of this village. We were mostly peasant farmers but the emergence of the craft business has...any young man you find in this village as well-to-do is a carver. Some of them through the industry have managed to build their own houses in Kumasi. It is all because of the craft business". This respondent went further to indicate how the industry also influences migration: "if a person has a job to do, he hardly migrates. It really reduced emigration in this village. In fact, people were even coming from Kumasi to this village to learn the trade".

¹⁵ Foase village was not mentioned in the available documented historical accounts of craft villages that surrounded Kumasi (see Johnson, 1979 and Browne, 1981b). It has no historical links with the Ashanti court crafts, suggesting that the village as a craft production site is more recent.

The experience of a local Baptist Pastor: This pastor is a key player in the craft industry in the village of Foase. His involvement in the industry dates back to 1984 when he returned from Nigeria in an unsuccessful attempt to seek greener pastures there. He came to settle in Foase in 1987 purposely to work as a wood carver and also to plant a church. He actively got involved in the craft business and fortunately for him in 1997 he secured a contract from Getrade to execute a large export orders; marking a significant entry into the export sector. This order, according to him enabled him to build his first house. He is not able to tell exactly how much the artisans working for him earn per contract because the order size keeps changing. However, he gave an example where in the previous year a carver earned about US\$760 for an order he executed within two months. He claims that because some of the artisans, especially, the master craftsmen get orders from many sources, they could earn up to US\$1,000 for a two-month period.

The experience of a master craftsman: Christian Okyere is a well known master craftsman who until becoming a carver was a shoe-shine boy in Accra. The quest to see improvement in his standard of living failed to materialize as the days went by as a shoe-shine boy. So he decided to change course and lacking formal education he saw an opportunity in the craft business as where he could get improvement in his standard of living. So in 1993 he went to Kumasi to start a new life as an apprentice trainee. Two years later he graduated and set-up his small firm in Foase through the help of ATAG. He began by producing and sending his products to Ghana's neighbour countries for sale but at the moment he produces for a number of export vendors in Accra and Kumasi as well as small-scale international buyers. In corroborating the Baptist pastor's claim about the poverty impact of the industry, Okyere indicated how the craft industry has helped him and his peers in the village: "even though here is a village, most of the young guys have been able to buy plots of land and build 2-3 bedroom houses. But for the craft industry, it would have been very difficult for them to build. If you go to their rooms, you will see that they are well-furnished with modern electrical gadgets. Theft and robbery cases are uncommon in this village. I was a shoe-shine boy. I neither dreamt of buying bed mattress to sleep on nor did I ever imagine that I could buy car tyres, cement or iron rods...I have been able to build this house and I drive my own car. Whenever my extended family is in any difficulties they call on me to make contribution financially or materially, by my age I am not suppose to do so but through this trade I have been accorded that social status".

6.7 Conclusion

Chapter six discussed how some other exporters rely on inside-contracting arrangements to coordinate craft production for export. These exporters inside contract their export orders to contracted artisans to execute within the confines of their production premises.

The logic underlying this emerging trend towards inside-contracting is to minimize quality deficiencies, reduce monitoring and transaction costs, gain control over the labour process and flexibly respond to changes in export market demand. Another visible feature, apart from coordinating production in-house, is the multiplicity of relationships that the exporters maintain with different trading actors. They occasionally subcontract orders to external artisan subcontractors they have built trustful relationships with when they have large order volumes to execute. By maintaining informal relationships with small-scale international buyers (and to a limited extent with large American buyers) the exporters tend to benefit from export market information, product development and sometimes financial resources. The collaborative relations between the in-house exporters and the buyers, and the benefits derived the relations are clearly linked to the characteristics of the exporters who demonstrate professionalism in their work, educated and highly entrepreneurial, possess organizational flexibility and have invested in internal production capacity. There are, however, problems sustaining inside-contracting (building internal capacity) without a sustained export market demand. There is also the difficulty of getting the skilful artisans to stay in-house if the exporters cannot assure them of frequent orders. In the nutshell, the inside-contracting arrangement enables the exporters to have control (but less rigid) over the production process and at the same time enables them to flexibly adjust to fluctuations in export market demand.

CHAPTER SEVEN

SYNTHESIS: COMBINING THEORY WITH EVIDENCE

7.1 Introduction

The object of this study had been to explore how small-scale craft exporters coordinate their production and export activities to mitigate high transaction costs, address market failures, meet stringent demand requirements and succeed in the market. The dominant viewpoint in the new institutional economics literature is that institutions shape markets to work effectively. The argument goes that markets are prone to risks or the markets may fail to operate effectively in the absence of economic incentives and strong institutions. The conceptual framework in chapter two sought to capture the transaction-cost-reducing perspectives of institutions and other market coordination mechanisms; and the conditions under which transaction costs and uncertainties could be reduced. Institutions help to minimize risks and correct market failures require institutions. Strong institutions and the associated enforcement mechanism provide stability to uncertain market transactions (North, 1990). Alternatively, in the absence of strong formal and informal institutional mechanisms to help minimize risks and enforce compliance with quality standards, agents internalize functions they otherwise exchange across firm's boundaries; to minimize uncertainty, save on transaction costs and to meet product quality standards (Coase 1937; Williamson, 1975). This study, which is situated within these theoretical perspectives, attempted to address the following questions:

- What economic and environmental factors constrain the activities of the small-scale exporters?

- What is the nature of the market and institutional arrangements utilized by the small-scale exporters and how sufficient are these arrangements in enabling the exporters to succeed or otherwise in dealing with the limitations placed on them by the uncertain local economic environment and export market forces?

The craft export industry was used as a case for addressing these questions because of the moderate success of the small-scale exporters in entering the export market and the possibilities it offers for understanding how the small-scale exporters vertically coordinate their production activities in response to local constraints to production and new export markets requirements. The common understanding in the literature is that small firms in underdeveloped economies mostly rely on indigenous practices and relational arrangements in their trading transactions in the absence of effective state-sponsored institutions that provide trade support services, but the gap that remains largely unresolved in our understanding is how such local market practices and institutional forms satisfactorily enable the small exporters to surmount constraints (both domestic and international) to productions as they seek to trade in distant markets where there exist different trading culture; emphasizing stricter adherence to contractual obligations (Bigsten et al. 1998).

The general pattern evident in the presentation of the empirical data in chapters five and six is that the market in which the exporters operate is highly uncertain; opportunistic risks are high, local cultural attitudes and practices impede production, and the monitoring of independent artisan subcontractors in order to meet order requirements is difficult to achieve. It was demonstrated in the previous chapters how informal institutions, informal subcontracting relations and partial internalization of production

functions in order to overcome market failures and opportunism. Though helpful in minimizing market risks and also ensuring the flow of critical resources; these mechanisms remain largely weak in engendering effective market exchanges in an environment characterized by stark local market imperfections and enforcement difficulties. The reason for the adoption of inside contracting by some of the exporters (the relatively successful ones) in the industry is to better mitigate some of the limitations placed on them by the uncertain local economic/environmental circumstances and external market forces. Noting that most of the transactions of these exporters take place outside the formal regime, the adoption of the inside contracting system by the exporters also reinforces the weakness of informal subcontracting arrangements as effective tools for reducing opportunistic risks and dealing with other market failures.

The discussion in this chapter is sub-divided into five sections. Following the introduction is section 7.2, which summarizes the main features of the uncertain and the risky micro-environment pertaining to the industry, a discussion follows in section 7.3 on the extent to which subcontractual arrangements and the underlying informal ties enable the exporters to reduce transaction costs and also ensure access to needed resources, section 7.4 contains the analysis of *inside-contracting* as a “new” path to arranging production activities by some of the exporters to partly deal with the high transaction costs and gain control over the production process and how it relates to the literature. Section 7.5 concludes the chapter with a summary of the discussions in the previous sections.

7.2 The Local Market Imperfections: Much of the Same

Underdeveloped societies and particularly markets in Sub-Saharan Africa are characterized as imperfect so are the institutions that shape these markets (McCormick and Pedersen, 1999; Fafchamps, 2004; Luiz, 2009). The market imperfections regarding the Ghanaian craft export industry are consistent with other observations of the workings of the markets on the African continent. These risks emanate from opportunistic behavior, unprofessional and cultural attitudes that are at variance with the demands of the end markets, the lack of the requisite skills and capacity more especially on the part of the independent small artisan subcontractors to meet the required buyer standards. Also imperfect monitoring and enforcement of informal contracts make it difficult to achieve compliance with buyers' standards and specifications. These factors together make the execution of orders extremely unpredictable. These specific areas of market imperfections are discussed below

Opportunism in the industry mainly takes the form of small artisan subcontractors absconding with advance payments, using the money for other extra activities other than the intended purpose of executing the orders or using raw materials procured for them to execute the orders of other clients and stealing of product designs from their principal contractors. Even when the offending artisans are traceable, the exporters are less likely to use formal coercive measures to retrieve their monies for two main reasons. The competition for getting skilful artisans to execute one's order is intense and therefore the exporters do not want to antagonize their relationships with the artisans whom they may need to execute future orders. The size of the transactions is most of the time not large

enough to warrant the expensive legal process; reinforcing similar observation by Fafchamps (2001) that when the size of the transaction is small, economic agents are less likely to resort to the more expensive legal process of dispute resolution. Stories abound of the situation where some of the exporters allow sleeping dogs to lie in cases of deceit and shirking and reassign the orders of the offending party to another artisan subcontractor.

Opportunism is not a problem in competitive market environment but in the view of Williamson (1975) it becomes more costly to the lead producers when they make significant investments in the production process and the behaviour of the contracting party cannot be determined *ex post*. The exporters take bank loans and wholly pre-finance export orders subcontracted to the artisans making deceit on the part of the artisan subcontractors more costly to the exporters. The modest increases in the volume of trade has consequently led to increase in working capital requirement for executing export orders but this has not necessarily translated into greater profit margins. This means that the exporters and even those who could afford to reassign order execution to other artisan subcontractors in the event of breach cannot continue to accommodate deceit. It was therefore not surprising that most of the exporters interviewed expressed the reluctance to externally subcontract export orders for fear of being cheated by artisan subcontractors. The institutional solution that Williamson would offer to the craft exporters to counteract the risk of opportunism is to internalize those transactions in-house; the discussion on this would be turned to later in the analysis of inside contracting in this chapter.

Besides opportunism, there are other factors that add to the uncertain environment of the craft industry. These risks stems from the interface between local trading practices, local capabilities and attitudes of the artisan subcontractors on one hand and buyer standards and product specifications on the other hand. The empirical data evince a pattern where there exists a significant discordant between the indigenous production capacity possessed by the local artisans and the ever changing buyer requirements. This capability gap was long recognized by Keesing and Lall (1992) as a major problem that bedevils many developing countries' firms seeking to enter the international market. The small-scale suppliers from developing countries are often required to meet stringent export requirements, something they are generally unaccustomed to and also without the requisite internal capacity to enable them to meet those demands. There are risks to bear when buyer specifications and standards are not complied with.

The typical problem of lack of appropriate technical skills that face many developing countries' firms is not uncommon among the artisans who are hired by the exporters. The indigenous know-how gives the exporters some competitive edge in terms of churning out indigenous designs; however, the new demands for high quality functional products and competition from Asia pose new challenges to the Ghanaian craft exporters to adapt these indigenous designs to contemporary trends. The artisans who are hired by the exporters to execute their export orders are mostly uneducated and therefore face enormous difficulties adjusting to new product designs and buyer specifications. The production activities of the artisan subcontractors remain largely unstructured; executing orders without recourse to any time schedules or scientific method of organizing

production. The artisans rarely appreciate the urgency to produce to meet deadlines and in many occasions other social and cultural factors may obstruct the smooth execution of orders. Working overtime or on weekends in order to be able to meet deadlines is not part of the culture of the artisans. Other domestic trading practices such as *contractual flexibility* accept delays as adaptive mechanism to dealing with the difficult and unpredictable local economic circumstances (Bigsten et al. 1998; Fafchamps, 1996) yet it is incongruous with the export markets, which require suppliers to meet stricter timelines.

There are other market failures that pertain to artisans' training and product designs. The initial attraction of the sector had much to do with the indigenous designs, which are increasingly losing appeal in the export market. The design content has largely remained the same over the years and buyers are getting fed-up with the over-copied traditional designs. Buyers now demand functional products and not merely African decorative items. The shift in demand from simple traditional products to functional products brings to the fore the training of the artisans to keep up with the new demands or induce the potential actors in the industry with the skills to come out with new product designs. As indicated above the artisans neither possess the requisite training/capability nor do they have the relevant market information to enable them to design products that meet market trends. The exporters who can afford to invest in artisans' training are unwilling to do so for fear of losing them to their competitors. The professional designers in the industry are also reluctant to come up with new product designs because of negative market externalities (i.e. excessive design copying). Like many other sectors of the Ghanaian economy, copyright laws are not strictly enforced. As evident in the empirical chapter,

the practice of using formal contracts as an institutional tool to curtail design copying and provide the incentive for undertaking productive activity such as investing effort and resources in product design is absent in the industry. Some of the designers were incidentally willing to enter into bilateral contractual agreements with exporters who are ready to compensate them financially for their effort.

This analysis sets the stage or provides the micro-economic and institutional contexts for examining the extent to which the subcontractual arrangements and other informal mechanisms enable the small-scale exporters to deter opportunism, enforce compliance and to ensure the flow of critical resources for greater success in the export market.

7.3 Are Informal Mechanisms and Subcontracting Relations Sufficient for Small-Scale Enterprises to Succeed in the Export Market?

The general thinking in the new institutional economics literature is that in the absence of perfect formal institutions that facilitate trade, informal institutions emerge to mitigate agency problems (Fafchamps, 2001; Dixit, 2004; Anderson, 2004) and facilitate the flow of critical resources. Studies by Ensminger (1996) and Greif (1993) are frequently cited (see Fafchamps, 2004; Dixit 2004) to buttress this theoretical claim. Further empirical studies that are specific to the organization of trade in Sub-Saharan Africa also bring to the fore the significant role informal institutions play in enabling small African firms to transact business and get access to critical resources for productive activities in the midst of opportunism and high transaction costs (Fafchamps, 1996, 2001, 2004; Barr, 1998; Brautigam, 1997). The extensive reliance on informal institutions by small-scale African

entrepreneurs and the effects they have on reducing transaction costs had led some authors to argue that they could successfully substitute for weak formal institutions in shaping market transactions (Brautigam, 1997). Noting that informal institutions play significant role in trade transactions in developing societies where market imperfections are pervasive and enforcement of informal contracts problematic, they lead us to question the efficacy of informal institutions in deterring deceit and overcome information problems as trade expands (North, 1991; Dixit, 2004). The argument goes that informal institutional arrangements could substitute for formal institutions in minimizing transaction cost and address market failures. This study recognizes the need for caution and questions the sufficiency of informal institutional arrangements to reduce transaction costs and address market failures as trade complexity increases. Based on the empirical evidence, one theme that emerged is that informal institutions and informal subcontracting relations may help small entrepreneurs to minimize agency problems, and also ensure the flow of resources for productive activities. How adequate are subcontractual and informal arrangements in enabling small-scale exporters to access critical resources and also mitigate market failures and opportunism as trade expands? Inter-personal trust is an important requisite for successful inter-firm relations but the absence of it constrains any meaningful trade relations between partners. The trade relationships the exporters establish with artisan subcontractors, trade intermediaries and buyers as played out in the areas of access to trade credit, market access, quality control and monitoring, product development/design and access to skilful labour or artisans are given attention in the next discussion.

7.3.1 Informal Arrangements and Access to Trade Credit by the Exporters

The formal financial institutions are often reluctant to provide credit to small firms because of high transaction costs and the problem of information asymmetries (Stiglitz, 1998). The formal financial institutions often lack the relevant information on prospective small-scale loan applicants to determine their credit worthiness and also encounter lots of difficulties monitoring them to ensure that the loans advanced to them are used productively for the intended purpose to ensure repayment (Stiglitz, 1990) against the backdrop that these small firms often lack movable collateral that can be used to service default.

The informal credit arrangements between the bank, Prudential, and the exporters demonstrate a formal actor reaching out to small-scale actors who are often considered marginal to the formal sector and in doing so tend to rely on the available assets; intangible and informal mechanisms to which informal small-scale firms have in abundance to minimize the risk of default. In the event of repayment difficulties, the bank prefers to use mere threats of court actions to enforce repayment or may defer loan repayment subject to future export orders. Using the court system to recover relatively smaller loans is expensive, cumbersome and may also strain the relationship with the exporters to which the bank wants to preserve. This lends credence to the position that when formal enforcement institutions are weak, economic agents may rely on informal mechanism to enforce loan recovery. Also the informal nature of the loan agreement (i.e. the use of intangible assets instead of movable collateral) makes the use of courts untenable.

Besides this intangible safeguard that is embedded in the relationships with the various exporters operating under the export agents, the bank has also instituted another system in which the exporters contribute a certain percentage of their loan amount into an “insurance pool” to use as safeguard against possible defaults. Similarly, Morduch (1999) noted that the Grameen scheme mixes a *peer monitoring system* with *partial collateral* arrangements, which require borrowers to make contributions to a fund as insurance against default.

While these informal mechanisms and semi-formal arrangements are utilized by the bank to mitigate risks and at the same time allow low-income actors to access formal trade credit, it is important not to overstretch its role in facilitating non-collateral trade credit in an environment of high risks. There is a limit to the size of loan can be sustained under this informal arrangement. Morduch (1999) in a review of a number of group lending schemes in some developing countries indicated that the range of the average loan size under the schemes is \$70-\$1000. In the case of the Ghanaian craft exporters, the maximum credit threshold tolerable under this non-collateral regime is US\$ 10,000. Any amount above this figure requires the borrower to provide fixed assets as collateral. Because of the huge trade credit that the graduated craft factories, for instance, require to execute high volume orders, they often have to provide fixed assets as collateral. The laxity of the informal group arrangement makes it insufficient as insurance against huge trade credit that is needed by some of the exporters to meet greater export demands. Let us refresh our memory about the narrative in section 6.2 case 2: When the American buyer, Cost-Plus offered huge export orders to Fritete and its affiliated export vendors,

the bank was initially unwilling to grant the exporters the huge credits they requested to execute their orders. The bank demanded that they provide movable collateral that many of them did not possess. In this instance, Fritete had to use the reputation it had built with the bank over the years and some other informal arrangement to facilitate credit for the vendors. Though the arrangement was successful in ensuring repayment, the bank later opted to enter into a formal contract directly with Fritete by making the company the foremost risk bearer. To the bank, it meant a reduction in both administrative cost and transaction cost (information asymmetries and monitoring cost) in dealing with large number of export vendors. The move by the bank to formalize the credit agreement with the exporter attests to the implicit apprehensiveness by the bank to rely on informal arrangements to safeguard sizeable trade credits.

7.3.2 Informal Subcontracting and the potential for growth in the midst of market imperfections

Trust as was discussed in the conceptual framework is an important ingredient that sustains subcontractual relations between independent partners even if the relationship entails specific investment. As it was evident in both chapters 5 and 6, the exporters maintain complex relationships downstream with export agents, international buyers and upstream relationships with numerous artisan subcontractors. Based on the relationship that the exporters establish with these trading actors, they are able get access to the export market, develop new products, get access to artisanal labour, as well as quality management and export processing services. Another theme that is manifested in the empirical section 5.4 is that despite the advantages the exporters derive from the various

subcontracting relations with their trading partners, the potential for generating high order production functions for export is constrained by market failures and mistrust. In effect, private enforcement and provisioning, though holds promise for firms' success, but for externalities that stifle the incentive for achieving greater success and opportunism that makes reliance on inter-firm trade relation more costly. This theme is discussed at three levels of contractual relationships to include exporters—export intermediaries relations, exporter— artisan subcontractors relations and exporters—buyers relations.

7.3.2.1 The Relationship between Exporters and Buyers

There are two categories of international buyers that trade with the exporters. They are large volume retailers/wholesalers and small quantity niche buyers. The large volume buyers indirectly deal with the numerous small-scale exporters through local intermediaries. The trade arrangement between the large volume buyers and the exporters remains largely arm's length. The wish of the numerous small-scale exporters is to have a more intensive relationship with the buyers by which they could benefit from relevant market information or direct skill transfer. Qualitative trade relations have failed to develop between the exporters and the buyers, especially, the volume buyers because of the long held view about African business people, and also confirmed, by this study as being untrustworthy and also lacking good professional attitudes towards work. The local exporters also lack direct communication channels with the buyers. The inability of the exporters to directly communicate with the buyers is in part a direct orchestration by the export intermediaries who obfuscate any direct contact between the local exporters and the buyers. Again the individual exporters do not have the capacity to produce the

volumes that are large enough to warrant the exclusive attention from the large international buyers. The impersonal interrelations between the buyers and the exporters entailing little exchange of market information and technical information between them suits the product types that are exchanged in the transaction between the volume buyers and the small-scale exporters. The bulk of the products that are exchanged in this relationship are the low-quality and low-price products for the low end of the market (see similar observation in Nadvi and Schmitz, 1994, p 23). The converse is the case for the relationship between the small quantity international buyers (e.g. the niche buyers and sometimes large volume buyers) and the local exporters. They mostly trade middle-ranked quality products and the transaction takes place within personalized and trust-based arrangements. This happens in the case of the exporters with in-house production capabilities and has proven records of producing relatively good quality products. Local market imperfections, difficulties of individual producers accessing relevant market information, enforcement difficulties and other capacity constraints currently make achieving high quality products through impersonal market transactions between buyers and producers an unlikely path. The role of buyers or other external intermediary agents with enormous capacity would be crucial in helping number of the local exporters to move up to the high end of the export market by building their production capacities (e.g. WATH established by USAID has been instrumental in providing market and technical aid to numerous small firms in West Africa to enable them to integrate into the Western Markets).

Risks of non-compliance comprise buyers' "charge-backs" for supplying sub-standards products, financial penalty for late delivery and at worst a buyer switching completely from buying from a whole country or an exporter. Some of these measures, though punitive but effective, are employed by the large volume international retailers through their local agents to enforce compliance. The hierarchical relationship the large American buyers establish with the small exporters enables them to extract compliance through financial punishments. This is also because they generally operate in an impersonal or arm's length trade transactions with the small-scale Ghanaian craft exporters in which the motive is not to build informal trade relationship. However, some large buyers and small international buyers that engage in personalized transactions with the exporters use penalties but rarely. In a study to investigate whether there are differences among firms in selected countries in Africa regarding the use of financial penalty to enforce contractual obligation, it was concluded that large firms that operate in less personalized manner use penalties to enforce contracts (Fafchamps, 2004). However, Asian-owned firms in these countries that place importance on and invest specifically in trust building relationship rely on informal and intangible enforcement mechanisms to extract compliance. These evidences reinforce the theoretical claim that harsh sanctions though effective in ensuring compliance in market transactions, may be inimical in fostering personalized trading relationship, if the motive is to build such relationships.

7.3.2.2 The Relationship between Exporters and Intermediary Agents

The export intermediaries play important trade bridging function between the numerous local exporters and the international buyers. Fafchamps (2004) in a review of the role of

traders in economic activities criticized the extensive attention given to producers and consumers in economic theory to the neglect of traders. According to him traders are often treated as redundant actors and the trade intermediation function that they perform is implicitly assumed to be so trivial that individual producers and/or consumers can easily undertake it at no cost. They are also wrongly assumed to operate in a transparent manner: they are powerful and do not just pass prices and commodities without affecting them. The rise of trade intermediaries in the craft industry was a spontaneous development following the entrance of major international buyers into the Ghanaian market. When the international buyers first visited Ghana, they faced coordination challenges and information asymmetries in properly estimating the production capabilities of the small-scale artisans (Biggs et al.1994). Fafchamps (1996) in his survey in Ghana showed that the institutional response Ghanaian firms have found in responding to enforcement problems locally is to deal with handful of suppliers and clients they have established personal relationships with. He argued that this limits the economic reach of the Ghanaian firms and reduce the local market into fragmented networks of small firms with consequence of restricting specialization and firm growth. However, the existence of trade intermediaries forms an important link that has enabled Ghanaian firms to engage in cross-border trade sometimes in anonymous way. On one hand, they help the buyers to overcome local coordination bottlenecks and ensure that the local exporters comply with contractual obligations. On the other hand, they help to link the numerous small-scale producers to the international market through the various functions they offer to them. The activities of the intermediary agents manifest in the areas of monitoring of the small-scale exporters to ensure compliance with buyer specifications and quality standards,

export processing services, financial intermediation and market linkages services. The small scale exporters receive these services through the subcontractual relationships existing between them and the intermediaries. In majority of cases, the exporters do not directly pay fees for the costs of these services but they are covered through the operating revenue margins of the intermediaries. In other cases the exporters are made to pay commissions but only deductible from the earnings of the exporters upon receipt of payments from buyers. Unlike many intermediaries, the small-scale exporters do not have to make upfront payment of service user fees. This and the fact that the services are “embedded” in the subcontracting trading relationship increases the accessibility and the outreach of these services to the small-scale exporters. The intermediaries are motivated to provide these services because by helping the producers to meet product specifications and quality standards the consequence is that it could strengthen their relationship with the buyers with the greater prospect of securing export orders in the future. However, there are questions about the sustainability of the services offered through this arrangement; the intermediaries only offer these services when the secured orders by the exporters are coordinated through them. Also the services offered by the intermediaries are classified as low order services, which do not require huge private investments. Investment in high order services needed for greater success in the export is not popular with the agents. One re-occurring theme in this study is the fact that economic agents in the industry are often discouraged to invest in productive activities for lack of economic incentives to do so. This is also the case with the trade intermediaries. They cannot be certain that if they invest in high order services that go to promote high quality products they can reap the benefits of their fruits because of the problem of free riding. There is

also no guarantee that the small-scale exporters would be able to pay commission fees upfront for such high order services; the traditional problem many small-scale enterprises face in accessing third party services in developing economies. It is therefore not surprising that high order services regarding product development and training of labour are viewed as “public goods” by many of the actors in the industry and are considered to be outside the functional domain of the export intermediaries. The relationship between the exporters and the intermediaries is not a-moral; it is also characterized by double-crossing and mistrust. The intermediary agents were often accused for withholding important buyer information from the exporters. Some officials of the intermediary agents “unofficially” compete with the local exporters by also going into production and sometimes divert repeat orders from the buyers intended for the exporters to their underground production sites. The conclusion that we can draw from this analysis is that in the absence of effective third party public enforcement and service provision, we cannot be certain that third party private enforcement and service provision would be a good substitute, for their effectiveness could be stifled by market failures and imperfections.

7.3.2.3 The relationship between Export Vendors and Artisan Subcontractors

The relationship between the exporters and the artisans is reciprocal but the relationship is being undermined by mistrust and opportunistic behaviour. The exporters obtain product design samples from the indigenous artisan subcontractors and present at buyer fairs for export orders and the exporters in turn reciprocate this gesture by subcontracting the orders to the artisan subcontractors. The ingredient that glues this relationship

together is trust. If the exporter has any reason to believe that the artisan would behave opportunistically, shirk or has ever cheated, the exporter would not accept product samples from him for exhibition let alone to subcontract orders to him. Likewise if the exporter has ever reneged on contract terms such as failing to honour full payments for previously executed orders, the artisan who possesses the indigenous skills may not give his product sample to the exporter to present in an exhibition nor would he work for him.

The study also revealed a deep seated mistrust between the exporters and the artisans. We know that the success of relational contracting as a form of organizing industrial activities in Japan are preconditioned on high degree of trust and commitment among the transaction partners (Dore,1983). Opportunism as defined by Williamson (1975) is counter-productive to fostering reciprocal trade relations that is built on trust and commitment (Fafchamps, 2004). The lack of trust¹⁶ in the artisans to conform to specifications/standards and deceit means the exporters have to expend a lot more effort and resources to monitor the artisan subcontractors to ensure compliance if they choose to rely on arm's lengths subcontracting arrangements. In effect, the absence of trust implies increase in monitoring costs. The fluid relation between the exporters and the artisans makes it difficult for the exporters to control the artisans. The powerful position of the artisans in the relationship is connected to their possession of the unique artisanal skills. Though the exporters do maintain some fairly personalized relationship, this is not strong enough to avoid losing them to competitors. The artisans are highly mobile and therefore could easily migrate from one exporter to another depending on who offers them the highest bid. Sometimes they are "poached" by exporters who could offer a higher bid or

¹⁶ Untrustworthiness may also mean the lack of capacity to execute orders to meet the required standards.

provide them with relatively frequent orders. Entering into exclusive relationship with the artisan subcontractors could offer the exporters some level of control but this can be maintained if they can assure the artisans of a fairly regular orders. It is worth emphasizing that the export vendors depend on other agents for export orders themselves and do not have the marketing capacity to secure, or predict with certainty the frequency of, export orders. Levy et al. (1999) reported of a similar situation in the Jepara Furniture industry in Indonesia where the exporters were confronted with the challenge of gaining control over production in order to enforce quality standards. The successful Jeparan exporters responded to this challenge by shifting from loose contracting arrangements to exclusive subcontracting arrangements in which the subcontractors agreed to work for the lead exporter only in turn for an ongoing flow of orders.

This subcontracting relationship between the Ghanaian exporters and their artisan subcontractors correlate with the type one subcontracting arrangement described by Mead (1984 see the theoretical discussion). Mead observed that in a market characterized by market imperfections and distrust, the arm's length subcontracting arrangement becomes the less likely candidate to foster the growth of firms for the reasons that there is little sharing of qualitative information and the general reluctance by principal firms to invest in the capability of the subcontractor producer. Mistrust generally characterizes the relationship because of the tendency of the artisan subcontractors to cheat. The complaints of subcontractor artisans running away with advance payments or using raw materials procured for them to execute other people's orders abound. The artisan subcontractors are neither in captive relationships with the exporters nor are there

channels or common platforms for communicating information about cheating subcontractors at the industry level. This makes informal sanction like the artisan subcontractors losing their future trading relationship, less of a deterrent for opportunistic behaviours. The power relationship also explains the lack of control over the artisan subcontractors as alluded to in this quotation: "...from the exporters to artisans, the chain is broken...the artisans have more power than the export vendors" (refer to full quotation in section 5.4.6). These factors together with the limited production capacity and unskilled labour that pertains to the local markets make the deployment of subcontracting arrangement (as a tool for meeting new and exacting buyer requirements and specifications) less effective. In instances of imperfect enforcement mechanism and imperfect market support services, market exchange only takes rudimentary form.

Though least suitable for growth under the existing microeconomic environment, the fluid subcontracting arrangements allow a number of people to earn incomes as subcontractors and producers. The artisan subcontractors and the craftspeople in the villages earn their livelihood through the arm's length subcontracting linkages but the robustness of such arrangements to meet new market demands and the ability to foster long-term growth is constrained by market imperfections; including opportunism and difficulties of enforcing informal contract, shirking, inappropriate local and cultural practices, weak production capacity, lack of incentives to induce the producer to invest in high order product development and training of labour. This lends support to other observations that subcontracting is less widespread in Sub-Saharan Africa because of the difficult microeconomic environment that is characterized by deep seated market failures

and imperfections (Biggs and Shah, 2006). This discussion also raises the question of why subcontracting in the Ghanaian craft export industry, even at its rudimentary stage, would be difficult to sustain as market coordination mechanism but sophisticated subcontracting arrangements thrive in Japan. The answer lies not just in the stability of the micro-economic environment but also the quality of institutions that support subcontracting arrangements in both the Ghanaian craft industry and in Japanese industries. The Japanese example of relational contracting is noted to be built on trust and effective enforcement of informal contracts. Even where market abuse cannot be curtailed by such informal arrangements, it is backed up with the use of formal contracts to minimize abuse (Dore, 1983). In the Ghanaian case, inter-personal relations play a role in the subcontracting relationship but less robust since informal contract enforcement is weak and the trading partners rarely use formal contracts to reduce abuse.

To address some of these market imperfections some of the entrepreneurs adopt inside-contracting system (sometimes mixed with external contracting) to gain control over the production process and address some of the domestic market imperfections. It is important to note that the inside-contracting regime is not an institutional response only to domestic market circumstances but also to external market forces. It is an institutional attempt to meet buyers' demand for quality and also to match the intense competition from the Asian countries. The next section looks at inside-contracting as practiced by some of the exporters, the forces shaping its adoption and how it relates to what we know in the literature.

7.4 Inside-Contracting and Enterprise Success under conditions of Market Imperfections

The transaction cost theory offers fundamental perspectives to understanding alternative choices of contract mechanisms. The pioneering works of Coase (1937) and Williamson (1975) offer refreshing perspectives with regards to the circumstances under which economic activities may be organized by the entrepreneur-coordinator within the firm. Coase argued that the rationale for establishing a firm is that there are costs to using the price mechanisms, which may include the costs of negotiating, concluding and enforcing contracts and that by allowing some “authority (‘an entrepreneur’) to direct resources, certain marketing costs are saved”(p392). He particularly singled out uncertainty in the market as the major cause for the emergence of the firm; “the question of uncertainty is one which is often considered to be relevant to the study...of the firm [and] it seems improbable that a firm would emerge without the existence of uncertainty” (p392). Williamson expanded on the Coase’s work and elaborated on how opportunism and the limitation on human cognitive ability to foretell possible actions of transactions partners create the conditions for the rise of the firm. The difficulty of assembling the relevant market information during contract negotiation and execution coupled with imperfect enforcement increases the uncertainty in the market (see the discussion under theoretical chapter). Williamson like Coase posits that under such conditions and with transaction-specific investments economic agents or the entrepreneur coordinator would seek to limit uncertainty and transaction costs by organizing production hierarchically within the firm with correspondingly limited role for subcontracting. In a commentary on Williamson, Levy (1991) indicated that societies differ in their propensity for opportunism, with

activities involving specific assets more likely to be organized within the firm in opportunism-prone societies. The proposition is therefore that transactions with substantial potential for post-contractual opportunism will be organized within the firm. This theoretical perspective provides a starting point for our interpretation of inside-contracting.

The inside-contracting system in the literature contradicts external subcontracting in that the entrepreneur-coordinator organizes production inside the firm but also less rigid than the typical vertical integrated firm. From evolutionary perspective, it is considered a transitory stage in the development of the firm finding its place somewhere along the continuum between the arm's length market exchanges and vertically integrated firm. The inside contracting arrangement, according to economic historians, outlived its usefulness by the early part of the 20th century, though the forces that led to its emergence are of relevance to this study and it would be safe to state that the fitness of the inside contracting system to the Ghanaian craft industry is in part due to the traditional stage of the industry's development. Though inside contracting is an old system its development in the Ghanaian craft export industry is new. Recapitulating the factors that led to the emergence of inside contracting is worth noting. These factors of change included:

- Increase in demand for the product in question, made it difficult to fill orders using existing arrangement by the entrepreneur without additional capital and labour. The concurrent emergence of the principle of interchangeable technology and the availability of contractors ready to be hired to produce inside the entrepreneur's factory made mass production possible (Buttrick, 1952);
- The weakness of the traditional subcontracting system to address difficulties pertaining to the economic environment provides the impetus for other production arrangements like inside contracting, which gave the entrepreneur some level of control over the production process. Some of these factors, which have been

discussed under the theoretical section and fleshed out in the empirical chapters, include issues bordering on control of labour, quality control and product flow and unstable work commitment on the part of subcontractor producers, which is partly linked to other activities such as subsistence farming and other local cultural practices. Under the traditional putting-out system, entrepreneur coordinators could not directly control the producers working in dispersed locations and operating as independent producers; supervision difficulties resulted in poor quality, widespread theft, opportunism and delayed deliveries (Lazerson, 1990).

The case of the craft industry exemplifies modest increases in the volume of trade in recent times resulting from a boost in demand from large US buyers. The increase in demand and the accompanying new buyer requirements and specifications had had two implications on the organization of craft production for export. First, the existing rudimentary production arrangement via subcontracting as discussed above is proving to be inadequate in meeting new demands requirements bordering on quality standards, volumes and delivery times. Second, the modest increase in volume of trade means a corresponding increase in the size of transactions and the investments the exporters make in their export transactions. Failure to meet buyers' requirements carries the cost of paying "charge-backs" in much the same way that making direct investments in the form of working capital or supply of inputs could be costly if trade partners renege on contract agreements.

How can the entrepreneur-coordinator organize production and be certain that the finished products he/she sends to the buyer is of the right quantity, the right quality at the specified delivery time so as to avoid penalties or how can they ensure that subcontractors do not abscond with monies advanced to them to execute orders? Some of the craft exporters have sought answers to some of these issues by internalizing

transactions that are prone to opportunistic risks and uncertainties. They however, recognize that rigid internalization deprives them the opportunity to adjust to fluctuations in market demands. Instead of permanent and rigid employment relations with the artisans, these exporters *contract out* the orders to the artisans *inside* their production premises. By maintaining a flexible relationship with labour inside the factory, the entrepreneur has the opportunity to adjust the size of the labour force to changes in the volumes of orders. However, the control over labour and the production process is not sacrificed by maintaining fluid contractual relationship. Producing on the factory floor, the entrepreneur has some level of control albeit indirect over the production process to minimize opportunism and shirking, and enforce adherence to product quality and specifications. The other advantage of the inside-contracting arrangement is that the entrepreneur who does not possess the craftsmanship skills tends to benefit from the skills of the artisan subcontractor producing inside the factory. The entrepreneur has the advantage of possessing relatively rich market information, which he transfers to the artisans producing inside his/her factory. By virtue of their participation in international trade fairs and their direct contacts with buyers, the owners of these enterprises described in this study as factories/workshops are much closer to the international market than the small-scale artisan subcontractors in the craft villages in terms of the understanding of the changes in market trends and buyer requirements.

The exporters interviewed overwhelmingly adduced quality control, the urge to tighten supervision to reduce opportunism and indiscipline as the prime motivations for coordinating production in-house. The inside-contracting system helps to minimize the

indiscipline that is endemic in the industry and also assures product quality. Critics often point to the increase in overhead costs that confront the entrepreneur as he undertakes detailed supervision in-house to minimize risks. Others also argue that this is compensated for by the product quality that could be achieved (Dietrich, 1994). The views expressed by the exporters are consistent with the economies of quality control that is achievable through inside contracting. Let us consider a selection of specific responses offered by some of the Ghanaian craft exporters for choosing to coordinate production activities in-house instead of subcontracting externally to independent subcontractor artisans in the craft villages:

Motivations for In-house Contracting: Selected Quotations

We don't subcontract much because of our quality
If you keep most of them (artisan workers) at a place where you don't have direct supervision, expect that if you get 10 pieces, 5 of them would be faulty
It comes down to the quality aspect of the production. When you have the carvers on-site you are able to check the quality and distractions are also a bit less
It...would increase my control or monitoring over them (artisan workers); monitoring is a big problem in the industry
Initially, there wasn't the need to have all those in-house things but now there is the need for them; otherwise you won't be able to meet your target. They (artisan subcontractors) would delay it for you
I can always check everything to ensure that they produce according to the specification of the sample
The problem has to do with supervision. Sometimes when they produce from the villages, they get drunk and sleep instead of executing the orders and give a lot of excuses...
But having my production site helps the process to move faster and quality can be achieved
Production in-house is actually to regulate process and products. We don't want our products to be copied
Once you get into large-scale production, then you need to consider more important issues like quality control...the use of machines ...in export production is to ensure the quality aspect; your target for quality you attain it.

Inside-contracting is noted to be a transitory institutional arrangement consisting of “ad hoc regulations, within the firm” and the reduction in its significance at the turn of the 20th century was occasioned by the formalization of rules and procedures within the firm

(Dietrich, 1994). In effect, there was a shift from indirect control based on informal relations inside the firm to direct control based on formalized relations between the entrepreneur and workers. Williamson (1985) made a similar observation about the development trajectory of the firm and argues that current modes of organizing production are superior to replaced modes in terms of effectiveness and efficiency. In the light of this he concluded that the “progression from Putting-Out to Inside Contracting to Authority relation is especially noteworthy in that respect” (Williamson, 1985, p321). The case of inside contracting adopted by the Ghanaian craft exporters do not conform to Williamson’s predictions in entirety. What this study is not certain about is whether the exporters inside contracting could grow to become large firms. Much would depend on the market size and the ability of the entrepreneurs to learn and adapt to changes in the circumstances of the export market as well as the conditions pertaining to the local microeconomic environment. At the moment it is difficult to establish which direction the enterprises would head towards. They could, for instance, “grow” to become vertically disintegrated or delinked firms relying on subcontracting relations given that there are improvements in the conditions of the microeconomic environment. This is a conjecture to which this study does not have the evidence to support and remains a question for the future. What this study, however, is certain of is that the exporters who are today adopting inside-contracting were once putting out entire production orders to outside artisan subcontractors. Almost all of the exporters since the formative years of the craft export industry were vendors with minimal on-site production capacity and relied mainly on artisan subcontractors in the craft villages to execute their export orders. The emergence of craft workshops/craft factories using inside-contracting arrangement marks

a new mode of organizing production in the craft export industry; a response to the changing market conditions and the uncertain local institutional and economic environment. Inside contracting in the case of the Ghanaian craft export industry is an offshoot from the putting-out arrangement as predicted by Williamson and the industrial organization literature and have lots of commonalities with the inside contracting system as it existed in the 19th century in Europe and America in terms of the character of the system and the processes undergirding its development.

But the study also established that the change is not a *complete shift* from external subcontracting to inside contracting; the exporters inside contract within their production premises and at the same time continue to put-out orders to outside subcontractors though on a limited scale. These exporters contract out externally to artisan subcontractors they have built long term relationship with and the products that are subcontracted in this fashion are the simple and traditional items, which do not have complex quality dimensions. As the study has demonstrated, a single entrepreneur-coordinator could adopt bi-polar contracting regimes in response to different exigencies. The coordination choices that entrepreneurs make in reality are far more complex than the uni-polar or singularity of alternative coordination mechanisms that are very often assumed in the transaction cost framework. Also there are numerous exporters who continue to rely on external independent subcontractors to execute their production orders in the industry. Inside-contracting co-exists with external subcontracting in the industry.

Williamson also points to the superiority of internalization over arm's length market exchange in a risky environment. This study shows that the exporters relying on the internal contracting are more successful than the exporters relying solely on external contracting. Caution, however, is exercised here in making this conclusion since evidence on the performance of the exporters in terms of profit margins was not forthcoming. Scanty evidence on the export sales, used as proxy for performance, of the enterprises showed that the in-house producers were better performers. This gives an indication that if transactions are internalized albeit partially within the firm in an imperfect market, it gives the entrepreneur a performance urge. The inside contracting firms could be considered as growing firms whereas the majority of the export vendors and subcontractor artisans who rely on the traditional subcontracting arrangements do so for survival motives. Given the uncertain environment the informal subcontracting and the inside contracting relations lead to differing levels of the exporters' success, with the latter having greater prospect for success.

In whatever form Internalization takes also carries some costs. Fixed costs or investments in fixed internal production infrastructure may increase as the entrepreneur seeks to increase control over production. Inside contracting and the associated moderate investment in production infrastructure requires frequent export orders to avoid the costs of allowing those fixed investments to sit idle. One exporter told about acquiring new equipments to expand his internal production capacity in anticipation of increase in export demand and suffered the cost of the his equipments having to lie idle because of the sudden slump in demand. Unfortunately, this exporter in question does not possess

the marketing capacity to search for frequent export orders. Infrequent orders suggest that transactions would have to take place in a spot market manner because the costs of building internal capacity cannot be justified (Sturgeon, 2002). Again, in the absence of frequent orders, it would also be difficult for the entrepreneurs to maintain the skilful and experienced artisan workers in-house, regardless of the informal relationships that they might have established with them. As the exporters adopt internal contracting, their products tend to be near standardization, which reduces the variety and range of their products.

Some of the exporters with capacity to undertake buyer contacts trips abroad seek to minimize the problem of infrequency and the volatility of the export market demand by maintaining multiple client bases. Through this they are able to secure fairly frequent orders to keep their inside contractors busy; enabling them to extract near exclusive relationship.

The relationships with small quantity international buyers (and in few cases large international buyers) serve as a source of market information, product development, pre-financing and learning. The inside contracting exporters that have the benefit of engaging in collaborative trade relationship with the buyers are visible and also demonstrate some reasonable level of capacity and professionalism towards production for export (competence trust). They could be trusted not cut corners or behave dishonestly. Though these exporters remain a minute constituent in the industry, they are increasingly controlling greater proportion of the industry's total export volume. They are rare case of

medium-scale indigenous African exporters (often perceived as opportunistic and incompetent) engaging in collaborative and information-laden trade transactions with foreign buyers. This is a testament to the fact that given the right conditions (i.e. trustworthiness, professional attitudes towards work, and reasonable level of competence) qualitative trade transactions can be developed between international buyers and indigenous producers in societies that have long being characterized as having endemic market imperfections.

7.5 Conclusion

This chapter sought to explicitly relate the empirical evidence presented in chapters five and six to the theoretical expositions in chapter two. The three main areas discussed in line with the research objectives were the incidence of domestic market imperfections, the extent to which informal subcontracting relations enable the small scale exporters to overcome some of these market imperfections and the emergence of inside-contracting as another form of market coordinating strategy for dealing with agency problems as well as addressing quality control concerns. The theme that is consistent throughout the discussion is that informal subcontracting relations and ties enable the small-scale exporters to assemble the relevant resources and overcome some coordination challenges in their engagement in distant trade. However, new demand pressures emphasizing quality, speed and order volumes coupled with supply side constraints including subcontractors' lack of capacity, the threats of deceit and the lack of contract discipline makes the traditional informal contracting relations imperfect strategy for achieving success in the export market and to ensure firm's growth. Stated differently, under

conditions of market imperfections, laxity of control and enforcement difficulties, the fluid subcontracting relations and other informal ties can at best enable the small firms to achieve imperfect results, especially, when they are required to meet more demanding changes in the market. The other theme that emerged is that other exporters partially internalize functions in-house (inside contract) to minimize coordination difficulties, reduce high transaction costs and enforce compliance with product quality standards but to be able to sustain this arrangement requires reliable and predictable source of demand. The inside contracting system as practiced by the Ghanaian craft exporters is far from being simple; they maintain multiple informal and trust building relationships with segmented buyers as well as subcontractors to keep the system operational.

CHAPTER EIGHT

CONCLUSION

8.1 Introduction

The study set out to explore how Ghanaian craft exporters coordinate their production activities given the context of the micro-economic environment. The specific objectives were to identify the micro-economic circumstances impinging on the activities of the small exporters, the responses to these conditions in terms of institutional and market arrangements and the efficacy of the chosen arrangements in dealing with the prevailing socio-cultural and economic conditions. The study, which relied on the new institutional economics framework as its theoretical foundation (chapter two) demonstrated that informal and private institutional arrangements i.e. informal subcontracting relations and inside contracting system constitute the media through which the small-scale exporters seek to mitigate agency problems, gain access to working capital, labour, and obtain market linkages and export processing services. The informal and private arrangements play instrumental role in the trade transactions of the small-scale exporters; however, the informal subcontracting relations between the exporters and artisan subcontractors are being undermined by the very presence of market imperfections. Lack of geographic closeness makes it difficult to enforce and monitor informal contracts to avoid shirking and opportunistic risks. But that is not all to the difficulty of enforcing informal contracts between the small-scale exporters and their subcontractors. The artisan subcontractors are very often not in captive trade relationships; making informal sanctions such as the loss of future contracts ineffective. Again, there isn't a common platform of information sharing, for instance, at the industry level about rogue artisan subcontractors (blacklist

dishonest ones), which would enable the exporters to avoid making any contractual commitments to dishonest subcontractors. At another scale of the trading relationship, international buyers through the institutional arrangement they have established with domestic export intermediaries are to some extent able to overcome information problems and enforcement difficulties through the intermediary agents who hold special position in the production chain and are able to use punitive measures to achieve compliance. Likewise, the informal financial arrangements between the exporters and the bank seem to work well because of the bank's ability to reduce information asymmetries and minimize the risks of default by using the platforms of the agents and the trade association for screening, monitoring and enforcement. In both instances, the *position* of the agents and the association is an important enforcing element to the cohesion of the system. Effective enforcement (*power to enforce*) and monitoring are critical in enabling private and informal institutions to work better as market constraining mechanisms.

Other exporters seek to counteract enforcement difficulties by adopting inside-contracting system to reduce market risks and also to achieve economies of quality. Following the introductory section is section 8.2, which consists of the summary of the main findings of the study. This is followed by some policy prescriptions in section 8.3.

8.2 Summary of main findings

Studies that have delved into the instrumentality of informal and private institutional arrangements in Sub-Saharan Africa allude to their usefulness in enabling market transactions to take place by minimizing risks and ensuring the flow of resources. These

studies, however, are often restricted to the localized or the domestic market. This study adds to this emerging literature by testing the robustness of informal and private inter-firm relations beyond the scope of the local economic setting. This way, it enabled us to gauge how these local institutions and market practices fare in supporting trade transaction that extends beyond the local environment. In this direction, and as demonstrated in this study, private institutional forms are necessary given the current stage of development of the case study industry in facilitating market transaction between the exporters and their trading partners. That private channels offer the potential for success in the export market but for pervasive market imperfections and enforcement difficulties that renders relation-based contracting as ineffective coordinating and market constraining mechanism.

The spill-over effect of the informal subcontracting relations manifests itself in the form of the flow of export market information, access to labour, access to raw materials, design ideas and working capital. Private export agents also play crucial intermediation role in the subcontracting arrangements by linking the numerous craft exporters to the export market through buyer linkages platforms, quality monitoring and export processing services they provide to the exporters. The spill-over effects though helpful is also a source of disincentive for investment in new designs and labour training under conditions where products branding is not a common practice, copy rights and patenting laws are non-functional or non-existent and the local control of artisans very difficult to achieve. Also informal group mechanisms serve as substitute for conventional collateral for short-term loan as working capital but less acceptable as guarantee for long-term loan for

capital investment. Ambitious entrepreneurs seeking to expand their production base often encounter difficulties raising the required capital for lack of physical collateral.

Integration into the export market via various forms of personal subcontractual relations provides a source for enterprise growth. The study demonstrated that an exposure to the international market serves as a source of learning and access to new market information. Buyers' pressure and intense competition, especially from Asia, induces local firms to improve on their production process. The markets to which small firms in developing economies serve are often fragmented, small in size and rudimentary offering little for innovation and growth. The thinking therefore is that for small firms to grow beyond their local significance, they need channels that connect them to foreign demand or bigger markets (Hayami et al. 1998, Fafchamps, 1994). The linkages with foreign markets have provided some of the small exporters, who are largely informal operators and were mainly serving the restricted domestic and tourists' market, the opportunity to achieve some modest growth. This is peculiar in the context of the generally held view that microenterprises in Sub-Saharan Africa hardly grow to become even medium-sized firms. Feeding into innovate private trade channels that are linked to foreign markets presents the possibility for microenterprises to graduate to become medium-scale enterprises.

Finding new markets and buyers are therefore crucial if the exporters are to continue to stay in business and grow. Apart from relying on export agents for international buyers, there are other channels through which they seek buyers; either through participation of government sponsored trade fairs abroad often with financial assistance from

international development agencies or the exporters undertaking foreign trade fairs and exhibitions by themselves. Both routes have their own difficulties. As demonstrated in chapter 5, donor-sponsored exhibitions executed through government intermediary agencies are fraught with corruption. Prospective exhibitors sometimes have to pay bribes to government officials before they are given slots to attend trade exhibitions abroad. The government officials sometimes trade the exhibition slots to individuals or give them to relatives and friends wanting to travel abroad to seek greener pastures but are not known craft exporters. Directly undertaking retail and buyer exhibitions abroad by the individual exporters is potentially the effective buyer-contact development channels. However, private undertaking of these foreign trips regularly are expensive and beyond the financial strengths of many of the small scale exporters. Donor sponsorships for exhibitions abroad could yield positive results if directly targeted at visible private actors in the industry and where possible the support extended beyond market linkages programme to include effort aimed at helping the promising small-scale producers to build their local production capacities. Local NGOs and representatives of international development agencies could also play a crucial role in facilitating market linkage programmes.

Inside-contracting is a new institutional arrangement adopted by the “in-house” exporters to save on transaction costs, achieve product quality and meet delivery timelines. Products with complex quality dimensions left with difficult to monitor and uneducated artisan subcontractors in the craft villages would mean quality could be poorly enforced. From the perspective of the transaction cost model, inside contracting could be viewed

either as an alternative to, or an offshoot, from the putting-out subcontracting system. The study showed the relative strengths of both the traditional subcontracting arrangements and the inside contracting to enterprise success in terms of reducing transaction risks and addressing other forms of market imperfections. The exporters who have achieved modest increases in output sales against the backdrop of difficult market conditions are the ones that are partially internalizing functions within their production premises and have developed the internal capacity to be able to produce middle-ranked quality products. This gives theoretical strength to Coase (1937) and Williamson's (1975) position that the firm is better able to deal with high transaction costs under extreme uncertainties compared with arm's length market coordination arrangements. The firm that is being discussed here is far from the vertically integrated firm as predicted by the transaction cost framework. It is a quasi-firm that mixes the attributes of informal and external subcontracting relations with fluid control mechanisms instituted inside the entrepreneurs' production premises. This is a survival production strategy that is still embroiled in traditionalism.

8.3 Implications for Institutions and Policy Interventions

The thrust of this study has been that informal (private) institutional arrangements are less robust in helping to reduce agency problems under conditions of market imperfections and enforcement difficulties. Following from this, the logical thing to do implicitly is to seek institutions that are better able to deal with high transaction costs and expanding trade; possibly formal institutions. Regardless of this position, informal and private

institutional mechanisms would continue to persist as a number of theoretical and empirical studies suggest even in modern economies. The issue is not about replacing informal private institutional arrangements with formal institution. It is about improving the microenvironment for informal private institutional arrangements to thrive and the simultaneous incremental development of modern formal institutions in commensurate with the rate of expansion of trade transactions and the stage of economic development. Whiles recognizing that it takes time to build strong formal institution, Biggs and Shah (2006) proceeded to offer some policy options that could help African small enterprises in developing private institutional support arrangements. In their view, a prudent strategy for institutional development to support market exchanges should include intervention that makes the environment as supportive as possible for relation-based contracting, building on the existing private institutional arrangements to improve their efficacy and the development of other formal institutions to reflect the gradual transition from personal to anonymous market exchanges.

These areas of policy interventions are addressed to this study. The lesson learnt from this study is that subcontracting relations do not thrive well under unstable and weak microeconomic environment characterized by opportunistic risks, capacity constraints and bad socio-cultural practices. These factors weaken the incentives for inter-firm relations and thus limit the ability of the firms to create and sustain efficient subcontracting relations. Linkages programmes in which firms are linked to small scale subcontractors is gaining currency in policy initiatives in Sub-Saharan Africa with the effort aimed at building private support mechanisms for small enterprises' development

with donor assistance (see Kuada and Sørensen, 2005 on inter-firm collaborative initiatives between Ghanaian exporting firms and Danish firms). The sustainability of such initiatives, according to Biggs and Shah, is more than introducing one firm to another. They maintain that it should also entail trust building initiatives and efforts aimed at upgrading the capabilities of for example subcontracting firms. Trust-building initiatives should embody programmes that would enable small firms to understand the economic effects of eschewing short-term opportunistic behaviours and the long-term benefits of operating in professional and trustful manner in business transactions. In effect, such initiatives should stress not just inter-personal trust building but also seek to build competence trust e.g. build the capabilities of subcontractors so that they can deliver according to the quality standards they promise to deliver. Firms' capabilities and owners' backgrounds are important requisite for building successful inter-firm relations. For example, the craft exporters that have succeeded in engaging in qualitative relations with international buyers are the very firms that have shown an appreciable level of competence in meeting order requirements and the owners having a reasonable level of education. International buyers are confident doing business with local producers who have demonstrated reasonable level of competence. Likewise the local exporters would contract out production orders to subcontractors they can trust to have the capacity to produce according to contract terms. Improvements in the quality of subcontracting firms as well as lead enterprises would facilitate quality local and international inter-firm linkages. Exporter-buyer relationship could serve as important channels for exchange of market information about changes in demand trends and for learning about best practice methods of production and designs. Therefore initiatives aimed at building exporter-

buyer relationship would be an appropriate policy response in helping to minimize the problem of export market information asymmetries.

Training initiatives should also encompass government sponsored training programmes for artisan subcontractors en-mass at the industry level to improve their skills levels and to re-orient them to adopt work ethics that are in tune with the culture of the export market.

This study points to the insufficiency of informal and private arrangements in dealing with modest increases in the complexity of trade. It does not suggest for their replacement. With regards to the case study sector there has been a modest increase in volume of trade since its formative years as well as the increases in the complexity of quality dimensions driven by international demand but the evidence is not adequate to suggest that such modest increases would warrant elaborate formal institutional arrangements. Informal and private institutional arrangements would continue to be viable though there are limits to their sustenance under conditions of market imperfections. The pervasiveness of opportunism and mistrust that characterize the transactions between the actors runs counter to the notion of the abundance of trust or social capital that is often touted to aid economic interactions in less developed markets (Ensminger, 2000). Poor economic agents may yield to short-term temptations by cutting corners to survive present economic circumstances and therefore may place little premium on the gains of building long-term trade relationships.

We can extrapolate from this study, though cautiously, that formal institutions would be required as market widens and the scope of opportunism and complexity increases (North, 1991, Dixit, 2004, Biggs and Shah, 2006). Effective formal institutions would need to be developed to protect property rights, enforce contracts, reduce uncertainty and transaction costs and enable firms to appropriate gains associated with increasing scale of trade and specialization. Personalized trust is often assumed to be a major resource among the poor but as evident in the study it could be lacking among the poor and in underdeveloped societies. Under such a circumstance, Ensminger (2000) argues that serious economic development could be better realized through generalized trust embedded in formal government institutions and thus recommend attention to be focused on building formal institutions to generate generalized trust in such societies. Formulating intellectual property laws or effectively enforcing existing patenting laws and creating awareness of their existence could provide the institutional incentives for small-scale exporters to come up with innovative product designs that have greater marketability knowing that opportunists who attempt to expropriate their designs could face strict legal sanctions and penalties.

This study did not set out to examine the role of formal institutions in reducing transaction cost due to the initial disposition to explore the functionality of informal and private institutional arrangements to the craft export trade. This is not an attempt to underestimate the importance of formal public institutions in facilitating complex and impersonal trade transactions. As discussed earlier under chapter two, strong formal market support institutions are often nonexistent and the very ones that exist are weak,

unresponsive and poorly managed in developing economies of SSA. In the particular case of Ghana, an empirical study by Jackson (2002) revealed the internal capacity problems of formal third party institutions that provide business development services to the private sector. Lall and Pietrobelli (2002) also observed the financial and technical constraints that hinder the operations of state sponsored standards and quality assurance institutions in SSA. There is no clarity either about the efficiency and the effectiveness of the courts in SSA when it comes to the resolution of transaction disputes and contract enforcement. What makes for effective and market friendly legal framework in Africa is largely elusive? What mechanisms are required to make the legal system in SSA supportive of the private sector, especially the small and medium scale sector?

Most of the studies that have delved into the implications of global trade on developing countries, as exemplified in the global value chain literature, are often concentrated on the implications of global trade on (often ignoring the implications of domestic factors and circumstances on) coordination responses of suppliers, employment conditions and poverty reduction. This study, with all its limitations, draws attention to how success or failure in participating in global trade may not only be determined by the decisions and actions of, for example, global buyers, but also the organizational responses and actions of local actors, which are embedded in domestic institutional mechanisms and also shaped by microeconomic and socio-cultural factors. Domestic factors and efforts have implications for the extent to which small-scale exporters can successfully integrate into transnational commodity chains. The broad conclusion of the study is that under the conditions of imperfect microeconomic environment and endemic opportunism, informal

arrangements and loose arm's length subcontracting relation feebly enable the small firms to integrate into the export commodity chains. The inside-contracting exporters are seemingly better integrators into the export market. Since this study was more concerned with the effectiveness of inter-firm informal institutional arrangement, it failed to adequately address the micro impacts of export participation on employment and poverty reduction (Jenkins, 2005; Maertens and Swinnen, 2009). This area would require further investigation by looking not only at the craft industry but also the horticultural sector, where suppliers are required to meet stricter quality standards with far reaching implications for local capacities and livelihoods of small enterprises and workers. It will also be important to explore whether or not small-scale or large-scale production models hold the key for improving local livelihoods in the face of international competitive pressures and exacting buyer demands.

8.4 Conclusion

The study set out to explore how small businesses in the Ghanaian craft export industries coordinate their activities in response to local constraints to trade transactions and the requirements of the export market. Private channels via informal subcontracting and inside-contracting arrangements remain the primary tools for coordinating craft production for export. There are differences in the strengths of both private arrangements in enabling the small exporters to overcome local market imperfections and consistently meet the quality and timelines expectations of their clients. The observation in this study is that exporters relying on inside-contracting system are able to deal with quality issues

better than their counterparts relying on the traditional subcontracting and informal relations under the prevailing imperfect market circumstances. In particular, the informal subcontracting relations and mechanisms though key in enabling the small craft exporters to access resources and integrate into the export market, they remain largely imperfect arrangement. With improvements in the microeconomic environment subcontracting relations may offer the promise as a production strategy that may enable small business as little acorns to grow to become mighty oaks in SSA.

APPENDICES

Appendix 1: List of Respondents

Export Agents (craft)

Afripeche	E.K.Asamoah
Fritete	Robert Ellis
Sankofa	Nana K. Agyemang
Getrade	Nii Ankra Aryee
Delata	Mawuli Akpenyo
Kraft Export Consult	Robert Darko

Craft Exporters

L’afrique Concept	Hetty Zakour
Katalvic Industry	Ramseyer Agyarko-Nyamekye
Tekura	Mrs. Josephine Forson
Neocraft	Kwesi Asante
Treasures of Africa	Tina Ellis
Unity and Progress	Stephen Acheampong
Agyadu Creations	Joseph Boateng
African Dreams	Ralph Ashong
Kottage Originals	Ofoli Ahinakwah
Boassan Ventures	Edward Akwesi Boateng
Delhause	Del Boampong
Lorenpee	Kwasi A. Antwi
Wild Gecko	Poem van Landewijk
Celebate Services Ltd	Myles Quainoo
All round marketing	R.K Adjasoo
Hide-Out Enterprise	Ms Grace Mensah
African Version	Nanasei Opoku
Joad Enterprise	John Apau Pinamang
Papsay Enterprise	Alhassan Abukari
Afwel Ltd	Mr Coleman
Marks Impex	M.W. Hanson
Echoing Hills	William Agbeti
AACD African Market	Stanley Felten
Al-Tatma Enterprise	Alhaji T.A.Tahiru
Acarv Enterprise	Rev Apraku
Christian O Enterprise	Christian Okyere
Frank-Pee	
Ahenfo Classics	
Eleagbe Enterprise	
Eddison Sculpture	
Alahet Trading Co.	

Machine furniture exporter/producers 4

Scanstlye Mim Ltd	Samuel Nick Ayison (Operations Manager)
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Irokko
Ashanti Furniture
Furnart Ghana Ltd

Celia Cann-Anaman
Kwasi Appiah
E.G. Wellington

Lists of informants

Marcu Clottey (AMC quality Compliance Inspector)
Bridget Kyerematen-Darko
Maxwell Osei-Kusi
George Adomako
Julius Yaw Mensa (Pseudonym)
Adu Mensah

Lists of organisations contacted

Presidential Special Initiatives Directorate
Prudential Bank
Aid to Artisans Ghana
Ghana Export Promotion Council

Appendix 2: List of Buyers Identified by Exporters

Appendix 2 is not available in the digital version of this thesis

Appendix 3: Interview Guide for the Focal Enterprises

This guide for the field interview is derived from the literature on the link between inter-firm relations and the flow of resources through the linkages. The individual items in the

guide are grouped into themes that reflect firm histories, the nature of inter-firm relations, meeting quality standards

1. Firm-level Data

Date of interview

Firms Name

Name of Respondent

Position

Address/Production site

Tel/Email

Product or Process specialisation

1.1 Firm's History

Date of establishment

The person or entity that established it

Ownership/Legal status

Critical periods in the history of the firm i.e. periods of boom and busts

1.2 Labour force

Size of labour force and changes from its day of establishment till date

Size of Management/ Owner(s) and Background

Skill background of employees or technical staff

Sufficiency of skill levels to market demands of products and processes

Mode of acquisition of skills by management/owner and workers

Labour sharing with other producing firms

1.3 Performance

Annual output from the date of establishment or since the last 10years

Volume exported and volume sold in the local market

Trends in export volume from the date of establishment or the last 10years

Unit price (US\$) of export and changes over time

Turnover

Improvements in product and process quality

Effect of product and process quality on turnover

1.4 Finance

Main source(s) of finance

Inputs purchase on credit or cash payment. Duration for repayment of inputs if on credits

Use of letters of credit in business transactions

Output sold for cash or deferred payments

2. Inter-firm linkages

2.1 Linkages with Processes subcontractors

Contract out components, processes or whole products

Major subcontractors (name and location)

Reasons for subcontracting

Description of the relationship with the subcontractor,

- Frequent orders to subcontractor (how often)
- Irregular orders (how irregular)
- Single batch orders (arm's length)

Intention to carry out all production processes in-house and reasons

Other ways production is/could be organised

The capability of subcontractor to meet order requirements

Consequences for failure to meet orders

Specific supports provided to the subcontractor(s) and why these support activities aren't carried in-house if subcontractors don't have capability in this area

- Product development
- Skills and technology
- Quality management
- Input supplies

2.2 Focal Enterprise as Subcontractor

Main clients and location (Domestic and International)

- Other producing firms
- Retailers

- Wholesalers

The main product or processes contracted out to (FE)

The description and the history behind the relationship with the client (repeat as in 2.1)

Support benefits from subcontractor (repeat as in 2.1)

Other ways of accessing benefits to boost performance apart through the linkages

2.3 Linkages with the Market (Export Agents/ Traders)

Business relationship with export agents and Traders

Name and Location of your main Agents and Traders

Reasons for selling through agents

Description of relationship with Agents and Traders

- Frequent and dense and reasons
- Occasional, arm's length and weak and reasons

Would you have wished to sell direct to customers and reason

Benefits from the Export agents and Traders (strong ties)

- Market access
- Provision of market information
- Product development
- Finance
- Quality Management
- Training of workers(in product development, quality management, technology diffusion and adaptation)

Perceived benefits from weak ties with agents and traders

2.4 Linkages with Input suppliers

a) Suppliers of raw materials, major suppliers and location

Frequency and reliability of raw material supplies

Raw materials meet expected quality requirements

Difficulties arising from supplies and reasons

Mode of payment for supplies

Consequences of supplier failure to meet quality and delivery requirements

Collaboration and information sharing to improve quality

b) Major suppliers of equipment, machines and tools

Description of the linkages with equipment suppliers

Collaborative benefits in the areas of;

- Information on new equipment
- Providing training for workers to adapt to new technology
- Repair of machinery.

**2.5 Linkages with other firms producing similar products (horizontal linkages)*

Cooperation with other producers of similar products (Name major ones & Location)

- Areas of cooperation
- Machine lending
- Product Development
- Purchase of inputs
- Sharing of orders with other producers
- Sharing of workers

Forums for exchange of information (e.g. Meetings of Business Association)

Inter-firm competition

Main competitors and location

- Large firms
- Medium firms
- Small firms

Competitive strengths

- Product quality and design
- Speed and Punctual delivery
- Price

Detailed benefits that could be accessed through the linkages or through other alternative means

Product Development

Type of designs (e.g. authentic traditional designs or functional designs that combines traditional designs with designs with foreign functions, foreign designs)

Sources of Design

Developed locally

Developed by external designer

Design offered by clients

Designs introduced with inputs from international/local consultants

Ideas for the designs sourced through

Local fairs

Trade fairs abroad

Catalogues and magazines

Specifications from clients

Quality Standards (sector specific)

Quality Standards

Product-specific standards

Quality Management

Quality training

Quality monitoring and control

Standards setting or specification and enforcement

Who sets and enforce standards (clients, external independent bodies, private consultants, enterprise itself, business association, or NGOs).

Technical expertise to the implementation of standards or skill support to raise quality.

Appendix 4: Recession in the West Cuts Off an Economic Pipeline in Ghana

By Karin Brulliard

Washington Post Foreign Service

Wednesday, August 5, 2009

ADUASE, Ghana -- When the U.S. housing crash triggered economic chain reactions around the world, one ended in a lush forest near this village, where on a recent day

Appendix 4 is not available in the digital version of this thesis

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