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Why Do Firms in Developing Countries Have Low Productivity?

By NICHOLAS BLOOM, APRAJIT MAHAJAN, DAVID MCKENZIE, AND JOHN ROBERTS

The productivity of firms in developing countries appears to be extremely low. [Table 1](#) reports GDP per capita and average firm-level sales per employee in manufacturing—commonly known as labor revenue productivity—across a sample of countries from a new international firm database (ORIBS). While there are some data comparability issues, the broad message seems clear: developing-country firms have lower levels of labor productivity.

Prior work, such as that summarized in James Tybout (2009) and World Bank (2009), has highlighted a set of issues around infrastructure, informality, regulations, trade policies, and human capital that reduce the productivity of firms in developing countries. In this short article we want to focus instead on three other areas which recent research has emphasized: management practices, financial constraints, and the delegation of decision making.

To summarize: we find evidence that firms in developing countries are often badly managed, which substantially reduces their productivity. This appears particularly important in larger firms (100+ employees), which are operationally complex so that effective coordination and motivation require formalized management practices. We also find that financial constraints are a binding factor for growth, notably in smaller firms. In larger firms, which often appear to have already overcome financing constraints, another growth constraint arises in the inability of firms to successfully decentralize decision making. In developing countries owners tend to make almost all major management

Table 1—Average Firm-Level Revenue Productivity across Countries

| Country | GDP per capita, dollars | Sales per employee, dollars |
|-------------|-------------------------|-----------------------------|
| US | 43,736 | 453,684 |
| UK | 37,896 | 437,678 |
| Japan | 35,699 | 429,336 |
| France | 35,293 | 393,024 |
| Germany | 33,838 | 379,346 |
| Canada | 32,480 | 350,829 |
| Poland | 7,967 | 178,325 |
| Spain | 4,787 | 144,876 |
| Colombia | 1,170 | 130,898 |
| Ecuador | 2,884 | 71,263 |
| Mexico | 1,952 | 105,278 |
| China | 1,361 | 96,985 |
| Indonesia | 1,249 | 80,305 |
| Philippines | 1,090 | 82,975 |
| India | 761 | 120,056 |

Notes: GDP per capita from the IMF 2005 in PPP. Sales/Employee in current dollars, across all firms in the ORIBS database, using the most recent accounts. Full underlying data available at: <http://www.stanford.edu/~nfbloom/ITF.asp>.

decisions because of fears of expropriation by their managers. But, because the owners' time is limited, they have the capacity to make decisions for firms only up to a certain size. Thus, without delegating decision making these firms find that growth becomes unprofitable, or even impossible, because decisions are constrained by their owners' time. This suggests that the results of Eric Berchman, John Haktwangar and Stefano Scarpetta (2009) and Chang-Tai Hsieh and Peter Klenow (2009)—that productive firms in developing countries like India and China do not expand as rapidly—due to a mix of financial factors (particularly for smaller firms) and organizational factors (particularly for larger firms).

I. Management Practices

There has long been a suspicion that poor management practices have held back the productivity of firms in developing countries. Indeed, even among industrialized countries,

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