



SUDAN ECONOMY RESEARCH GROUP
DISCUSSION PAPERS

**The Role of Home Based Enterprises (HBE's)
in Alleviating Sudanese Urban Poverty and the
Effectiveness of Policies and Programmes to
Promote HBE's.**

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Republic Of Sudan



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Appreciations:

ACCORD	Agency for Co-operation in Research and Development
BOS	Bank of Sudan
CPI	Consumer price Index
DUGAP	Dutch University Gedaref Assistance Programme
GDP	Gross Domestic Product
HBE's	Home-Based Enterprises
ICDB	Islamic Co-operative Development Bank
ILO	International Labour Organisation
IMF	International Monetary Fund
LS	Sudanese pounds
MNE	Ministry of national Economy (Sudan)
MSP	Ministry of Social Planning (Sudan)
NCS	National Comprehensive Strategy (Sudan)
NGOs	Non-Governmental Organisations
NIDGB	Nelein Industrial Development Bank Group
PFBs	Productive Family Branches (of the SIB)
SIB	Sudanese Islamic Bank
UNDP/ADS	Area Development Scheme (of the UNDP)
UNIDO	United Nations Industrial Development Organisation

Abstract:

The long lasting crisis of the Sudanese economy is obvious and the search for strategies to reduce poverty is urgent. The paper highlights the role of Home Based Enterprises (HBE's) in the Sudanese economy and discusses the possibilities to reduce poverty by promoting HBE's. Current programs and policies in place are analysed and policy suggestions are given. The main conclusion is that promotion of HBE's in particular via the various ways of Islamic finance offers a chance for economic development and poverty reduction in Sudan, but programs and policies in place are mainly driven by foreign NGO's and governmental support is too poor.

1. Introduction

The aim of this paper is twofold: The assessment of the role of Home-Based (HBE's) to poverty alleviation in Sudan, and the review of the major policies and programmes to help HBE's in Sudan. Section 1 outlines the economic conditions, and the volume of poverty in Sudan. Section 2, tackles the employment contribution of HBE's. Institutions, policies and programmes to promote HBE's are in section 3. We choose to review the efforts of different institutions (namely the banking, official and NGOs efforts). Section 4 assesses these efforts to promote HBE's for Urban Poverty Alleviation in the Sudan. Concluding remarks are made in Section 5.

2. The performance of the economy and the crisis of poverty in Sudan.

The Sudanese economy has been in the grip of a crisis since the 1970s. During the period 1970-2 Sudan attempted a breadbasket strategy to restructure the export sector by producing food, sugar, textiles and meat for export — and to promote import substitution. The strategy is an export-led, agro-industrial strategy, based on the belief that Sudan could, given adequate financial support, develop its vast untapped agricultural resources to provide food security for the Middle East through a combination of Arab funds and Western technology (Ibrahim, 1992a). This highly ambitious programme led to huge inflows of capital mainly from Arab states through bilateral agreements.

By the end of the 1970s, however, the economy was in a crisis. As a result of an increase in government development expenditure, the budget deficit rose by almost 100%. The balance of payments deficit increased from 2 to 5 per cent of GDP. Exports fell from 15 per cent to 11 per cent of GDP. The real growth rates started to decline (Ibrahim, 1992a). The inflow of capital from oil-rich Arab countries decreased, and as the grace periods of the loans reached their end, severe economic crisis emerged. After 1978, Arab oil-producing countries started to make fund disbursement to Sudan subject to IMF/World Bank conditions. The deterioration of the economy continued during the 1980s and the 1990s, after the liberalisation strategy, which was pursued starting 1992.

The current economic situation is not that much better than it was in the late-70s, early-80s. The country's current account balance of payments deficit has reached over

US\$800 million. The parallel exchange rate deteriorated after 1992, the year when economic liberalisation measures were declared. During the period 1992-1995, the exchange rate deteriorated seven times. The current exchange rate is over LS 2660 per dollar, up from only LS 18 in the late 1990s. Money supply increased by more than 30 per cent annually during the past decade. Official annual inflation rates exceed 100 per cent, but the actual rates are greater than that figure.

Unemployment, rural-urban migration and immigration further aggravated the difficulties of the economy. As a result of the change in age structure and the increase in women's participation in economic activities, the annual growth rate of labour force increased from 3.9% during the 1980s and the early 1990s, to 5.9% during the last few years (Republic of the Sudan, 1997). Sudan also suffers from rural-urban migration as a result of drought, desertification and civil war. Estimates of the 1993 population census show that 25% of population are urban (Department of Statistics, 1993). Recent statistical evidence of the Department of Statistics (Quoted by the Republic of the Sudan, 1997) shows that the urban population is 32%, 43% of them living in the capital, Khartoum. According to the 1993 population census, population in Khartoum has doubled ten times from what it was in 1956, while the population in other major cities has increased by four to seven times. Sudan has also been a host to refugees for about a quarter of a century from certain neighbouring countries because of civil wars, drought and famine. Total refugees are now estimated to be over a million, 50% of whom do not receive assistance from the UN (Republic of the Sudan, 1997).

The deteriorating economic conditions together with unemployment and migration necessitate measures to enhance employment and income. Micro-enterprises, of different types and sub-sectors, constitute one important strategy in Sudan to eradicate poverty. Researchers are concerned with the absolute poverty line concept i.e. the bundle of basic consumer goods required, in addition to other expenditure on health, education, housing etc. Sudanese measurements of the absolute poverty line are LS 3,947 and LS 203,818 in 1990 and 1996 respectively (Nour, T. 1996). Other earlier estimate (Ministry of Social Planning, 1997) shows that the poverty line was LS 777 in 1978, raised to 6384 in 1986 and further to LS 27000 in 1993. The cost of living over the same period was escalating. The CPI was 10.2, 82.9 and 3691.9 for the years 1978, 1986 and 1993 respectively. The rate of inflation in Sudan has reduced recently to around 10% only. Moreover, the growth rate of the number of poor families was estimated to be more than 4% annually. The income-expenditure gap is estimated to be 200.7

% (that is the expenditure is more than twice the average income) and increasing over time. Studies (Nour, T. 1996) indicated that the bulk of Sudanese are in absolute poverty ranging between 85% and 94%, and the rich-poor gap is growing. Recent studies show that 86.5% of urban dwellers are classified as “poor” (MSP, 1997).

3. The employment contribution of HBE’s

The role of HBE’s in alleviation of poverty can be seen from the contribution of different small enterprise sub-sectors. In fact, small-scale enterprises such as home-based unincorporated small-scale sector, productive families, informal (officially unregistered) sector, income-generating activities, craftsmen and small-scale and micro industries, comprise HBE’s.

Sudan’s industrial sector constitutes not less than 5 per cent of the total labour force, and about 8 per cent of GDP and less than 1 per cent of the total exports — mainly semi-processed goods (BOS, 2000). Among the industrial sub-sectors in Sudan are small-scale industries - defined by the total employment of less than 25 workers. According to the outdated Industrial Survey (Department of Statistics, 1970) small enterprises have a major contribution to Sudan’s industrial sector, sharing 95 per cent of the total industrial establishment. Small-scale industries (including HBE’s) accounted for less than 10 per cent of investment in the industrial sector, but more than 35 per cent of gross manufacturing output, and constituted nearly 50 per cent of the industrial revenue. They need less capital measured by the average investment per enterprise, yield an annual output of three times the level of investment, and need about half the investment of large-scale industries to create one job (UNIDO, 1996).

The “informal sector” first appeared in the 1970s, following a huge migration influx from rural to urban areas as the result of unequal development, wars and drought. There is no up-to-date information on the volume and role of the informal sector in Sudan. The ILO Report (1976) showed that self-employment in this sub-sector contributed between 25 and 30 per cent of employment in urban areas, and the annual growth rate was shown to be 45 per cent. In 1986, another ILO report re-emphasised the importance of the informal sector and estimated its contribution to be 60 per cent of the total urban employment (ILO, 1986). The role of women in the informal sector was estimated to be 12 per cent in 1990, up from 2.9 per cent in 1983 (Idris, & al-Faki, 1993).

As a result of the difficult economic situation in recent years, many families have moved towards HBE's. The number of those engaged in micro-enterprises as productive families constitutes a huge proportion of small enterprises in Sudan and this number is increasing all the time. Because of the lack of statistical data, it is difficult to determine exactly the contribution of productive families.

NGOs started programmes for refugees and migrants, specifically home-based income-generating activities for women with the aim of creating income and employment opportunities. This has been achieved by revolving funds, and by charging very low interest and administrative charges, without noticeable guarantees. According to our observation, more than 100 local and foreign NGOs are presently active in providing income generating credit, counselling and training programmes to tiny home-based enterprises.

4. Institutions, policies and programmes to promote HBE's

4.1 Official efforts

The state policy to promote HBE's in order to mitigate poverty in Sudan is mainly reflected in the National Comprehensive Strategy, NCS, 1992-2002 (MNE, 1992). One major objective of the NCS is to encourage micro – enterprises as a tool to combat poverty. A target to provide 2 million poor with the means of production was set at 200,000 poor families a year. To achieve this target the Ministry of Social Planning established the Council of Co-Ordination of Productive Families and Environmental Industries in 1993, which determines policies and programmes and mechanism to finance productive families. In its efforts to combat poverty the Ministry of Social Planning, in co-ordination with the Ministry of Industry, established the Supreme Authority to Promote Small-Scale Industries in 1995. The aim of the Authority is to co-ordinate official and technical efforts. Government efforts include the work of some local social funds and local NGOs, which are established to serve specific religious, social and economic goals. Among other activities, they are also engaged in providing small-credit for living-provision, home-based projects (such as leatherwork, cloth-making, tailoring, macaroon production and poultry production) especially for poor, widowed, divorced and deserted women in the displaced areas around the big cities. Other government efforts to combat poverty include different funds to serve specific religious, social and economic goals.

The *Zakat* fund, which annually collects slightly over 1% of the national income of the country, is also involved in small enterprise financing. In 1995, nearly LS 2 billion (29% of the *Zakat* fund allocated for the poor in that year, and slightly over 1% of the country's national income) were allocated for the provision of the means of production for HBE's.

4.2 Banks

Funding small HBE's has been seen as a challenge all over the globe. A multitude of financing schemes has been in operation for many years in different developing countries. Experience shows that financing small and micro-enterprises is hampered by the absence of collateral, the high risk of default on loans and high administrative costs. One of the major developments in Muslim (and non-Muslim countries as well) in the last two decades is the emergence of Islamic banks. Their estimated assets are around US\$ 100 billion and, today, they share over 15 per cent of the total market's assets (Yousif, T., 1996). Sudan is a country where the whole banking system has been converted into Islamic banks. The Sudanese Islamic banks are rare examples of formal institutions, which manage to utilise Islamic financing formulae to provide venture capital to small entrepreneurs including those who work at home.

4.2.1 The usefulness of Instruments of Islamic Finance to HBE's.

Instead of paying a premium by the borrower to the lender along with the principal amount as a condition for a loan, Islamic banks mix capital and skills and share the risk and the resultant profit or loss. Here it is only the profit sharing ratio, not the rate of return itself that is predetermined. More than one major mode of finance have been in operation such as *Murdaraba* — agency joint venture/limited partnership; *Murabaha* — purchase or resale of debt/mark-up/deferred payment sales;¹ and *Musharaka* — joint partnership, credit/partnership, which also take another form, in which the bank can enter into partnership with the client on the basis of diminishing *Musharaka*, through which the full ownership of the business assets passes to the partner after a certain period. Under this type of agreement, the client is given the right to gradually buy, as much as he can, from the bank's shares until

¹ Islamic banks also resort to other modes of finance on a deferred payment base (*Bai'muajjal*), leasing (*Ijara*), and pre-paid purchase of goods (*Bai'Salam*) to name a few. These and other modes of finance are not used in the Sudanese banking system, or when used, are not applied to HBE's.

he/she becomes the sole owner of the asset, providing the following apply — if the total cost of the project is 1,000 currency units and the client's share is 50 per cent and if the project is divided into 10 shares each equal to 100 currency units. At the end of each financial period, if the partner buys the bank's shares, and if at the end of the first year he/she buys shares, then his/her ownership in the second financial period will be 60 per cent, while the bank's ownership will be 40 per cent. This will continue until the client becomes the sole owner of the project.

Islamic financing modes are better suited for meeting the needs of small enterprises. No strict security is demanded, as Islamic investment arrangements put great emphasis on the transaction itself, rather than the creditworthiness of the partner (Ibrahim, 1997). If the operation ends in a loss the partner does not bear this loss alone. If he or she is unable to settle his or her bills, a grace period is given without any additional fees. Islamic financing does not require the partner to present securities against possible losses. Since the Islamic principle is basically based on profit and loss sharing arrangement then “any security demanded by the Islamic bank is against possible fraud or repayment-evasion, and not against the risk of losses”(Awad, 1994).

Partnership financing has many advantages to offer to small home-based entrepreneurs. *Musharaka* is a flexible, fair, easily understandable form of financing. It caters for both production and management, thus leading to increased incomes for income groups who do not own capital. It is a suitable mode of financing for both working and fixed capital. In countries with high inflation, *Musharaka* preserves the real value of capital invested — that is, at the time of selling the two partners may decide to wait in anticipation of higher prices. *Musharaka* does not require strict collateral guarantees and does not leave the partner with a heavy burden of debts, post-dated cheques or any other kind of obligations. Personal acquaintance with the client, and his behaviour, in addition to continual supervision and follow-up by the bank's management, are necessary requirements in the absence of conventional guarantees.

4.2.2 Banking and government financing policies of HBE's

In Sudan, the partial recognition of the small enterprise sub-sector started at the beginning of the last decade. The Financing Policy (Islamic Credit Policy of the Central Bank of Sudan) of 1990, for the first time, included crafts as one of the priority sectors for financing. The full recognition of the small enterprise sub-sector started with the 1994/95 Financing Policy, "craftsmen, professionals and small producers including productive families" is considered one of the priority sectors for banking finance (BOS, 1994/95) The Financing Policies included the following concessions and financing regulations to this sub-sector.

- a) Specification that finances to this sub-sector may be based on the restricted *Mudaraba* or other financing systems. Financing per transaction may not exceed 1 million Sudanese pounds raised to 3 million in 1995. Banks are free to obtain whatever "sufficient guarantees" they need when financing this sub-sector.
- b) In financing Policy 1994/95, the first instalment of *Murabaha* for small enterprises was determined not to be less than 15 per cent of the value of the asset. The Financing policy of 1994/95 permitted that the first instalment of *Murabaha* can be delayed and be paid as part of the total instalments. Starting from the 1995 Financing Policy, the first instalment is cancelled and the payments can be arranged between the bank and the client.
- c) In the financing policies of 1994/95 and July-December 1995, the percentage of participation in *Musharaka* of finance granted to craftsmen or professionals must not to be less than 15 per cent of the bank's total funding. In the case of small producers the percentage of participation is left for mutual agreement between the bank and the partner. In the Financing Policy of 1996, the small entrepreneur's percentage of participation in *Musharaka* must be 10 per cent. For craftsmen and professionals, the percentage of participation is still 15 per cent. In the 1996 Financing Policy, the percentage of participation for professionals and craftsmen was raised to 25 per cent, and that for small producers was raised to 20 per cent. The percentage of participation for professionals and craftsmen was raised to 30 per cent. As for small producers, the partner's participation shall be a maximum of 25 per cent.
- d) The minimum *Murabaha* margin in 1994/95 and 1995 was 15 per cent per annum, raised to 30 per cent for professionals, craftsmen and small producers, and 20 per cent for

productive families. In 1997, the two margins were 35 and 30 per cent respectively. The Financing Policy of 1998 unifies the minimum percentage of profit margin under the *Murabaha* system for all priority sectors at 30%, while leaving the minimum percentage margin under the *Murabaha* system for non-priority sectors undetermined.

e) Exemptions of craftsmen, professionals, small producers (including productive families) from registration certificates, audited statements and profit and loss accounts in the case of financing of less than LS 5 million.

The successive financing policies determined the financing ceiling for priority and other non-priority sectors. The agricultural sector was granted 40 per cent, but no specification for the other priority sectors, including craftsmen, professionals, and small producers including productive families was given.

In accordance with the Financing Policy of the Bank of Sudan, and the national financing policies, the Sudanese Banks determined their internal financing policies for financing small producers to ensure successful projects, consolidate the application of the central bank regulations and make sure the success of the marketing of the output and so on. These conditions include socio-economic surveys of applicants, checks for debts and a review of the marketing experience of the loan applicant. In addition to other fees, the national policies requires banks to comply with Tax and *Zakat* clearance certificate and other government fees and duties namely: 2% Finance Tax of investment operations, 0.001 per cent management fees on investment operations, 0.005 per cent fees out of the total finance, and 0.025 per cent charge of stamp duties. The burden of taxes can be seen in a real case of laundry soap financed through *Musharaka* at the Sudanese Islamic Bank in 1997, with the contribution of the bank and the partner were LS 500,000 and LS 62,000 respectively. In this case we calculated the following banking and government fees: finance tax LS 10000, Stamp Duties LS 2,500, Bank Commissions LS 1,935, Administrative Fees LS 500, Total Fees LS 14,935 (Ibrahim, 1997).

We are hastening to show the following observations:

- a) Government fees (finance tax and stamp duty, equivalent to LS 12500) constitute about 84 per cent of total fees.
- b) The total fees paid equals to around 3 per cent of the contribution of the bank and 24 per cent of the contribution of the partner.
- c) In addition to the above, small producers are burdened with the presentation of tax and *Zakat* (alms tax) clearance certificate.

4.2.3 Banking finance to HBE's

Here the experience of some selected Islamic banks in Sudan will be reviewed. The Sudanese Islamic Bank (SIB) is the first bank in Sudan that initiated and opened family specific branches in urban residential areas to extend capital to small home-based enterprises.² The first specialised branch was opened in a normal house in Omdurman in May 1992. A second branch of the same kind was also opened in Wad Medani, a town south of Khartoum. Because of the success of the initial branches, the bank opened a model branch in March 1994 to cater for two districts in Omdurman City. Although the structure and the general features of the branch have not changed, the new model branch was meant to address the major outstanding constraints. Encouraged by its success, the bank has also decided to open four other similar branches in other parts of the capital. In financing productive families the privately owned Sudanese Islamic Bank (SIB) has the following aims:

- a) The consolidation of the sense of social justice and solidarity (*Takaful*) among the members of the society.
- b) Participation in investment in ways that benefit the local community.
- c) Promotion of banking awareness, and help in developing the sense of saving money.
- d) The use of the largest possible portion of the available fund in income-generating activities (Ibrahim, B. and Khalifa M. Osman, 1994).

Deposits at the three branches are in the form of current accounts and family savings accounts. Total deposits in the three branches reached LS 84 million by the end of December 1994. Around 73 per cent of the volume of deposits is in the form of current accounts, and 27

² The idea behind Productive Families' Branches is similar to the idea of a social or ethical bank, which viewed that at least 'some financial institutions need to be kept small and should be designed to serve particular communities and investment policies', *The Economist*, 25/12/93; 7/1/94:105.

per cent is family saving accounts. There are 440 current accounts, compared with 72 family saving accounts. Up to December 1994 over 500 projects (mainly women's projects) were financed in the three branches, with normal project financing not exceeding LS 500,000. Since their inception the branches have invested over LS 40 million in family-based projects (Ibrahim, 1995). About 17 per cent of these projects were financed through *Musharaka*, in which the bank's share is 20 per cent of the total money invested. *Mudaraba* constitutes only 6 per cent of the total finance. *Murabaha* is the most dominant financing mode in the productive families' branches, comprising about 74 per cent of the total finance. Most of the partners are depositors, but not all depositors are using the bank as a source of finance. Projects financed cover a wide range of home-based small urban enterprises such as tailoring, food processing, shoe, soap making, chalk, cheese-making, goat and poultry-keeping, petty retail trade and some informal sector activities, such as local bread making.

The SIB experience in financing productive families has brought with it some innovations in banking. This new banking convention has reformulated the bank-client relationship with regard to regulatory control. Thanks to the nature of the *Musharaka* operations, bank-partner relations are much closer and more cordial than is possible under the conventional banking system. Moreover, in *Musharaka* the partner gains some advantages to his/her business such as obtaining good quality raw materials at reasonable prices; and also acquainting him/her with how to operate a business, dealing with a bank account, and maintaining proper business accounting records. The system also allows for flexibility in dealing with small investors, since the objective credibility of the applicant, well known through the field survey, is more important than the ability of the client to repay his debt. Thus, no court cases have been incurred through this method up to now. The failure cases are not related to the repayments of debts, but to other social and marketing/ follow-up factors. The Productive Family Branches (PFBs) experiment also widens the use of the branch buildings to marketing the products there and sometimes using them for production.

The only formula for financing small producers in Islamic Co-operative Development Bank ICDB is *Murabaha*. *Murabaha* is used for loans not exceeding LS 400,000, and it has a duration of up to one year, with a maximum grace period of two months. Repayment is made in equal instalments, every month or every three months. The margin of *Murabaha* is 3 to 4 per cent monthly. The ICDB finances urban craftsmen through a special fund, which was valued at LS 88 million in 1992-93, including funding for home-based blacksmiths, carpentry,

fishing boats and oil mills. Financing home-based productive families was estimated to cost LS 41 million, mainly poultry, cows, manual looms, tailoring, needlework, soap-making, grain-mills and sweets. The bank's finance to craftsmen, productive families and small producers reached 10 per cent of total finance between 1991 and 1993. According to our observations the guarantee policies of the bank are flexible. The bank accepts a personal guarantee from a third party through cheques. Other guarantees include storage of raw materials and assets.

The basic formula for financing small enterprises, including productive families, in the Nelein Industrial Development Bank Group NIDBG is *Murabaha*. The range for the loans is from LS 500,000 to million-and-a-half. *Murabaha* can be extended up to 21 months, with a grace period of three months. Repayment is made by equal instalments, either monthly or quarterly. The *Murabaha* margin ranges from 3 to 4 per cent per month for the small enterprise sector, though it is higher when the amount of finance is LS 1.5 million. The bank accepts personal guarantees by third parties and social funds. NIDBG financing of small enterprises amounted to LS 442 million in 1992, representing 4.4 per cent of the bank's total financing. In 1993, the amount reached LS 839 million, representing around 7 per cent of the total financing. NIDGB has financed more than 465 projects in the field of productive families, small enterprises and crafts during the period 1989 to 1992. Projects financed included cheese, yoghurt, local bread, biscuits, and sweets, tailoring and needlework, leatherwork, and soap making (Ibrahim, et. al. 1995).

Although the Sudanese banks use all modes of Islamic financing, *Murabaha* is the most commonly used method. It has used up to 90 per cent of the time in some banks. On the other hand and compared with other private banks in Sudan, SIB tried to use *Musharaka* as one of its major financing formulae, based on the belief that the Islamic system is principally one of partnership. *Musharaka* constitutes about 20 per cent in the SIB. Other banks, however, rarely use it. Banks prefer *Murabaha* because it guarantees a given return on capital invested, and the bank does not have to bother about the supervision and management of the project. In the bank's view, *Murabaha* is safe both for profit and for repayment³. *Murabaha* margin for small producers in general ranges between 3 to 4 per cent per month, above the

³ Islamic banks in general have shown strong preference for 'mark-up' devices. According to Yousif, T., (1996), 'The evidence indicates that the majority of Islamic banks do not uphold the fundamental principles of profit-and-loss sharing; instead, the bulk of their financing takes on a debt-like character similar to that in conventional financing'.

minimum margin of 15 per cent per annum stated in the financing policies. The repayment methods are also different than those stipulated. The financing policies, as we have previously mentioned, state that banks are free to obtain whatever “sufficient guarantees” they require when financing this sub-sector. Banks resort to traditional guarantees such as personal guarantees, post dated cheques, and third party guarantees (Ibrahim, 1994).

There are variations in the total volume of finance to small and micro-enterprises by Sudanese banks, and similarities in the volume of finance per project. Although the target group is small producers, banks separate it into different categories such as productive families, crafts, informal sector and so. There are no separate rules and procedures of financing female-owned enterprises, despite the growing phenomenon of women entrepreneurs.

4.3 Social efforts

In Sudan, apart from institutional financial support by banks, a plethora of social schemes to provide micro-credit for the poor have historically been in operation. *Khatta or sanduq* (savers/investors self-administered revolving fund) is the most popular and widespread social effort of an informal savings and credit scheme. It is a self-managed system in which individuals contribute an agreed sum (*Sarfa*) at regular intervals. The pooled amount is distributed in an agreed order, and used mainly (but not wholly) for small home-based businesses (rent, purchase of equipment/utensils, working capital etc), (Safa, E., 1997). *Khatta* gives individuals access to a lump sum, which could otherwise be difficult to accumulate. It serves multi functions for the poor: it encourages small savings, consolidate the solidarity of the saving groups and provides small credit without guarantee in convenient time and space. Apart from *Khatta*, village traders provide another way in which micro-enterprises are funded. They represent one of the most flexible and traditional financing institutions. They require only personal guarantees, but operate with high profit margins. Another form of these small enterprise funding is the “traditional partnership” in the means of production. In this system, a relatively poor small entrepreneur gets access to the means of production. Returns are distributed equally between the factors of production. Provision of micro-credit in certain parts of the Sudan is made via kinship and tribal fiber. Members of the same clan/tribe or area, provide flexible financial help to start businesses without any additional costs. Another

form is the collective help action (*Nafir*), where village inhabitants contribute to poor families in the form of collective work (Ibrahim, 1996a).

4.4 NGOs

Over 100 local and foreign NGOs, with direct co-ordination with the official authorities, are active in providing micro-credit, emergency loans, medical care and educational services to the poor in Sudan. Foreign NGOs play a very strategic role in mitigating the effects of war and resettlement of refugees and migrants by means of small, home-based business loans, counselling and training programmes.

Foreign NGOs provide loans for tiny projects such as tea making, sheep rearing, water services, petty trade, brick making, vegetable distribution, shoe making, women's handicrafts and house restaurants, in addition to providing training services, not only for migrants but also for the rural and urban poor. Conditions for providing financial support include the degree of poverty, minority group and unemployment. Other NGOs are based on saving/lending associations and a Grameen Bank-type of group guarantee, together with some use of the Islamic (*Murabaha*) finance system. PLAN SUDAN, Dutch University Gadaref Assistance Programme (DUGAP), and ACCORD are a few of the groups involved in this kind of practice (Ibrahim, 1996a).

DUGAP has established four credit unions with a total membership of 146, managed by women. The objective is to contribute to an increased financial security of women through their savings and the access to loans in the case of loss of business capital. In addition to small credit, DUGAP provides consumption loans, illness and pregnancy loans, training on financial matters, and technical support. In providing small credits, the *Murabaha* mode of finance is used, with a profit margin of 4 per cent. Repayment is made monthly, and the maximum duration of the loan is six months (Janssen, 1995). PLAN SUDAN has four families' associations in cities of eastern Sudan with a total membership of over 500. The main objective of these associations is to make funds available for small, home-based, mainly migrants' enterprises and income generating activities via self-directed financing associations. Up to August 1995 about LS 284 millions were distributed to 244 members of these societies, via Islamic *Murabaha* mode of finance with a profit margin of 4 per cent, a grace period of one to two months, and repayment intervals of a month and a quarter (Ibrahim, 1996a). The

objectives of ACCORD's programmes are to assist small enterprises through extended micro-credit for the poor and refugees in Eastern Sudan. ACCORD uses Islamic modes of finance such as *Murabaha*, *Musharaka*, *Mudaraba*, and *Quard Hassan* (benevolent). Between 1984 and 1992, more than 26,000 people benefited from the programme in businesses such as fisheries, retailing, welding and sheep rearing. The duration of the loans ranges between two and five months and the maximum profit margin of *Murabaha* is 4 per cent per month (Nourain, 1997).

The United Nations Development Program (UNDP), Area Development Scheme (UNDP/ADS) has targeted around 500,000 poor people. This is a community self-reliance, participatory development programme, to alleviate poverty and raise the standard of living of selected areas. The project provides capital through a self-administered rural revolving credit financing system (*Sanduaq*), which is applied through the Islamic *Murabaha* mode of finance to extend credit valued at US\$3.8 millions (Ibrahim, 1996b). Payment and collateral are secured through third party guarantees, social pressure and, sometimes, valuable assets. The actual amount of the loan, loan repayment schedules and the length of the grace period, all depend on the type of the project (grain milling, poultry, goat raising, soap making, crafts, and traditional small grain stores).

Some of the local social funds and local NGOs (the National Fund for Pensions, the National Fund for Social Insurance, *Takaful* Fund, *Zakat* Fund, Social Solidarity Fund, *Shariah* Implementation Support Fund, National Pension Fund, *Ashad*, *Elkifaya* Bank etc.) are established to serve specific religious, social and economic goals. Some are financed from the budget, while others are financed through charity, or by beneficiaries. Among other activities, they are also engaged in providing small-credit for living-provision kind of projects (such as leatherwork, cloth-making, tailoring, macaroon production and poultry production) especially for poor, widowed, divorced and deserted women.

5. Promotion of HBE's for Urban Poverty Alleviation in the Sudan: An Assessment

Home based Enterprises are now considered as one-priority areas in development policy in developing countries. Recently, the political economy of development has undergone radical change, and there are changing perceptions about the state, market and society. The role of the public sector has been minimised, and solutions to development problems have shifted to the private sector, in which tiny projects are receiving increased attention and new roles. In spite of the concerns about small home-based enterprises, they have not been high on the development agenda of many developing countries. It is clear that home-based enterprises have certain economic advantages of employment and poverty eradication.

Poverty alleviation through grass roots productive families in Sudan is currently receiving considerable attention from the target group, banks, the government and NGOs alike. The question arises as to what the Sudanese experience offer to promote HBE's in order to mitigate poverty?

The combined lending to combined deposits of the banking system is 40 per cent. The combined deposits are LS 400 billion Sudanese pounds in 1997 (equivalent to around US\$800,000 at that time), so the total lending is LS 160 billion. At maximum, the banking system allocated 6 per cent of this to craftsmen, professionals and small producers including productive families i.e. LS 9.6 billion Sudanese pounds. A per capita loan is calculated at LS 600 and total operations are 3,200 per year. That is to say, the beneficiary is 3,200 small enterprises per year out of a total population of 16 million classified under the poverty line (Ibrahim, 1996c).

Given the volume of poverty, a considerable effort is needed from the financing agencies to enhance funding to HBE's. But national policies and the internal policies of commercial banks have defeated this. Sudanese banking finance to HBE's cannot be considered effective for poverty mitigation, if we take into consideration the following characteristics of the Sudanese banking system:

- a) Demand deposits ratio is over 70 per cent of the total deposits. Demand deposits in Sudan are characterised by a high degree of instability.

- b) Regional inequality in the distribution of branches and the concentration of branches in commercial towns and urban areas. Khartoum and central states share almost 50 per cent of the total number of banks in the country (Ibrahim, 1992b).
- c) Sectoral concentration of investment and the bias toward the most organised sections with high profitability in the modern sector. The analysis of sectoral lending in 1993 shows that about 74 per cent of the combined total lending of commercial banks was directed towards modern agriculture, industry and exports. Small producers shared only 6 per cent of the total lending.
- d) Weak financial resources of the banking system, and relatively low lending capacity. The actual lending capacity in 1993 was only 46 per cent of the total lending. This figure compares badly to the 1980 figure of 88 per cent (Ibrahim, et. al. 1995). The ratio of financial resources to GDP did not exceed 12 per cent and total banking assets to GDP were only 17 per cent in 1992, while total deposits to money supply was 20 per cent at the very best.
- e) The adaptation of the Sudanese banking system to the requirements of the Basel Committee, require the banking system to look at internal problems rather than external, including their role in alleviating poverty.

The Sudanese experience was, and still is, capable of offering some lessons for HBE's financing. What lessons we can learn from this experience?

In his prominent work on Islamic partnership financing for small and micro-enterprises, Harper (1997, p. 1), argued that "there is a wide range of methodologies through which [*institutional*] finance can be delivered to the owners of [*small businesses and micro*] enterprises, and recovered in a way that is profitable for the financing institution" (Harper, 1997; *emphasis added*). Although these methodologies, he added, managed to avoid most of the outstanding problems of micro-enterprise finance, they are not free from other constraints. One, if the enterprise fails, loss of livelihood occurs and small businessmen are burdened with debt. Moreover, when inflation is high, loans are inevitably de-capitalised in real terms even if there are high recovery rates and coverage of operating costs. The conclusion is that profit and loss sharing formulae are known to avoid these two constraints. On another occasion, Harper asked a logical question that "even if the whole system of partnership financing, with

or without its religious implications, cannot be applied, are there some aspects of the system which can be used to overcome one or other of the problems of inflation and the ‘double burden’ of loss?” (Harper, 1997). There seems to be an advantage that Islamic partnerships can offer to small enterprise’s financing. Despite this partnership potential a formula has not yet received wide acceptance. If profit and loss sharing formulae are taken as one form of venture capital, rather than an ideological concept, it will possibly have a great deal of universal application, especially as a supplement to interest credit financing to HBE’s. Before showing that, let us first concentrate for the moment on the difference between the limited conventional and *Musharaka* partnership (Ibrahim, 1999).

- a) Limited conventional partnerships (defined as two or more persons who join together with a view to gaining profit) are not always specified for a limited period; *Musharaka* ends with the end of the business cycle. That is the dissolution of the Islamic partnership is on the expiration of the time fixed in the agreement for the length of the partnership. Commencement and liquidation of the *Musharaka* venture is known in advance and recorded in the contract.
- b) Although profit and loss of limited conventional partnerships can be distributed in two ways, *Musharaka* profit and loss allocation is only made in accordance with partners’ contribution of capital and services provided.
- c) Although withdrawals from a partnership fund are possible, since it is a long-term agreement, withdrawal from *Musharaka* is not common, since it is a short-term agreement.
- d) Unlike limited conventional partnerships, *Musharaka* contribution is fixed by the contract and no additional amount subsequently contributed to the business. This fixed original contribution makes *Musharaka* a limited partnership for a limited duration.
- e) In *Musharaka* the distribution of profit is made once at the time of liquidation, whereas in limited conventional partnerships the net income is distributed periodically among the partners while the project is still in operation.

f) Limited conventional partnerships are made between equal partners, whereas *Musharaka* can be between a small businessman and a big bank, hence it is a simplified form of venture capital.

In sum, the unfamiliar Islamic partnership is just a simplified, short-term, fixed contribution limited conventional partnership. If the Islamic system, guided by its principle of profit and loss sharing managed to modify the limited conventional partnership for financing small enterprises, why can't the interest-based banking system apply whatever sort of partnership, based on its conventional one to extend finance for small enterprises? When comparing the Western medieval economy and the Islamic system of banking, Taylor and Evans wrote that "the closeness of the two systems [*the Western medieval economy and the Islamic system*] is great and there is some evidence of common origins. Contemporary Western thought, however, has apparently removed itself far from its own tradition — hence the gap between Western and Islamic banking systems" (Taylor & Evens, 1987; *emphasis added*). Moreover, Harper concluded that "the Islamic prohibition of fixed interest lending, *which is also reflected in the Jewish and Christian traditions*, has led to the evolution of a number of financial innovations from which everyone can learn" (Harper, 1997; *emphasis added*).

There is a growing recognition of the importance of HBE's development as one major means to combat poverty in Sudan. Despite these efforts, and given the volume of poverty in Sudan, more efforts are still to be made. There are many constraints and obstacles facing the effectiveness of the government and NGOs' programmes and policies. Insufficient capital, especially foreign exchange is needed to purchase implements and equipment. Another major constraint is the scattered target group, which raises the cost of administering programmes to promote HBE's. Moreover, the government and NGOs efforts lack proper co-ordination not only at the top level but also at the grass root levels. Even though there are some joint co-operation efforts between the government and the NGOs, such efforts should be enhanced and extended to cover other parties. Limited market size poses another problem to the products offered by HBE's. Finally, any effort to alleviate poverty is costly when low education standards and the inadequate comprehension of dealing with money exists.

There are no elaborate and consistent long-term government policies and programmes to combat poverty via HBE's. Policies and programmes cover a small fraction of the target group and partially implemented. The creation of Councils and Committees did not improve

the decision-making, and they lacked funds. Although it is explicitly stated in the planning document, the targeted population was not reached. Moreover, policies and programmes to promote HBE's in Sudan reflect partially the supply side-approach of assistance (finance and training facilities), with a neglect of policies to improve the access to raw materials, extension of services and infrastructure. Moreover, supply side policies might be inappropriate in the case of widely dispersed and heterogeneous structure of HBE's. Demand-side policies, include the inequality of incomes and discrimination against HBE's, are also neglected. This is mainly because it is easier for planners and donors to establish funds for finance than to raise questions related to income distribution and to disturb the vested interest benefits from subsidies offered to large-scale production. Proper measures might be achieved via genuine policy reforms within a long-term plan that includes the economy at large.

6. Conclusion

Poverty alleviation through grass roots small-scale productive families projects is currently receiving considerable attention in Sudan, mainly from banks, the government and NGOs. Given the huge volume of poverty in Sudan, the intentions to use HBE's for poverty alleviation is not enough. Moreover, a considerable effort was made from the financing agencies to enhance funding to HBE's, but national policies and the internal policies of commercial banks themselves have beaten this move. Moreover, the Sudanese banking finance to HBE's were not able to mitigate poverty mainly for reasons related to the characteristics of the Sudanese banking system itself. Nevertheless, the principle of partnership used by Islamic banks can have some world-wide advantages to small enterprise's financing.

There are no elaborate and consistent long-term government policies and programmes to combat poverty via HBE's. Policies and programmes cover a small portion of the target group and partially implemented. At the programme and policy level, there are obstacles facing their effectiveness. In addition, government and NGOs efforts lack proper co-ordination both at the top level and at the grass root level. Moreover, policies and programmes to promote HBE's in Sudan reflect partially the supply side-approach of assistance (finance and training facilities), with a neglect of policies to improve the access to raw materials, extension of services and infrastructure.

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