Poorly targeted aid and lack of capital leaves small businesses struggling following natural disasters

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New research from the University of Warwick suggests the way foreign aid is distributed following a natural disaster in developing countries does little to help small firms recover.

Economists are calling for a reassessment of the way aid is distributed in low-income countries hit by disasters such as earthquakes and tsunamis. A lack of quick access to capital grants means many small businesses take a number of years to recover profit levels, and many struggle to recover at all.

In a new paper published in *The Economic Journal*, a team of economists including Professor Christopher Woodruff from the University of Warwick followed the progress of small businesses in Sri Lanka in the wake of a tsunami in December 2004.

The research team, which also included Suresh de Mel from the University of Peradeniya and David McKenzie from the World Bank, provided grants to randomly-selected businesses and compared them to a control group that did not receive the grants. They then monitored how the businesses developed for more than three years.

The team found that firms receiving the grants recovered profit levels almost two years before other damaged firms.

Professor Woodruff said: “The grants we provided served a purpose similar to that of the cheques many firms receive from insurance companies in the wake of natural disasters in more advanced countries. We found the businesses with the grants recovered more quickly and in some cases the capital appeared to have allowed an immediate recovery of the firms, compared to the control group.”

Professor Woodruff and his team found speedy access to capital proved significantly more effective in the retail sector.

He said: “Our research found that aid was both uncorrelated with the extent of business losses, and insufficient to the needs of firms. Aid to businesses only covered around 10% of reported losses. Loans did not seem to be an option, only 4% of businesses reported receiving a loan following the tsunami, and these covered less than 1% of losses.”

In developing countries, the researchers noted that small business owners rarely have insurance. They found less than 15% of the losses from the 2004 tsunami were covered by insurance.

Professor Woodruff added: “Our research demonstrates the need to expand avenues that provide access to credit for small businesses and to improve the targeting of aid. Addressing these two issues should speed up the recovery of these firms following a natural disaster.”

More information: The paper, ‘Enterprise Recovery following Natural Disasters’, is published in *The Economics Journal*.

Provided by University of Warwick

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