

**ADDIS ABABA UNIVERSITY**  
**SCHOOL OF GRADUATE STUDIES**

**DETERMINANTS OF ENTERPRISE GROWTH: THE  
CASE OF SMALL MANUFACTURING ENTERPRISES  
IN BAHIR DAR TOWN**

**BY: ENDESHAW MULATU H/WOLD**

**A Thesis submitted to the School of Graduate Studies, Addis Ababa  
University, in Partial Fulfillment of the Requirements for the Master of Arts in  
Regional and Local Development Studies (RLDS)**

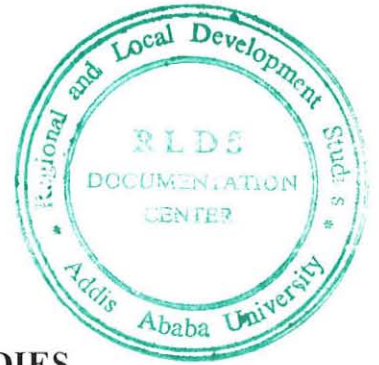
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**REGIONAL AND LOCAL DEVELOPMENT STUDIES  
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# TABLE OF CONTENTS

ACKNOWLEDGEMENTS	
TABLE OF CONTENTS	
LIST OF TABLES	I
LIST OF APPENDICES	I
ACRONYMS AND ABBREVIATIONS	II
ABSTRACT	III
<b>1. INTRODUCTION</b> .....	<b>1</b>
1.1 Background .....	1
1.2 Statement of the problem .....	2
1.3 Research questions .....	4
1.4 Objective of the study .....	4
1.5 Significance of the Study .....	5
1.6 Limitations of the study .....	6
1.7 The Study Area .....	7
1.8 Organization of the paper .....	9
<b>2. VIEWS ABOUT THE ROLE OF SMALL ENTERPRISES, AND SIGNIFICANCE AND SITUATION OF SMALL ENTERPRISES</b> .....	<b>10</b>
2.1 Opposing views on the role of small enterprises, and significance and situation of small enterprises .....	10
2.2 Problems and challenges of the small enterprise sector .....	15
2.3 Overview of the strategy of small enterprises development .....	21
<b>3. THEORETICAL AND CONCEPTUAL FRAMEWORK</b> .....	<b>26</b>
3.1 Theoretical framework .....	26
3.2 Concepts and definitions .....	29
<b>4. REVIEW OF RELATED LITERATURES</b> .....	<b>34</b>
4.1 The dynamics of small enterprises .....	34
4.1 Empirical literatures on the determinants of enterprise growth .....	37

<b>5. METHODOLOGY .....</b>	<b>42</b>
5.1 Study design.....	42
5.2 Data collection methods.....	42
5.3 Sampling design.....	43
5.4 Instruments.....	44
5.5 Data analysis .....	45
<b>6. DATA ANALYSIS AND INTERPRETATIONS .....</b>	<b>46</b>
6.1 Characteristics and profile of the small enterprises surveyed .....	46
6.2 Model specification, estimation and interpretation.....	53
6.2.1 Model specification.....	53
6.2.2 Variables or factors of enterprise growth and hypotheses .....	55
6.2.3 Estimation and interpretation of the regression results.....	58
<b>7. SUMMARY, CONCLUSIONS AND POLICY IMPLICATIONS .....</b>	<b>65</b>
7.1 Summary and conclusions .....	65
7.2 Policy implications .....	67
<b>BIBLIOGRAPHY .....</b>	<b>70</b>
APPENDIX 1	
APPENDIX 2	

## **LIST OF TABLES**

- Table 4.1: Key determinants of MSE survival and growth
- Table 5.1: Type and number of sampled enterprises
- Table 6.1: Type and number of enterprises covered by the study
- Table 6.2: Number of establishments and the observed rates of growth
- Table 6.3: Observed pattern of small enterprises growth by type of enterprise
- Table 6.4: Age of enterprise owners by age category
- Table 6.5: Level of education of small enterprise owners
- Table 6.6: Operators' reasons for choosing the current business
- Table 6.7: Age of small-enterprise establishments by age group
- Table 6.8: Size of small enterprises by employment-size category
- Table 6.9: List of major obstacles of small enterprise operators to expand their  
businesses as reported by owners
- Table 6.10: Definition of variables
- Table 6.11: Coefficient estimates

## **LIST OF APPENDICES**

- Appendix 1: Partial Regression Plots
- Appendix 1: Interview Questions

## ACRONYMS AND ABBREVIATIONS

ADLI	Agricultural Development-Led Industrialization
ANRS	Amhara National Regional State
BoFED	Bureau of Finance and Economic Development
CSA	Central Statistical Authority
GDP	Gross Domestic Product
ILO	International Labour Organization
LDCs	Less Developed Countries
MSE	Micro and Small Enterprises
MSESP	Micro and Small Enterprises Strategy Paper
NGOs	Non Governmental Organizations
ReMSEDA	Regional Micro and Small Enterprises Development Agency
RGDP	Regional Gross Domestic Product
SMEs	Small and Medium Enterprises
SSEs	Small Scale Enterprises
UNCTAD	United Nations Conference on Trade and Development

## ABSTRACT

The dynamic role of small enterprises in developing countries as engines through which the growth objectives of these countries can be achieved has long been recognized. In the face of a rapidly growing labour force where public sector hiring slowed and the growth of the large modern private sector has relatively stagnated, the role of the small as well as micro enterprises in employment creation is indispensable. Despite the fact that Small Enterprises have been recognized as a major contemporary source of employment and income in a growing number of developing countries, yet relatively little is known about the characteristics and patterns of change in these enterprises.

Most past research in this area, however, have been static in their orientation, providing a picture of how things look "today" or as of the time of the study. This argument holds true to our case that studies on dynamic aspects of small enterprises are almost non-existent.

The aim of the study is to examine and identify factors affecting growth of employment in small enterprises. This study used cross-sectional data collected through a field survey in Bahir Dar town of the Amhara Region. The method employed is a multiple linear regression analysis that makes an econometric estimation on 76 small manufacturing enterprises to determine the explanatory factors of their employment growth. The explanatory variables considered in the study represent firm and owner-manager characteristics and business practices. The results at most do not reveal any surprises compared to other similar previous empirical researches conducted elsewhere. Factors found to influence significantly small manufacturing enterprise growth in Bahir Dar are market size, young age of the entrepreneur, age of the enterprise and reliance on external sources of finance i.e. Bank loan. However, sex of the owner, size of the firm, post-high school level of education and experience of the entrepreneur have no significant effects on the growth performances of small enterprises as far as the study area is concerned.

The findings give rise to several policy implications that are crucial for the improvement of the sector's performance. These include policy makers have a role in dispelling the myth, particularly among finance or credit providers (mainly banks), that small enterprises in general and women owners in particular are high-risk borrowers of capital. The findings call for public policies such as the youth employment strategy, which among others encourages the young entrepreneurship. Blanket policy approaches to small enterprise growth may not be effective. Policies targeted at small enterprises that are willing to take risk and able to grow are preferable. The findings also call for introduction of guarantee schemes to support small-sized enterprises that can not meet bank and financial collateral requirements.

# CHAPTER ONE

## INTRODUCTION

### 1.1 Background

The important role of micro and small-scale enterprises as a source of income and employment to poor households is a widely acknowledged fact in many developing countries. Detailed surveys in a number of these countries suggest that as many as a quarter of all people of working age are engaged in micro and small enterprise activities (Mead and Liedholm, 1998). In addition, micro and small enterprises are the basis for large industrial development. It is these small industries that did develop to medium and large size factories in many of the today's industrialized nations. Of particular interest is the process of expansion of these enterprises from very small to medium size, as it is when they become medium sized, that growth-oriented small and medium enterprises make their most tangible contribution to economic growth and job creation (UNCTAD, 2000).

To day we find that the issues of Small-Scale Enterprises (SSEs) have stimulated so much interest among donor agencies, governments, non-governmental organizations, policy makers, development analysts, etc. to the extent that all are very much concerned with the promotion and development of SSEs (Andu-Alem, 1997). In Ethiopia, the SSE sector has been neglected in the past. However, especially following the country's shift to a market economy, the government as well as NGOs and donors have shown interest in the area. The shift to market - led economic system would mean the strengthening of the private sector, which would then foster the development of Small Enterprises in Ethiopia, as they constitute the majority of the sector.

A national survey on small scale manufacturing industries conducted by CSA in 2001/2002 and covering 48 Major towns reported that more than 750,000 people are engaged in informal sector and small manufacturing businesses. The small scale enterprises together with the micro enterprises account for 3.4% of GDP, 33% of the overall contribution of the industrial sector and 52% of the manufacturing sector to GDP (Ministry of Trade and Industry, 1997). According to the records of the Bahir Dar Special Zone Micro and Small Enterprises

Development Branch Office, currently there are more than 134 small enterprises, which are engaged in manufacturing activities such as wood, metal, food and non-metal products processing

Employment in small-scale enterprises expands as a result of new enterprises starting up in business, and through an expansion of existing enterprises. These positive forces are off set by the contraction or closure of other enterprises. These components of change are subject to different forces and determinants. According to Mead and Liedholm (1998) many micro and small enterprises promotion projects seek to influence one or another of these different components of change. Some projects aim to promote new business starts by addressing the constraints that make it difficult for people to establish new enterprises. Other projects provide assistance aimed at countering the forces that cause existing enterprises to fail, while still others seek to help existing business to improve their performance and to expand. This, however, would be more effective when such determining factors, which have a varying degree of influence depending on the prevailing socio-economic conditions relative to a given locality, are identified in concrete terms.

In this regard, the Ethiopian Government has formulated a National MSEs Development and Promotion Strategy with a major objective of creating long-term employment and providing the basis for medium and large scale enterprises there by facilitating economic growth. However, as reported in this document and in other related literatures this objective would not be easily realized because of many problems and constraints associated with legal and regulatory environments, access to market and finance, business information and premises, etc. Moreover, the design of those strategies needs to be supported by detailed studies. Ajibefun and Daramola (2003) emphasized this issue by saying "many of the studies that exist in the developing countries are macro in nature and generally rely on cross-country or multi-country data rather than firm level survey data. Therefore, policy formulation has been hampered by a lack of studies at firm level."

## **1.2 Statement of the Problem**

The dynamic role of small enterprises in developing countries as engines through which the growth objectives of these countries can be achieved has long been recognized. Despite the

fact that small enterprises together with micro enterprises have been recognized as a major contemporary source of employment and income in a growing number of developing countries, yet relatively little is known about the characteristics and patterns of change in these enterprises.

More over, small enterprises are springboards for medium and large-scale industries. The question, therefore, is how to promote this sector. However according to UNCTAD (2000), in many developing countries there is evidence of shortage of middle-sized growth oriented enterprises that could make an important contribution to development. This absence of middle-sized enterprises is attributed to hidden and largely inadvertent biases in the sector's development policy, or in its implementation, of these countries that militate against the gradual and organic growth of their small enterprises. The lack of coherent small and medium scale enterprises development strategies, which take in to account the three dimension of enterprise evolution i.e. start-up, survival and growth, and the different needs of enterprises in their various stages of evolution, is another important contributory factor.

It is also argued that much less is known about the business attributes and environments that promote enterprise growth. This is an important concern for policy makers, who in country after country are trying to implement policies that will foster enterprise start-up and growth.

According to some authors in the area, while the broad magnitudes of micro and small-scale enterprise structure are reasonably clear, there has been much less understanding of the sources of change and the process through which employment in this sector grows. Nevertheless, according to them, it is of great importance to understand the factors, characteristics and patterns of the changes that are taking place in the domain of the small enterprises, combining this with a vision of how things might develop better in the future in order to specify measures that might be done to help bring about the desired out come. An important part of this sorting out involves a better understanding of the determining factors of enterprise growth and the growth process-taking place among small enterprises.

Small enterprises differ in their growth performances. Some enterprises close, some enterprises experience high growth, the rest change their size moderately. But the question is

which properties of the small enterprise determine its growth and what promotes rapid growth. This study attempts to examine such factors or properties and determine their level of influences on the growth of the small enterprises in Bahir Dar. More over most past research in this area have been static in their orientation, providing a picture of how things look "today" or as of the time of the study. This argument also holds true to our case that studies on dynamic aspects of small enterprises are almost non-existent. This research work intends to contribute in filling such gaps by focusing on one aspect of firm dynamics i.e. firm growth.

### **1.3 Research Questions**

The central question that the study intends to answer is “what business environment and business characteristics do influence enterprise growth?”

The specific questions to be answered by this study are the following.

- Do owner-manager characteristics affect enterprise growth?
- Which characteristics of small enterprises play a decisive role in determining employment growth in small enterprises?
- Do the findings are consistent with the results of most similar empirical works in the literature?
- What are the problems faced by entrepreneurs or small enterprises that hinder their growth?
- Hence, what type of support should Small enterprises get? and how can they be supported?

### **1.4 Objectives of the Study**

#### **1.4.1 General Objectives**

The general objective of the study is to examine and identify major factors affecting growth of employment in small enterprises in Bahir Dar Town with particular emphasis on the manufacturing activities. This research work is believed to provide new insights, which will have implications for policy and intervention design mainly concerning to enterprise growth

and the determinants of the various components of change as far as the study area is concerned.

#### **1.4.2 Specific Objectives**

The specific objectives of the study are:

- To investigate what business environment and characteristics in the study area drive expansion of small enterprises
- To identify particular factors that contribute most in fostering the growth of small enterprises mainly as viewed in terms of employment
- To propose solutions and measures that would further the growth of small scale enterprises

#### **1.5 Significance of the Study**

Currently, the contributions of micro and small enterprise sector in terms of employment creation and poverty alleviation has been well recognized in many developing countries including Ethiopia.

Since small firms dominate the industrial scene in these most low-income countries, a deeper understanding of how these firms evolve may make it possible to pursue an industrialization path that builds on these enterprises.

Studies of small firms dynamics are important because they provide insights in to the desirable patterns of growth in out put and employment. Such studies can also uncover ways through which policies and programs can facilitate, or at least not impede, this evolutionary process. As Liedholm and Mead (1999) indicated,

It is important to understand the characteristics and patterns of the changes that are taking place in the domain of micro and small enterprises, combining this with a vision of how things that might be done to help bring about that preferred outcome. An important part of this sorting out involves a better understanding of the growth process among micro and small enterprises.

Job creation by small business is an important focal point for public policy and has been the subject of many studies in the area. In order to address this issue, it is essential to better understand the factors involved in the growth of small enterprises.

The significance of this study, therefore, lies on indicating the determinants of small enterprise growth and the degree of their influence in order to inform policy makers and government officials to take note of and act accordingly in their policy and strategy formulation.

### **1.6 Limitations of the study**

Efforts were made to get as representative and reliable data as possible. In most cases, research works that are undertaken on such sectors as micro and small enterprises suffer greatly from data shortages. The problem, in fact, is not only a matter of shortage but also a question of reliability of the data. This problem is mainly attributed to the fact that most micro and small enterprises do not pay attention to documentation of records on various business aspects. Particularly, it is hardly possible to get an organized record on financial matters like sales, revenues and expenditures. Such data even if they exist, the operators mostly would not be willing to provide them because of many reasons, fear of high rate of tax levy being the major one.

Firm growth models usually employ the volume of firm's sales and employment as measures of growth when data availability permits. However, in the face of the above-mentioned difficulties the use of such data becomes not easy. Despite this, in this study, the researcher has paid due attention to ensure the reliability of the data collected and to manage the impact of associated problems. Two of such measures were assigning of enumerators to the localities (or Kebeles) to which they are most familiar and have enough knowledge, and to use cross checking mechanisms.

However, it may be necessary to mention some points, which in the Author's opinion can be considered as limitations of the study. These include:

- Some of the respondents i.e. small enterprise owners, hesitated to give genuine information on some questions. This was because the survey was conducted in a time when most of the enterprise owners were complaining about the level of tax and when their complaints reached its climax. This could have influenced them to hide some important information, which in turn might have some effects on the precision level of the data.
- Small numbers of small enterprise owners were totally not willing to be interviewed. For one or other reason they declined to give information. This has reduced the number of enterprises which otherwise would have been included in the group of enterprises examined.

## **1.7 The Study Area**

Bahir Dar is located in the North Western part of the country at 565 kms road distance from Addis Ababa along the highway to Gonadar.

According to the population projection results of the Amhara Region Bureau of Finance and Economic Development, the total population size of the region is estimated to be 18.6 million in 2005, of which 89 percent live in rural areas while the rest represents the proportion of the urban dwellers. The sex composition of the population of the region is almost equal with little dominance of males over females. Likewise, the projected population of Bahir Dar for the year 2005 is 168,048. According to population estimate of the same source, the population size of the town is increasing faster than any other town in the region because of various reasons.

The region is located between  $9^{\circ}$  and  $30^{\circ} 45'$  North latitude and  $36^{\circ}$  and  $15'$  and  $40^{\circ} 30'$  East longitude and it is situated in the northwestern part of Ethiopia. According to BoFED, the region covers a total area of  $161,828.4 \text{ Km}^2$ . The region is divided in to 10 administrative zones and one special zone, which in turn are divided in to 106 woredas.

Agriculture is the mainstay of the region's economy and it accounts for 63.8 percent of the regional GDP followed by industry (22.1 percent) and service sector (14.1 percent) (BoFED, 2004a). The output of the industry sector has been increasing in the last 8 years and on average, industry grows at 5.8 percent per annum. Although the industrial sector as a whole is witnessing progress in terms of its share and growth overtime, the share of the manufacturing sub sector in the RGDP is still at a dismal level of 2.1 percent because of its low rate of growth relative to other sub sectors.

There has been a settlement at around Bahir Dar for many decades but the economic growth of the town began in earnest in the 1950s, when the town was legally recognized as a municipality and its status was raised to an "Awraja" capital.

Currently, the town is the capital of the ANRS. Bahir Dar, being the capital of the region and due to its historical sites around, and attractive geographical settings (situated at the shore of the Lake Tana), it is increasingly becoming a center of attraction for domestic settlers and local and foreign tourists. At the same time it serves as a business nucleus to the surrounding areas.

Bahir Dar is one of the few fast growing towns in the country. Moreover, it is one of the major towns in the country where many governmental and non-governmental offices and Bureaux are found. As a result, it has strong economic, administrative and social interactions with the rest of the urban centers as well as rural areas with in the region.

Consequently, there is a growing demand for processed goods and other economic services as input for construction works, office and household facilities and for daily consumption by the people. Most of these goods are provided by small-scale establishments, which are increasing in number from time to time as a response to the ever-growing demand. According to the records of the Bahir Dar Special Zone Micro and Small Enterprises Development Branch Office, currently there are more than 134 small-scale enterprises, which are engaged in manufacturing activities such as wood, metal, food and non-metal products processing.

## 1.8 Organization of the Paper

The paper examines the growth experiences in Amhara Region i.e. Bahir Dar, from the perspective of small manufacturing enterprises, concentrating primarily on the owner characteristics and firm-level sources of growth. It attempts to identify some of those factors influencing the growth process of small enterprises in Bahir Dar either positively or negatively.

The paper is organized in seven parts. The first part focuses on the background, problem statement and objectives of the study. The second part discusses the significance and common problems of the small enterprise sector with reference to the national and regional context (including that of the study area). This part also presents an overview of national and regional strategy of MSEs development.

The third develops theoretical framework for both systematically organizing our thoughts about the major factors influencing the growth process and estimating the quantitative contribution of each while the fourth part reviews the theoretical and empirical literatures that examines the major factors influencing the growth process of small enterprises. The fifth part is about the methodology of the study.

Part six summarizes the econometric results, based on cross-sectional data. The final part concludes the essence of the whole discussions and draws some conclusions for policy considerations.

## CHAPTER TWO

### OVERVIEW OF THE SMALL SCALE ENTERPRISE SECTOR

#### 2.1 Opposing views on the Role of Small Enterprises, Significance and Situation of Small Enterprises

##### 2.1.1 Opposing Views about the Role of Small Enterprises

The role of Micro and Small Enterprises to the creation of jobs and to the alleviation of poverty has increasingly been appreciated by many developing countries. MSEs in these countries are the predominant features of their economy. Despite their large numbers, MSEs are often seen as low-income activities that do not contribute to the economy. For example as Daniels (1995) puts it, some writers report that, "as agents of economic development, very small enterprises are, to put it bluntly, of little interest". Others have emphasized that MSEs have an important role to play in the development process (Liedholm and Mead (1999), Mead (1994), White (1999) and Daniels (1999)). Detailed surveys in a number of countries suggest that as many as a quarter of all people of working age are engaged in MSEs activities.

While the broad magnitudes of MSEs structure are reasonably clear, there has been much less understanding of the process through which employment in MSEs grow. This lack of knowledge has led to a lengthy and generally fruitless debate regarding the extent to which expansion in employment in MSEs should be seen as a component of a successful development process or as a sign of the malfunctioning of the rest of the economy (Daniels et al, 1995).

Many critics of MSE support argue that even though the sector is a significant employer of the poor, micro and small enterprises and the jobs they offer are merely parts of a survival economy but are not parts of a dynamic process of economic growth. Hence, resources directed to the support of these enterprises are considered as wasted from a long-term development perspective. Mead (1994) classified these opposing views on the basis of the deriving forces leading to growth in employment. According to him for many individuals

engagement in small enterprises is a kind of survival activity to sustain them until something better comes along, such employment growth might be thought of as "supply-driven". Expansion of employment of this type could be seen as reflection of the failure of the economy to develop in ways that provide rising levels of welfare for the majority of the people. The opposite polar case reflects a situation where employment in small enterprises grows as entrepreneurs identify and respond to market opportunities. In this case, the driving force is an increase in demand for labour as entrepreneurs expand their work force in response to these market opportunities. This pattern of growth is characterized as a 'demand -driven' expansion. Expansion of employment of this type clearly can be thought of as a component of successful development.

However, Daniels et al (1995) argue that in the absence of reliable information, it is difficult to determine the extent to which each side of the debate is justified, or to determine which MSEs are growth oriented and which are best considered as part of the survival economy.

Despite these opposing arguments about the importance and role of small-scale enterprises, there are sufficient reasons for promoting the development of small-scale enterprises in developing countries.

Mead (1994) emphasized the different roles that small enterprises can play at different stages of development. As development takes place, household and artisan activities decline in importance, being replaced first by small workshops and factories, later by large factories. White (1999) strongly underscores the benefits of the small enterprise sector from the practical context of Thailand's economy by saying, "it is easy to dismiss or ignore the contribution of the MSE sub-sector. However, to do this in Thailand would be to over look a large section of commercial activity". According to Assefa (1997) and Dondo (1998), small-scale enterprises, being labour intensive and capital saving, have great potential to absorb the growing number of unemployed and under-employed population. Small-scale enterprises also have potential for mobilizing local resources and they are also desirable because unlike medium and large industries, they can be located in rural areas or small towns and villages there by assisting in curtailing undesirable rural -urban migration. Hence, the important role of micro and small-scale enterprises in economies like that of Ethiopia cannot be underestimated.

### 2.1.2 Significance of Small Enterprises

The Ethiopian government has presently recognized and paid due attention to the promotion and development of micro and small enterprises for they are important vehicles to address the challenges of unemployment and economic growth in the country. A typical example of this recognition has been the design of a Micro and Small Enterprises Development Strategy.

There is, in fact, consensus on several points concerning the significance and role of small enterprises in many literatures written on the subject. Small-scale enterprises are justified for the following reasons.

- i) **They create substantial job opportunity.** Employment generation is one of the major objectives of the national development policy of a country. All small enterprises, broadly defined, display a remarkable capacity to absorb labour thus contributing to easing the pressure of unemployment. Thus, technologies that require more labour per unit of output should be favored than those, which need less labour. Being labour-intensive and capital saving, small enterprises could help in solving many of the problems Ethiopia is faced with. Small enterprises have great potential to absorb the growing number of unemployed and under employed population. They generally employ workers with limited formal training.
- ii) **They offer potential for resource mobilization.** Economic growth in Ethiopia is constrained, among other things, by shortage of capital. The country is in early stage of industrialization. Thus, much of the required investment for the industrial sector should come from domestic savings. There are, however, reserves of idle savings that could be drawn in to productive use if the owners had the choice to set up business by their will. Thus, one of the objectives of developing small-scale industries is to mobilize the unutilized and underutilized saving so as to make them productive.
- iii) **The decentralization argument.** Small-scale enterprises are desirable because they can be located in rural areas or small towns or villages. Often large and medium industries are concentrated in few urban centers, which entails undesirable

rural to urban migration. Such unwanted and unplanned flow of people from rural areas to urban areas could create social problems to the urban centers on the one hand and with draw the productive labour force from the rural areas on the other hand. In general, they are loose foot and also convenient for geographical spread of industrialization. The decentralization process may help balance the disparity in economic growth between rural and urban areas. Hence, decentralized distribution of industries and the promotion of industrial growth in small towns and rural areas with potential resource base is very essential for the country.

- iv) **They are sources of income for many people.** Because small-scale enterprises offer a remarkable capacity to absorb labour, there by relieving the problem of unemployment, they provide income-earning opportunities for a large portion of the population. They generally tend to contribute to a more equitable distribution of income.
- v) **They add to the variety of consumer goods.** They produce relatively cheaper goods and services locally using labour-intensive methods satisfying the needs of particularly the poor people-hence contributing to the variety of consumer goods. Besides, they develop a pool of skilled and semi-skilled workers that will be a basis for future industrial expansion.
- vi) **They facilitate forward and backward linkages.** They promote subcontracting arrangements and acts as ancillaries to large-scale enterprises. They facilitate effective technology transfer as a result. In addition, they provide significant inter-sectoral linkages, integrating economic sectors through backward and forward linkages.
- vii) **They serve as agents of rural transformation.** In the rural areas, they constitute centers of innovation as well as of economic and social changes thus helping transform rural areas in to market economy through gradual magnetization. Hence, they contribute to the economy, especially rural trade and production in terms of out puts & skills (Andualem, 1997).

- viii) **Seedbeds for entrepreneurial development.** They are seedbeds for entrepreneurial development and offer excellent opportunities for entrepreneurial and managerial talents to develop and mature, the critical shortage of which is often stressed as a major handicap to economic development of most developing countries.
  
- ix) **They are flexible and adapt to market changes quickly.** They also have great reliance on indigenous resources - raw materials. They generally show less need for developed and costly infrastructure.

In general, the small enterprise sector is seen as an important force to generate employment and more equitable income distribution, to activate competition, exploit niche market, enhance productivity and technical change and as a result stimulate local as well as national economic development.

### **2.1.3 Situation of Small Enterprise in Amhara Region**

As Harper (1997) put it, because the activities of small businesses are largely undocumented, it is very difficult for planners and researchers to know whether they are or are not acting in accordance with a given national policy or strategy. Detailed data on the situation of such activities are rare and for one or other reason it is hardly possible to get satisfactory information about small enterprises even from a responsible institution. Currently, what is available in this regard is a survey result of the Central Statistical Authority, which is based on sample data. The sample survey conducted in 48 major towns of the country by CSA, in May 1997, showed that there were 584, 913 and 2,731 informal sector activity operators and small scale manufacturing industries respectively, that absorb 739, 898 labour force. The same sample survey which was conducted in the major towns of ANRS i.e., Gondar, Dessie, Bahir Dar and other urban areas of the region by CSA in the same year indicated that 150,090 informal sector activity operators exist in Amhara region absorbing 199,515 labor force, which is 15.2% of the total labour force engaged in the informal sector in the country. Of the total operators 53.41% are engaged in manufacturing activities and the rest in trade, hotel, restaurant, personal services, fishing, agriculture and mining.

On the other hand, according to the 2002 report on small scale manufacturing industry survey by CSA, there were 260 small enterprises operating in Bahir Dar town, of which grain mills constitutes the majority of the establishments in terms of number. The CSA report also reveal that the number of people employed in those enterprises is nearly 1000 and the gross value of production of these enterprises is estimated to be Birr 8.9 million in 2002. Similarly, according to the Bahir Dar Special Zone micro and small-scale enterprise development branch office, the number of small enterprises (excluding grain mills) exceeds 134.

The small enterprises as well as the micro enterprises sector in the region are characterized by highly diversified activities, which can create job opportunity for a substantial segment of the population.

According to the concept paper for the formulation of private sector capacity building programme in the ANRS, the private sector in general and the micro and small scale enterprises sector in particular has not been performing well because of many problems and constraints facing them. Taking the advantage of encouraging policy measures, however, the sector is now growing progressively towards the right path.

## **2.2 Problems and Challenges of the Small Enterprise Sector**

Many of the small enterprises in the country are commonly constrained by several factors but some attempts were made to alleviate them by the government. Even though, the degree of severity of each problem varies from enterprise to enterprise, some of the major problems that have inhibited the development of the sector include the following.

### **a) Lack of access to finance**

The most serious problem facing the small-scale and micro enterprises sector have been raising of investment capital and lack of credit access. Small-businesses have been always constrained by lack of investment capital for buying machinery and equipment and for the day to day running of the business. The financial institutions loan policies have not been conducive and attractive (Assefa, 1997).

High collateral requirements, high interest rates, short repayment period are among the major problems that make easy access to credit difficult. Banks are unfamiliar with SSEs because they consider them as involving high-risk factor, not dependable, and involve excessive administrative costs. Hence, they regard them as not eligible for provisions of bank services. Therefore, the sector is neglected by the financial institutions and this is one crucial area where attention is deemed critical.

#### **b) Shortage of raw materials**

Shortage of raw materials is the most important and pressing problem facing small manufacturing enterprises. The source and proximity to raw materials determine MSEs' viability. Hence, MSEs should be located in the areas where their resources originate or where sufficient supply of raw materials is secured. Shortages of raw materials are frequent problem to SSEs. According to Harper (1987), this problem may arise from a shortage of working capital, which effectively ties the enterprise to one high priced, unreliable or low-quality supplier.

Assefa (1997) noted that since most of the small scale enterprises are located in the urban areas, and not in the areas where there is adequate supply of raw materials; shortage of raw materials is acute. As a result, most of the small scale-enterprises have been operating below capacity and some have been closed.

A study on constraints of micro and small scale manufacturing enterprises sponsored by the Amhara Region ReMSEDA and which was conducted in 2002 revealed that 30 percent of MSEs operators are faced with problem of shortage of raw materials.

#### **c) Lack of premises and land**

It is common to see most small enterprises taking advantages of their residence areas as business premises. Small enterprises by their very nature are started in and around residence areas, which through time and growth require additional working space. Lack of premises is a major problem for SSEs and for the informal ones; they can rarely acquire suitable locations where they can get easy access to markets. The

transaction cost of securing premises is also a constraint for SSEs. The land lease promulgation which has been effective in most urban areas has an impeding impact on micro and small entrepreneurs who wish to start up business (Andu-Alem, 1997).

In the CSA's 2002 survey result, it is reported that problem associated with working premises is mentioned by entrepreneurs as one major constraint hindering the smooth performance of small-scale enterprises in the region.

**d) Infrastructure problem**

The major reason why SSEs are concentrated in urban areas is because of the relative availability of infrastructure compared to rural areas. Water, electricity and market access or roads are vital inputs to small-scale industries. However, shortage of such infrastructure has been one of the major constraints to the development of the sector in many urban areas of the country.

**e) Market problem**

Many literatures and authors stress that lack of market information as well as markets have been the major impediments to the development of small enterprises in Ethiopia. Because of the absence of market research and information many of the small enterprises are often concentrated in the production of similar commodities which puts them under fierce competition among themselves.

These authors also argue that marketing their products effectively is one of the main bottlenecks that small entrepreneurs face all over the country. Marketing problem is a serious constraint that hinders small enterprises' growth and their product diversification. Liedholm and Mead (1999) emphasized that the inability to develop and introduce new product types can be seen as a problem of markets for the products SSEs do make.

According to a study conducted on small manufacturing enterprises in Amhara Region, of 690 industries from which information was collected 22 percent reported

that they are facing serious market problems (Amhara Region Trade, Industry and Urban development Bureau, 2004).

**f) Lack of entrepreneurial and managerial skills**

Various studies conducted on the sector revealed that there is a general lack of knowledge in entrepreneurial and managerial capacity. However, according to these studies there is a doubt whether these entrepreneurs themselves are aware of the need.

Lack of adequate skills is one of the seven major problems confronted by entrepreneurs at the starting of operation as revealed by the result of the national survey on small scale manufacturing industries undertaken by CSA in 2002.

**g) Lack of information and information system**

For the success of micro and small enterprises the presence of strong institution that can provide reliable and timely information through efficient information system is vital. MSEs essentially require information related to market raw materials, utilities, technology, business opportunities and information about government policies and regulation.

In Ethiopia, particularly at regional level like in the ANRS, access to such data and information is often limited, as it is cumbersome and expensive to collect, process and disseminate that information. Hence, Ethiopian entrepreneurs, in most cases, have not access to any reliable source of information on the line of activities with potential to growth (Amhara Region Trade, Industry and Urban Development Bureau, 2004).

**h) Technological problem**

Technological development is very low in the country. As a result, most of the small-scale enterprises use obsolete technologies of production. The technology used by small-scale enterprises is out dated, unhygienic and inflexible (Assefa, 1997).

Technology in most literatures refers to a combination of machinery, labour as well as the entire system of knowledge, skills, techniques, management, organization, etc.

The technological problem also has another dimension. The use of appropriate technology should be seen as a core issue in the context of developing economics like that of ours. These technologies need to be consistent with local resources and conditions to make effective utilization of the relatively abundant resources. However, the issue of adopting appropriate technology has been a serious problem of small scale manufacturing enterprises in our country. 29 percent of the small scale manufacturing enterprises among the entrepreneurs approached by the CSA survey (2002) on small scale manufacturing industries reported frequent machinery failure to be their major reason for not being fully operational.

**i) Inadequate consultancy and advisory services**

The concept paper for the formulation of private sector capacity building programmes developed for the ANRS in 2004 identified inadequate consultancy and advisory services to be among the major problems that hindered growth of the SSEs.

In competitive and constantly changing business environment, the production and supply of quality goods and services at a minimum cost depends highly on the availability and provision of business upgrading services and technical know how. Consultancy services as a tool to enable entrepreneurs to diagnose their business and to undertake informed decisions is one of the key elements from a range of services.

The inability to get insight of their own business problems i.e. to undertake business opportunity identification and feasibility study, to prepare business plan, to identify sources and procedures for finance, to build business linkage, to implement appropriate cash flow management and records, and other accounting activities necessitate consultancy and advisory services backstopping for SSEs. The existing situation of consultancy service in ANRS is fairly infant and weak. Though the institutional arrangement is in place, the achievement in this regard so far is not as such attractive.

## **j) Unfavourable legal and regulatory environment**

The private sector in Ethiopia was suppressed under the command economy of the past. Currently, nearly all business activities are open to domestic private enterprise except for a few areas kept as government monopoly. Presently, the policy related to private investment is very conducive for the development of the private sector. However there are still some regulatory problems affecting the sector. No strong private sector can exist in the absence of an adequate legal framework to resolve disputes, facilitate efficient transaction and to protect property rights. Various studies and discussions indicate that the following are some of the regulatory issues affecting the private sector in general and the small-enterprises development in particular (Amhara Trade, Industry and urban Development Bureau, 2004).

- ◆ Governance responsibilities of the government and the private sector are not clearly put. There are governance weaknesses on the part of both government and the private sector.
- ◆ Market regulation is not mostly ensuring fair competition and market efficiency.
- ◆ Dialogue between the private sector and government has not been strengthened which could have minimized the regulatory and governance weaknesses.
- ◆ Bureaucratic delays and administrative inefficiencies need to be avoided.

The CSA's survey result on small scale manufacturing industries (2002) revealed that, of the total establishments approached, some owners reported that government regulations were obstacles for starting their business operations. Among those who replied that government rules and regulations were obstacle for their business operation, 41.5 percent and 32 percent reported that getting license and regulation on obtaining working premises, respectively, were their major problems to start operation in this sector, and 13.4 percent reported that tax regulations were their major problems.

Finally it is important to note that in view of such diverse and complex problems facing the sector, government is required to take measures that facilitate smooth and healthy functioning of small enterprises as clearly indicated by W. R. Simpson who is Director of an ILO project in Thailand (In ILO and UNDP, 1999). He emphasized the importance by saying:

Perception of the role played by governments have changed; they are no longer expected to be the principal providers of jobs – jobs are created by successful, well-managed private sector enterprises. However, governments do have a vital role to play in ensuring that the policy environment is ‘enterprise friendly’. The path in to enterprise should be smooth, and entrepreneurs should be able to receive relevant advice and support (both financial and non-financial) in a highly effective manner from both government and private sector agencies. The needs of the micro and small enterprise sector should be clearly identified, and linked with a better understanding of the scale and scope of the enterprise sector and its role in national development.

### **2.3 Overview of the Strategy of Small Enterprises Development**

By virtue of their size, location and their capacity to generate greater employment, MSEs have proved their powerful propellant effect for rapid economic growth. Cognizant of this fact, the Ethiopian governments have given particular attention to the development of the sector. To this effect, the government has formulated a National MSEs Development and Promotion Strategy, which enlightens a systematic approach to alleviate the problems and promote the growth of MSEs.

The strategy paper is first prepared at national level and then after each region adapted its own strategy paper on the basis of the national one, after synchronizing with the prevailing conditions of the region. The national MSEs strategy paper is issued in 1997 while that of the Amhara region is issued in 2001. The objectives, principles and elements of MSE support framework that constitute the strategy paper are not as such different as presented in the national and the Amhara region strategy papers.

### **2.3.1 Objectives of Micro and Small Enterprise Development Strategy**

The overall objective of the national as well as the regional strategy papers is to create an enabling environment for MSEs while the specific objectives among others are to facilitate economic growth, to create long-term jobs, to provide the basis for medium and large-scale enterprises and to promote export.

### **2.3.2 Elements of the MSE Support Framework of the Micro and Small Enterprise Development Strategy**

The strategy paper emphasizes that small business is to be designated a priority sector for the government, in terms of policy formulation, direct support from its own resources and in the mobilization of external resources. The strategy addresses the major constraints, which have made it difficult for small business growth on their own, and hence it focuses on support areas. The support areas that the strategy paper incorporates are:

- ♦ Creating an enabling legal framework. This implies that the government is committed to pass a number of enabling proclamations that are meant to formally recognize the importance given to the micro and small enterprises sector and to facilitate policy implantation in different areas. In this regard the major focus areas include a law on institutional arrangement for MSEs, inter linkages promotion law, cooperatives' promotion law, chamber of industry and trade proclamation and a micro and small enterprises finance proclamation.
  
- ♦ Streamlining regulatory conditions. This is based on the viewpoint that inappropriate or unduly restrictive legislative and regulatory conditions are often regarded as critical constraints on micro and small enterprises' access to market and as obstacles to their growth. Streamlining regulatory conditions in the strategy paper's context understood as establishing user-friendly environment for the simplification and standardization of documents such as business registration and licensing, financial and loan applications, export documentation and other commercial export documents, simplified tax declaration forms for small business, etc.

- ♦ Other specific support areas/programmes. In addition to creating a favorable legal environment for the sector, the government is entitled to launch a series of support programmes to help these businesses overcome the specific commercial obstacles they face and exploit available opportunities effectively. These programmes include: facilitating MSEs' access to finance through relaxed collateral requirements by formal banking sector; encouraging and creating enabling ground for the establishment of MSEs-focused financial institution and through facilitated information on access to finance; provision of incentives schemes to MSEs by the government; encouraging partnerships for instance in the form of joint venture; provision of training in entrepreneurship, skill and management; facilitate access to appropriate technology, market, information & advice and access to physical infrastructure.

### **2.3.3 Criteria for Prioritizing MSEs for Support**

The strategy emphasise that as the MSE sector is highly diversified and characterized by an enormous number of problems at various degree and complexity, it is not possible to address the whole range of MSEs operating in different sectors at the same time. Thus, it is necessary to target certain groups of MSEs for the support programmes.

Even though, the identification and selection of priority target beneficiary MSEs depend on the specific conditions about the potential of the region, it is believed that, as identified by the Amhara region ReMSEDA, the following criteria shall be the main yardsticks for prioritizing the target MSEs.

- MSEs which are based on local raw materials and/or labor-intensive (local resource based)
- MSEs which have greater intra and inter-sectoral linkages (particularly those having higher linkage with agriculture)
- MSEs, which are engaged in import substitution and with a potential for export.
- MSEs engaged in activities that facilitate and promote tourism, etc.

- MSEs engaged in activities, which does not affect but rehabilitate the environment.
- MSEs engaged in activities and having a potential of creativity on the process of production and providing services.
- MSEs engaged in activities and having a potential of creativity on the process of production and providing services.

#### **2.3.4 Targeting Support Measures and Beneficiaries**

The vastness and complexity of the small and micro enterprises sector combined with serious financial and human resource constraints with respect to support programs and policies, necessitates focuses on target measures and beneficiaries. This implies that support measures have to be sectorally differentiated and packaged (in terms of finance, technology, information, training, market outlet, etc.) to address the various problems of MSEs.

Such target support packages will be designed by the regional agency in collaboration with other partners/stakeholders, the private sector, NGOs and the public at large.

In fact, it is difficult to develop a complete list of the target MSEs groups that qualify for the support packages, since circumstances may change overtime. Nevertheless, the following areas and/or target groups seem particularly relevant and they are identified and incorporated in the regional strategy paper.

- Small manufacturers with focus on food, textiles, and leather, clothing, metalwork, crafts, etc.
- Start-ups and expanding firms with particular emphasize to those owned by women.
- Small enterprises in drought areas.
- Agro-business and small-scale farming and fishing focusing on providing market information and promoting entrepreneurship ideas.
- Small builders/contractors.
- Small exporters revealing comparative advantage.

- Small-scale tourism industry operators.

### 2.3.5 Fundamental Principles

There are a number of general principles underlying this strategy's elements and which are meant to guide government's involvement in this sphere. The principles are also supposed to help orient the private sector, parastatal, NGOs and the stakeholders as to the role of the government vis-a-vis those of other players. The following are some of the principles as presented in the strategy paper.

- ◆ MSEs operate under ADLI strategy and market economy principles
- ◆ Government committed to develop MSEs via support services
- ◆ Emphasis given to advancement of women
- ◆ Regional states recognizes the diversity of legal and organizational forms
- ◆ Principles underlying this strategy are not static

Both the national and the Amhara region MSEs strategy papers highlight their roles, constraints faced by and the situation of micro and small enterprises at national and regional levels. The national strategy paper gives short description of the tasks and duties of regional and federal institutions, which are responsible for the provision of support service to MSEs. These institutions have already been established and started operations at regional and even at lower hierarchy up to zone level since 2001.

As one can clearly understand from the above discussion that the policy environment is conducive (both institutionally and strategy wise) to the enhancement of the small enterprise sector in the region. However, as discussed in chapter 6, even if the perception of the small enterprise operators in the study area is positive towards the private sector policy in general and the micro and small enterprises development strategy in particular, they emphasized that the support and services they are getting through the concerned government institution are not up to their expectation.

## CHAPTER THREE

### THEORETICAL AND CONCEPTUAL FRAMEWORK

#### 3.1 Theoretical Framework

There is large body of knowledge accumulated about firm growth in general. According to Laursen et al (1999), firm growth is a recently much debated issue both in economics, as well as in strategy research. In this debate it has been forcefully argued that the empirical evidence does not match theoretical predictions. According to Oliveria and Fortunato (2004), one of the most important strands in the literature on market structures vis á vis firm growth begins with Gibrat. The basic tenet underlying Gibrat's Law is that the growth rate of a given firm is independent of its initial size at the beginning of the examined period. Gibrat's Law, which assumes that firm growth is independent of size, was latter on subjected to empirical scrutiny, which will be discussed in the literature review part of this paper.

On the other hand, Papadaki and Chami (2002) explain that the relatively small body of business literature dealing with the reasons for small firm growth can be categorized in to two schools of thoughts. The first adheres to an organizational life cycle perspective, which sees growth as a natural phenomenon in the evolution of the firm. The second school of thought sees growth as a consequence of strategic choice. In either case the attributes of the business owner, organizational resources and environmental opportunity are crucial in expanding the firm or in overcoming the barriers to the evolution of the firm from one stage to the next.

According to some authors, "growth is the very essence of entrepreneurship," and commitment to growth is what primarily distinguishes small business owners and entrepreneurs (Liedholm and Mead, 1999, Voulgaris et al, 2001).

Classical economists were the first to acknowledge the role of the entrepreneur as an individual with special characteristics, with in the context of economic theory (Papadaki and Chami, 2002). Also according to some classical economists, the entrepreneur has the willingness and superior ability to make decisions, raise capital and assume the risk of failure.

Schumpeter (1939) added the superior ability to perceive new market opportunities - the entrepreneur as innovator.

Recent interest in integrating the role of the entrepreneur in to economic theory has attributed to an effort to explain some empirical regularities such as why do larger firms have higher and more stable rates of return than smaller firms? And why do smaller firms have higher and more variable rates of growth than larger firms. These theories that were developed, though abstract, shed light on some interesting aspect of business behaviour and provide an explanation of small business growth and evolution.

Both business and economic literatures recognize the role of the entrepreneur in business growth. They argue that differences in attitude and abilities among individuals are crucial in determining why some small firms grow and others do not.

In the theories of the firm, firm growth follows from, the assumption of profit-maximizing behavior and from the shape of the cost functions (Penrose, 1959). Thus profit-maximizing firms can achieve an optimal size if they behave rationally. A firm will grow until it has reached the size where long run marginal costs equal price, which is assessed as the "optimum" size of the firm. Relaxing the assumptions of this neoclassical theory of the firm permits many other explanations of firms' growth (Harabi, 2003).

Authors like Lucas (1978) equate the firm with the entrepreneur or manager and he assumes that a firm's output is a function of managerial ability as well as capital and labour. According to him, managers with higher abilities (i.e., higher efficiency levels) will have lower marginal costs and therefore will produce larger outputs.

Jovanovich (1982) later developed a model of the firm life cycle based on learning. According to his model individuals differ in their entrepreneurial abilities, but they are unsure of their abilities. In this model production technology is risky, partly because individuals are uncertain about their abilities and partly because production is inherently risky. Individuals who find out that they have underestimated their abilities in one period will expand out put in the next, while those that overestimated their abilities will dissolve their business.

Jovanovic's model has a set of important implications; young firms have accumulated less information than older firms about their marginal ability. Consequently, younger firms have more variable growth rates than older firms because they have less precise estimates of their true abilities. It follows that there will be more exits among younger firms, but also that among surviving firms, younger firms will grow faster than older firms. As younger firms tend also to be smaller firms, it is argued that the same observations hold for small firms as well. Surviving small firms are expected to grow faster than larger firms do and to have more variable growth rates.

Theories of entrepreneurial choice also explain some factors that determine small business growth. Accordingly, people have certain characteristics that are associated with the propensity for entrepreneurship. Individuals who have more of these characteristics are more likely to become entrepreneurs than those who have fewer. An individual chooses to create a new business so as to maximize his expected utility. Utility, in turn, is a function of entrepreneurial activity, such as one's taste toward work effort, risk independence, etc. Income, in turn, depends on the individual's ability to generate profit, such as managerial abilities to raise capital, and abilities to perceive new market opportunities and to innovate.

For Davidson (1989), firm growth is an indication of continued entrepreneurship. He notes that economic theories take the willingness to grow a business for granted, by assuming profit maximization. However, empirical evidence suggests that small business owners are reluctant to grow even if there is room for profitable expansion and that profitable firms of different sizes co-exist with in industries (Papadaki and Chami, 2002). Davidson argues that growth is a choice of the owner-manager and that profit maximization is only one of the possible motives for business growth. In empirical models of small firm growth, the characteristics of founders of businesses were linked to their growth aspirations (Davidson, 1989).

According to the theory of stages of development, growth is part of the natural evolution of a firm. As quoted in Voulgaris et al (2001), Scoff and Bruce (1989) proposed five stage models of firm growth; startup, survival, growth, take-off and maturity. In each stage of development a different set of factors is critical to the firm's survival and success. These among others

include the ability of the owner and the availability of enough cash to satisfy the greater demand for financial resources brought about by growth.

Many literatures dealing with firm growth associates the growth of firm with observable factors such as location, capital, sales, etc. However, due to this fact, in the words of Laursen et al (1999), firm growth has not been explained in a satisfactory way, as yet, there are still unexplored sources of explanation.

The vast majority of variation in firm performance, however, is not associated with traditional observables such as location, industry, size, age or capital, rather it is associated with unobservable factors specific to the firm or business unit, many of which appear to be permanent attributes of the business. One such attribute is the managerial or entrepreneurial capital of the firm.

## **3.2 Concepts and Definitions**

### **Small Scale Enterprises**

Definition is the fundamental issue or aspect facing all those who wish to understand what exactly a small-scale enterprise is and when it becomes medium sized or large? Efforts to define SSEs have led to a remarkable diversity of definitions in the literature. Policy makers, organizations, researchers, advisors, etc. all use a range of terms interchangeably in their effort to describe SSEs. To mention only a few, these include small business, small firms, small enterprises, small-scale industries, the informal sector, etc.

Hence, while there is a wide interest in SSEs, there is little agreement on the definitions and what exactly a SSE is (Andu-Alem, 1997). However, it is neither possible nor desirable to expect and attempt to provide uniform international criteria to define small-scale enterprises. Depending on its prevailing realities and objectives each country has to establish its own definition. In Ethiopia too, different government institutions adopted different official definitions to SSEs.

The actual definition adopted by the Ministry of Trade and Industry is as follows,

**Small Enterprises** are business enterprises with a paid-up capital of not less than Birr 20,000 but not more than Birr 500,000, but excluding high-tech consultancy firms and other high tech establishments.

CSA's definition of **small scale manufacturing enterprise** reads as, small scale manufacturing establishment engaging less than 10 persons and use power-driven machinery.

However, according to ILO (2004), for operational purposes, it is often agreed that micro-enterprise include self-employed persons and enterprises with up to 10 workers including apprentices and paid and unpaid family workers; small enterprises comprise between 10 and 50 workers. But, ILO proposes that these definitions have to be adapted to specific conditions prevailing in various countries.

### **Operational Definition of Small Enterprises**

Andu-Alem (1997), in light of some international qualitative and quantitative considerations and relating them to the Ethiopian situations tried to offer a more comprehensive definition to small enterprises. Therefore, as per his definition **Small Scale Enterprises** are those business activities that are:

- Independently owned and operated;
- Have a small share of the market;
- Are managed by the owner; and
- Employing 6-49 employees

However, now a days enterprise owner, particularly for relatively larger firms, in most cases would prefer to pass the management responsibility to hired managers. In such circumstances avoiding enterprises run by hired managers will reduce the number of enterprises to be examined. It is also evident that some enterprises may not be owned independently at the start-up, as it is the case among some enterprises in Bahir Dar. In such circumstances the first criteria has to be amended to accommodate partnering enterprises along with those

independently owned enterprises for partnership has been considered as one major factor of growth in this study.

Thus, this last definition, excluding the third criteria, serves as the Operational Definition of Small Enterprises in this study context.

### **Size of an Enterprise**

The size of an enterprise may be defined according to various criteria, including: the number of workers, the volume of output or sales, the value of assets, the use of energy, etc. ILO argue that the criterion of the number of workers is the most widely used, because of its apparent simplicity and because data on the other criteria are generally lacking. For operational purpose number of employees is used to represent enterprise size in this study context.

### **Measure of Enterprise/Firm Growth**

Employment or job creation is the primary objective set towards SSEs in the country. This has clearly been indicated in the SSEs development and promotion strategy of the country. Therefore, taking employment as measure of enterprises growth needs to be consistent with the goal set for the sector.

In this study, enterprise growth, as it is mostly applied to similar studies for developing countries because of serious problem associated with the availability of data, is expressed in terms of employment growth. The change in the number of workers since start-up is the indicator typically used to measure the magnitude of the net expansion of micro and small enterprises. This measure tends to be favored because it is most easily and accurately remembered by the entrepreneur and because it does not need to be deflated (Andreff and Redor, 2001; and Mead and Liedholm, 1998).

## **Entrepreneurship**

Entrepreneurship is a quality which is by no means only associated with small-scale enterprises and which is as necessary in government and public or cooperative enterprises as it is in private business. Individual small enterprises provide, however, both a nursery and ground for enterprise.

It is often stressed that the human being should be at the center of any economic activity. Given the human dimension of the enterprise, it is hence of utmost importance to mention the role of the entrepreneur.

It is not possible to identify an entrepreneur until identifying what exactly the concept of entrepreneurship is. As the term is usually a misused and confused one and a variety of definitions exist for it, it appears useful to briefly discuss what entrepreneurship involves (Anduaem, 1997).

Though there are a number of meanings and definitions given to entrepreneurship, they are meant to explain similar attributes of a business. According to Ahmed (1995), Entrepreneurship traits include initiative, managerial ability, innovative ideas and drive. Education and training are needed to assist a person to become a successful entrepreneur.

A popular definition of entrepreneurship is that "It is the process of doing something new and something different for the purpose of creating wealth for the individual and adding value to the society" (KAO, 1993 as quoted in Anduaem, 1997).

According to Malecki (1994), the term entrepreneurship has several levels of meaning, which makes it hard to reach a consensus about an appropriate definition. At one level, it refers simply to small firms or enterprises although entrepreneurship within giant corporations has also become part of the vocabulary. He explains entrepreneurship to involve accumulated knowledge, values, experiences and resources.

The common definition of entrepreneurship is that it is a quality required perceiving opportunities, organizing resources, creating facilities and setting up and running a business successfully.

A wide variety, of definitions for the term entrepreneurship exists. However, entrepreneurship in this study context is perceived in the perspectives of the definitions and explanations offered by Ahmed and KAO. Entrepreneurship is essentially a creative activity that consists of doing things that are not generally done in the ordinary course of business.

A reasonable level of entrepreneurship is necessary for successfully running of small enterprises as they involve relatively complex decision making in terms of production and sales. Also a certain level of entrepreneurship is necessary for properly managing enterprises however tiny they might be.

## CHAPTER FOUR

### REVIEW OF RELATED LITERATURES

#### 4.1 The Dynamics of Small Enterprises

Most of previous studies on firm dynamics and their analysis relating to small enterprises have been static in their orientation (Liedholm and Mead, 1999). However, studies have recently been conducted in a number of countries that provide a framework for better understanding of patterns of enterprise births, survival or closures, and growth. These studies of small firm dynamics are important because they provide insights in to the feasible and desirable patterns of growth in out put and employment (Liedholm and Parker, 1989).

Small firms are in a constant state of flux (Mead and Liedholm, 1998). This implies during any given period, new firms are being created (new starts, or enterprise births). While others are closing; at the same time, some existing firms are expanding and others are contracting in size. An important part of the process lies on better understanding the growth process among the micro and small-scale enterprises.

Analysis of small firm economics usually focuses on the dynamics of growth and survival, and on business formation (Ozcan, 1995). The relevant theoretical literatures and empirical evidences relating to the dynamics of micro and small-scale enterprises are found at firm level. According to the same authors, theoretical literatures on firm dynamics are quite limited. The classical theory of the firm sheds little light on the formation, growth or dissolution of individual firms. The classical theory for Liedholm and Mead (1999) is a static equilibrium theory, with no implications for the rate of entry, exit or speed of adjustment. Moreover, it assumes that the supply of entrepreneurs is perfectly elastic, and that no learning occurs with in the firm. Traditional neoclassical theory of the firm is also limitly useful, because firms are not endogenous, but production functions showing the relation between out put and inputs (Groenewegen, 1993). These "firms" operate in a given and static environment.

As pointed out by Mead and Liedholm (1998), empirical evidences on new business starts in developing countries, though limited in number, makes clear that new small enterprises are being established at a substantial rate. The results of those studies revealed that the annual rate at which new enterprises are started in the surveyed countries averaged over 20%, ranging from just below 20% in Kenya to over 30% in Botswana. These surprisingly high figures are substantially above the 10% rates typically reported for small enterprises in industrialized countries. As indicated in many literatures, relatively little is known about the factors driving the micro and small enterprises new start rates. But a recent study focusing on MSEs in Zimbabwe indicates that determinants of new starts differ between high and low return activities (Mead and Liedholm, 1998). For high return activities, initial capital requirements, experience of the entrepreneur and the level of regulations are all inversely related to new start rates. For low return activities, the rate of new starts is related (inversely) only to the aggregate level of economic activity; for these firms, the lower the level of aggregate economic activity, the higher the rate of new starts.

Liedholm and Parker (1989) identified excess demand for the goods of a small firm and excess supply of labour capital or other inputs to be responsible in stimulating firm starts in Africa.

Somewhat more empirical evidence exists on the closure (or death) rates of small firms in developing countries (Liedholm and Mead, 1999). They also noted that most empirical studies have indicated that mortality rates are inversely related to firm size, which means closure rates decline as one move to large size categories of firms. Nevertheless, one of the relationships found most consistently in empirical studies of firm dynamics is between firm closures and the age of the firm. Virtually all the empirical studies indicate that there is a strong inverse relationship between the age of the firm and the failure rate. Indeed, most disappearances occur during the early years of a firm's existence.

Liedholm and Mead (1999) holds that empirical relationships between new start rates of micro and small firms and other variables have not been systematically examined in any developing country. Empirical evidence on new business starts in developing countries makes clear that new micro and small enterprises are being established at a substantial rate.

Moreover, it is indicated in study works conducted on micro and small enterprises in Africa that the vast majority of new firms being created are one-person establishments.

The other dimension of firm dynamics is firm survival. Some studies gave particular attention to this aspect of firm dynamism i.e. firm survival, as in Agarwal and Gort (2000). The study decomposes the determinants of firm survival in to firm and product (industry) attributes. It is found that the principal variables that affect hazard rates are learning by doing, the dynamics of attrition of inefficient firms and technological intensiveness. All the three variables follow a predictable course over the life cycle of the firm. Hence, survival is viewed as a function of a vector of firm variables and vector of industry variables. Many other studies conclude that the survival rate of small enterprises is determined by location, sector in which the enterprise is operating, and gender of the entrepreneur i.e. female-headed enterprises are less likely to survive.

Several recent formulations of firm dynamics, on the other hand, have accorded a much more central role for the entrepreneur in firm dynamics Liedholm and Mead (1999) argue that entrepreneurs have different abilities, yet entrepreneurs are unsure about these abilities when a new business is established. Entrepreneurs gradually "learn" about their abilities by engaging in the rough and tumble business world and observing how well they perform. As they learn more about their own abilities, entrepreneurs change their behavior over time: those who revise their ability estimates upward expand, while those who revise them downward tend to contract or disappear.

The model is, in fact, developed by Jovanovic (1982). His model synthesizes the key elements of these entrepreneurial models with those of the stochastic models and generates a rich set of testable hypotheses about the life cycle patterns of firm growth. In general terms, this model indicates that the age and size of the firm play a crucial role in firm growth. More specifically; this particular "learning" model predicts that both the firm's failure rates and growth rates will be inversely related to the age and initial size of the individual firm. However, Jovanovic's model does not indicate what the key determinates of this managerial ability might be or how other important variables might affect firm growth.

## 4.2 Empirical Literatures on the Determinants of Firm Growth

Small business success, as well as all business success is predominantly measured in either increases in turn over, or revenue or in increases in the number of people employed (Berkham et al., 1996; Holmes and Zimmer, 1994; and ILO, 2004). Some studies define small firm growth as the average change in sales. Most other studies, particularly those in developing countries, measure firm growth as a change in number of employees.

The early growth theories of firm are based on Gibrat's Law, which states that firm growth is independent of firm size. The basic tenet underlying Gibrat's Law is that the growth rate of a given firm is independent of its initial size at the beginning of the examined period.

Recent literatures on firm growth reveal that previous studies on the determinants of small enterprises drew many useful findings and conclusions. Early studies on firm growth stemmed as an important issue of the investigation of Gibrat's Law and the testing of the relationship between firm size and growth. Gibrat's Law, which indicates that firm growth is independent of firm size, has been used as the basis for a number of theoretical formulations (Ozcan, 1995).

Subsequent studies on determinants of firm growth argue that Gibrat's Law does not hold very well empirically. In Geroski (1995), a number of stylized facts and results are presented which summarize recent empirical works. Some of the major findings have been that i) firm survival tends to increase with firm age and firm size and ii) firm growth tends to decrease with firm age and size. Evans (1987) and Harabi (2003) concluded that Gibrat's Law must be rejected for smaller firms.

Some of the recent theoretical works on industry and firm evolution have generated testable hypothesis about this process. More over as Davidsson and Henrekson (2001) pointed out, large bodies of these empirical researches aim at identifying micro-level factors explaining the emergence and growth of firms.

Results of empirical study by Harding et al (2004) indicated that for larger firms, there is essentially no relationship between growth and size. The findings of a study by Hart and Oulton (1996) on firms' variance of growth and size in UK revealed that the variance of growth varied widely across size classes of company. In the very smallest and very largest size classes it declined with increase in size of company. But for most size classes it increased with increase in size of company. While there is no simple relationship between size of company and variance of growth, there is a clear negative relationship between this variance and mean growth for most companies.

However, the important conclusions emerging from the growing empirical literature is that firm survival increases with the age and size of the firm. As quoted in Papadaki and Chami (2002), "Jovanovic (1982) relate this observation to incomplete information on efficiency levels. Firms learn their true costs only subsequent to entry; efficient firms grow and survive while inefficient firms shrink and die."

Liedholm and Mead (1993), arrived at similar results in their analysis of small firm survival and growth in Africa, and found that small enterprises with initial size and which are male-owned have higher survival and growth likelihood. The result of the same study indicates that growth likelihood is higher for younger firms. They presented a summary of the relationship between firm age, size, location and gender, and survival and growth likelihood of MSEs based on econometric results of research works undertaken in four South African countries and Dominican Republic. The results are displayed in Table 4.1. Most of the findings reveal that determinants of MSE survival and growth identified in the study are consistent with most empirical literature findings.

**Table 4.1 Key Determinants of MSE Survival and Growth**

<b>Factors of growth (firm characteristics)</b>	<b>Survival Likelihood (Higher if MSE is:)</b>	<b>Growth Likelihood (Higher if MSE is:)</b>
Age	Older	Younger
Past growth	Growth in past	-
Initial size	Smaller	Smaller
Sector	Not in trading	In particular sectors that vary by country
Location	Urban, Not in home	Urban, Not in home
Gender	Male-owned	Male-owned

Source: The dynamics of micro and small enterprises in developing countries, World Development, Vol.26, No.1, P.66.

*Note:* Smaller, older and younger in the above table stated relative to the firms considered in the analysis

As to the factors promoting or determining firm growth, an empirical analysis from Morocco by Harabi (2003) indicated that the following are the principal determinants of firm growth: location in large urban centers; the presence of price competition; presence in markets with high demand; product diversification and market share expansion; and certain government policies such as labour regulations. The study also found out that the principal factors impeding firm growth are lack of access to qualified workers and managers; location in smaller population centers and certain government policies and regulations. However, according to his analysis results, tax regulations, the level of taxes, and labor regulations do not seem to affect expected firm growth negatively. Despite this, there is different argument concerning the effects of tax on enterprise growth. For instance, Reinecke (2002) in his study indicated that tax deposit system and tax differentials in Uganda penalized small enterprises thereby affecting their growth.

As explained in Liedholm and Parker (1989), results of analysis of survey on small scale manufacturing enterprise in Sierra Leone, further substantiate the prime role of location to firms' success. The study indicate that none of the enterprises in the smallest rural area expanded at all; in localities with 2,000 to 20,000 inhabitants, 13 percent of the surviving firms added workers, while in the larger localities with 20,000 or more inhabitants, the percentage of firms growing was 31 percent.

According to Voulgaris et al. (2001), impediments to growth have been found to be low access to financing and to sources of information and technology. Lack of technical and managerial skill, inadequate organizational adaptability and ability to acquire or use new technology are considered also as impediments to growth. The authors argue that the lack of resources experienced by most small firms suggest that substantial benefits might be obtained through the development of strategic partnership with other small or even large- size firms. Ozcan (1995) also suggested the need for developing networks capable of delivering economies of scales and greater market penetration for successful enterprise growth performance.

Voulgaris et al (2001) relate successful growth of firms with entrepreneurial attributes. According to him many entrepreneurs choose not to grow because of fear of loss of personal control of the firm, fear of having to go in to debt or reluctance to pass the responsibility of running the business over to professional managers. Similar argument offered by Andreff and Redor (2001). They indicate that in theoretical terms the business creator is above all an "entrepreneur" whose individual characteristics are one of the determinants of new-business growth. According to Papadaki and Chami (2002), the entrepreneur has the willingness and superior ability to make decisions, raise capital and assume the risk of failure. They observe that firm's output is a function of managerial ability as well as capital and labour. These Authors drew many useful findings and conclusions from their empirical work on data obtained through survey of 1,337 small business establishments in Canada. They consider such variables as education level, age, gender, growth motivation and management know-how of the owner (manager) and other business practices as well as age and size of the firm. Their findings reveal that level of education, informal net working, partnership, innovation and market focus have significant impact on small firm growth. They also conclude that age and size of the firm have significant impact on firm growth.

But, for Bager and Scott (2002), important growth determinants of private firms are not only the education, age and gender composition of the firm's owner-manager but also the staff and its level of income. They conclude that those entrepreneurs who make their firms grow are relatively young and that those who make their firms survive are more experienced and older. If education and income levels are understood as indicators of knowledge and financial assets, young age are seen as empirical indicators of entrepreneurial orientation. They also comment

that these results support those who argue for an integration of resource-based theory and entrepreneurship theory in the growth field.

Person (2002) in her study on the survival and growth of new establishments also observed an important positive relation between educational and demographic factors, and survival and growth of firms. According to her study's results, although the probability of an establishment surviving is less, if the work force (including the owner) is very young, such establishments do grow faster provided they stay in business. New establishments dominated by workers with the lowest level of education exhibit a lower rate of growth.

## **CHAPTER FIVE**

### **METHODOLOGY**

#### **5.1 Study Design**

The universe of inquiry for this study includes the small-sized enterprises operating in Bahir Dar Town, while "small enterprises" refers to those enterprises categorized as per the context of the definition offered by this study. The researcher found the case study design to be suitable for the investigation. Accordingly, all the small enterprises, which are engaged in manufacturing activities and that are operating in Bahir Dar town, are the subject of this study.

#### **5.2 Data Collection Methods**

Both primary and secondary sources of data are used for the analysis. The secondary data include information that are obtained mainly from formal sources i.e., Amhara ReMSEDA, Bureau of Trade and Industry for the Amhara Region, Bahir Dar Special Zone Micro and Small Enterprises Development Agency. In addition, different reports, bulletins and literatures, which are relevant to the theme of the study, were gathered from various sources to complement the survey-based analysis.

The primary data source is enterprise/firm-level interview/survey. In the survey, each and every owner or manager of small manufacturing enterprise operating in Bahir Dar has been approached through a questionnaire (see Appendix 2).

Before conducting the survey it was imperative to get a complete list of small enterprises operating in the town. Accordingly, it was possible to get the list both from the Bahir Dar Special Zone Micro and Small Enterprises Development Agency and the Amhara ReMSEDA. The list incorporated some basic data like name and type of the enterprise, employment, year of establishment, address (kebele), etc. The enterprise lists that were obtained from these

sources were cross-checked and made ready for use as a guide and reference before the start of the interview and at the time of the interview.

### **5.3 Sampling Design**

The researcher considered the method of approaching the entire small manufacturing enterprises in the study area as appropriate. The major reason behind is that according to recent survey conducted by CSA i.e. Survey on small scale manufacturing industries (2001/2002), the number of small manufacturing enterprises working in Bahir Dar does not exceed 100. However, latest data from the Bahir Dar special zone Micro and Small Enterprises Development Branch Office reveal that the total number of small enterprises engaged in manufacturing activities, excluding grinding mills, is 134. Hence, taking sample out of such population would not be advisable and desirable. Therefore, efforts have been made to gather primary data from all establishments using the instruments.

The data were to be collected from all small manufacturing enterprises that, according to records of the Bahir Dar special Zone Micro and Small Enterprises Development Office, are 134 in number. The figure includes small manufacturing enterprises, which are registered, and legally operating in the town. However, during the time of survey additional number of enterprises, which are not registered in the lists of the office, were found. This makes the figure exceed the number that is reported in the list. Among these all small enterprises, around 87 found to satisfy the criteria to be included in the survey, the main criterion being their consistency with the definition given in this study's context. Of these selected small-manufacturing enterprises, only 76 enterprises were willing to provide the required information while the other 11 in one way or another failed to respond. This makes up the response rate 87 percent. The small enterprises to be included in the study had to have 6 and more number of employees three year prior to the survey.

**Table 5.1 Type and number of enterprises surveyed**

<b>Type of enterprise/production</b>	<b>Number of establishments</b>	<b>Percent</b>
Bakery	5	6.6
Furniture	26	34.2
Edible oil	4	5.3
Brick and cement pipe	12	15.7
General metal works	25	32.9
Metal and wood works (combined)	4	5.3
<b>Total</b>	<b>76</b>	<b>100</b>

Source: Data collected from field and computed by the Author.

#### **5.4 Instruments**

A structured interview survey questionnaire was used as a major instrument of primary data collection. Structured questionnaire involving both close and open-ended questions was employed for enterprise-level interview.

Five enumerators were recruited and trained for the purpose of gathering enterprise-level survey data, which was successfully accomplished. In addition, the researcher himself managed the interview together with the enumerators.

To administer the data collection more easily, the close and open-ended questions were first translated in to Amharic to be used during the interview. Then after the enumerators went for one day pre-testing of the questionnaire before it was put in to use for the survey. Each enumerator tried to complete two questionnaires during the test. The test exercise also gave opportunity for the researcher to make some minor amendments on the questionnaire for the final interview.

Accordingly, the majority of the small enterprises that were operating in the study area and which were eligible as per the definition given in the study were interviewed.

## **5.5 Data Analysis**

The data gathered has been analyzed in line with the study objectives already identified and the findings have been considered at each methodological level first. The analysis was carried out after the data were categorized and disaggregated in to appropriate descriptive statistics, some of which were presented in frequency tables.

Cross tabulations from the descriptive statistics for some key variables of the study were constructed to supplement to the output obtained through the application of the model. Multiple Linear Regression was used to estimate the coefficients and analyze the determinants of enterprise/firm growth, which is the main theme of the study.

The portion of data that were necessary for the analysis and which were obtained through the close-ended questions of the questionnaire have been entered in to the SPSS software for further tabulation of the out puts and for estimation of the econometric results. Finally the output has been analyzed and interpreted in such a way that plausible answers would be sought for the questions raised in the research.

## **CHAPTER SIX**

### **DATA ANALYSIS AND INTERPRETATION**

#### **6.1 Characteristics and Profile of the Small Enterprises Surveyed**

The data used for the analysis in this study are obtained through survey, which has been conducted on small manufacturing enterprises operating in Bahir Dar town. The data are both qualitative and quantitative types. The model chosen for estimating the average value of the variables under consideration depends primarily on data gathered with the help of the survey.

The small enterprises incorporated in the survey are from different sectors, which are engaged mainly in activities such as manufacturing of food items, furniture production, metal works and non-metal items processing. In the section that follows the data are described and interpreted in detail with the help of appropriate tables.

##### **6.1.1 The General Characteristics of the Enterprises**

Table 6.1 shows the type and number of small scale manufacturing firms considered in the study. The table also exhibits that enterprises engaged in furniture production (34.2%) accounts for the largest number of the enterprises covered by the study which is followed by general metal works (32.9%) while those engaged in edible oil production, metal and wood works (combined) and bakery constitute the smallest proportions which individually account for 5.3%, 5.3% and 6.6% of the total respectively.

**Table 6.1 Type and number of enterprises covered by the study**

Type of enterprise	Count	Percent	Cumulative percentage
Bakery	5	6.6	6.6
Manufacture of furniture	26	34.2	40.8
Manufacture of brick & cement pipes	12	15.7	56.5
Manufacture of edible oil	4	5.3	61.8
General metal works	25	32.9	94.7
Metal & wood works (combined production)	4	5.3	100.0
<b>Total</b>	<b>76</b>	<b>100</b>	

Source: Data collected from field and computed by the Author.

It is observed that almost one-third of all the enterprises exhibited no growth (either negative or zero growth) over the three-year period considered in the study. About 13.2 percent of the firms declined in size while more than 18 percent of them have been stagnant in terms of growth. But, well over 68 percent of the establishments more or less experienced some positive growth.

**Table 6.2 Number of establishments and the observed rates of growth**

Observed rate of enterprise growth	Number of establishments	Percent	Cumulative Percentage
-20% - -4%	10	13.2	13.2
Zero (no) growth	14	18.4	31.6
1% - 10%	9	11.9	43.5
11% - 30%	34	44.7	88.2
More than 30%	9	11.8	100
<b>Total</b>	<b>76</b>	<b>100</b>	

Source: Data collected from field and computed by the Author.

Among growing enterprises, the average growth rate is 18 percent while the highest rate of growth of employment in the growing firms reaches 60 percent. The highest rate of negative employment growth in the declining firms' category is 20 percent.

**Table 6.3 Observed pattern of small enterprises growth by type of enterprise**

Type of enterprise	Number of enterprises	Percentage of enterprises falling under each growth category				Total
		Negative growth	Zero growth	Positive growth (1% - 30%)	High growth (>30%)	
Bakery	5	40	20	40	-	100
Furniture	26	7.8	15.4	57.7	19.1	100
Edible oil	4	25	25	50	-	100
Bricks and cement pipes	12	-	-	91.7	8.3	100
General metal works	25	20	28	44	8	100
Metal and wood works (combined)	4	-	25	50	25	100
<b>Total</b>	<b>76</b>	<b>13.2</b>	<b>18.4</b>	<b>56.6</b>	<b>11.8</b>	<b>100</b>
<b>Number of growing/stagnant/declining enterprises</b>		<b>10</b>	<b>14</b>	<b>43</b>	<b>9</b>	<b>76</b>

Source: Data collected from field and computed by the Author

On the other hand, all of the enterprises engaged in bricks and cement pipe production have experienced some positive growth. However, bakery constitutes large number of enterprises (60%) having negative and stagnant growth. Likewise, edible oil and general metal works respectively account for 50% and 48% of them declining or exhibiting no change at all. Those enterprises engaged in furniture and combined production of metal and wood works have experienced the highest rate of growth i.e. more than 30%, and at the same time they embrace the largest number of enterprises having some positive growth.

### 6.1.2 Profile of the Small Enterprises

This section highlights descriptive statistics from the small manufacturing enterprise survey as they related to the explanatory variables that have been selected for this study.

## Owner-manager characteristics

Men own the majority of the small enterprises surveyed. This is in fact, one of the common features of small enterprises in the country. The data reveal that of the total, 13.2 percent of the operators are women.

Another indicator of owner-manager characteristics is age of the operator. The minimum age reported by the entrepreneurs is 23 and most small enterprise owners are between 23 and 30 years of age. Those enterprise owners whose ages fall between 31 and 49 old accounts for 25 percent of all the operators covered by the study while the rest 33 percent represents enterprise owners with ages of 31 through 49 old. Table 4 displays age distribution of small enterprise owners.

**Table 6.4 Age of small enterprise owners by age category**

<b>Age Category</b>	<b>Count</b>	<b>Percent</b>
23 - 30	32	42
31 - 49	25	33
50 and above	19	25
<b>Total</b>	<b>76</b>	<b>100</b>

Source: Data collected from field and computed by the Author.

A high school education level or 9-12 grade is the highest level of formal education attained for 51 percent of small enterprise owners. Whereas 7.9 percent of the owners have a college diploma and 9.2 percent have primary (1-4) level of education.

**Table 6.5 Level of education of small enterprise owners**

<b>Grade</b>	<b>Number of owners</b>	<b>Percent</b>
1 - 4	7	9.2
5 - 8	15	19.8
9 - 12	39	51.3
12+1	9	11.8
12+2	6	7.9
<b>Total</b>	<b>76</b>	<b>100</b>

Source: Data collected from field and computed by the Author.

Around 46 percent of the operators reported that they have prior experience in the same industry either in the form of paid-employment in similar enterprise or part time work. According to them, their experience has been the major driving factor for them to be engaged in the current business they run. Another 44.8 percent stated that they started their business because they saw prospects for growth in their current business or they had enough money to run their enterprises.

**Table 6.6 Operators' reasons for choosing their current businesses**

<b>Reason</b>	<b>Count</b>	<b>Percent</b>
I have Prior paid-employment experience	35	46
I have enough financial capacity to run the business	5	6.6
I saw prospects for growth	29	38.2
Other reasons	7	9.2
<b>Total</b>	<b>76</b>	<b>100</b>

Source: Data collected from field and computed by the Author.

With regard to ownership, nearly 11 percent of small enterprise owners reported that they had joint investment with a partner at start-up of their business. Their partners were mainly individuals other than parents. However, for 61 percent of the owners, own saving has been the major source of initial capital while 26 percent of them depended on borrowing from relatives and banks to secure fund for their venture.

### **Business practice characteristics**

Most small enterprises focus on markets around their establishments. Over 67 percent of small enterprise owners operating in the study area reported that they have no market network in areas other than Bahir Dar. As a result, their market size is concentrated in and limited to the town. On the other hand, 33 percent of the respondents mentioned that they have markets in other towns in addition to Bahir Dar. These market areas include not only the nearby small towns but also big towns like Gondar and Debre Markos.

For 17 percent of small enterprise operators, bank loan has been the major source of financing. Among these enterprises only 5 percent had the opportunity to obtain loan for 1 or more times. Most of the owners also reported that though they considered external loan to be their critical source of finance, they couldn't manage to get bank loan, the major reason being their limited capacity to satisfy the requirement of guarantee requested by banks. A good number of small enterprise owners also mentioned that the collateral requirement of credit and saving institution operating in the town also has limited their access to credit.

### **Firm characteristics**

Nearly 43 percent of the enterprises had been in operation at least 6 years or more at the time the survey was conducted. 9 percent of the firms had more than 20 years of age while 44 percent of them have been in operation for not more than 5 years.

**Table 6.7 Age of small-enterprise establishments by age group**

<b>Age of firms (in years)</b>	<b>Count</b>	<b>Percent</b>
3 - 5	44	57.8
6 - 10	15	19.9
11 - 20	8	10.4
More than 20	9	11.9
<b>Total</b>	<b>76</b>	<b>100</b>

Source: Data collected from field and computed by the Author.

The size of enterprises in this study context refers to the number of paid-employment provided by small enterprises. Nearly 82 percent of small enterprises had 6 to 10 employees at the time of the survey. However only 3 enterprises reported that they owned 36 to 46 permanent employees. These enterprises with relatively large number of employees are found in general metal works and small-scale industrial engineering enterprise category.

**Table 6.8 Size of small enterprises by employment-size category**

<b>Size Category</b>	<b>Number of enterprises</b>	<b>percent</b>
6 - 10	62	81.8
11 - 20	7	9.1
21 - 30	4	5.2
31 - 46	3	3.9
<b>Total</b>	<b>76</b>	<b>100</b>

Source: Data collected from field and computed by the Author.

### **6.1.3 Major Constraints and Problems of the Small Enterprises Surveyed**

Several factors could explain the declining growth of small enterprises operating in the study area. Their degree of influence too, may differ from one enterprise to the other.

Currently, the most significant obstacle to the majority of operators to expand their business is the level of tax levied on their enterprise, which is followed by problems of getting working premises and credit. 90 percent of small enterprise operators reported the level of tax to be the most serious obstacle to doing business. They stressed that its impact could lead to the extent of closure of their firms in the near future. Getting working premises and problem of low access to credit facilities are the second and third most important problems facing the small enterprise owners. According to the responses of the owners approached during the survey, the main constraint that hinders small enterprise operators' access to credit has been the collateral and bank guarantee requirements of bank, and credit and saving institutions.

On the other hand, 78 percent of the respondents mentioned infrastructure related problem including public services such as electricity and water is currently not a problem to their enterprises. Only 4 percent of small enterprise owners reported that infrastructure is their major problem.

Table 6.8 shows lists of major problems to business growth as identified by small enterprise owners in the study area. The majority of enterprise owners (61 percent) consider government's attitude towards private business to have positive effect. In fact, according to

their response, though they are aware that government has given due emphasis to the sector through its support programme, they cannot witness any tangible support and backstopping practically extended by the government through its responsible offices or institutions. Constraints such as lack of market demand, low level of competitive power and lack of raw materials have also entailed obstructing impact to the success and growth of most enterprise.

**Table 6.9 List of major obstacles of small enterprise operators to expand their businesses as reported by owners**

Type of the problem	Responses (in %)			
	Not a problem	Minor problem	Moderate problem	Major problem
Uncertainty about the economy (i.e. demand & competition)	58	5	16	21
Government's attitude towards private investment	61	7	14	18
The level of tax	4	1	5	90
Getting credit & working capital	40	6	15	39
Rate of interest to bank loan	44	17	28	11
Lack of market demand	32	17	22	29
Lack of raw materials	33	5	32	30
Infrastructure-related problems	78	5	13	4
Low level of competitive power	29	18	21	32
Getting working premises	12	12	31	45

Source: Data collected from field and computed by the Author.

## 6.2 Model Specification, Estimation and Interpretation

### 6.2.1 Model Specification

A variant of Evans' empirical model (1987b) was used to estimate the impact of, owner and firm characteristics on firm growth. Evans' model estimates the impact of firm age and firm size on firm growth. In order to model the growth of micro-enterprises capturing additional factors such as owner and business operations characteristics, dummy variables were added to Evans' model. Evans (1987b) defined firm growth as,

$$[\ln S(t') - \ln S(t)] / \mu = \ln G(A(t), S(t)) + u(t),$$

Where;

$S$  is firm size, measured by number of employees,

$G$  is growth function,

$A$  is firm age,

$t$  is time where  $t' > t$ ,

$\mu = t' - t$ , and,

$u(t)$  is normally distributed with zero mean and independent of  $A(t)$  and  $S(t)$ .

In order to take into consideration non-linearities in the functional form of growth, a second-order expansion of  $\ln G(A(t), S(t))$  can be estimated

$$\ln G = b_0 + b_1 \ln S + b_2 \ln A + b_3 (\ln S)^2 + b_4 (\ln A)^2 + b_5 (\ln S) (\ln A) + u$$

Adding dummy variables to this equation that capture business and owner characteristics,  $\Sigma$  (B, O), the final regression equation is of the form:

$$[\ln S(t') - \ln S(t)] / \mu = b_0 + b_1 \ln S + b_2 \ln A + b_3 (\ln S)^2 + b_4 (\ln A)^2 + b_5 (\ln S) (\ln A) + \Sigma (B, O) + u$$

Thus  $\mu$  takes the value of 3, and the firm's growth rate is calculated as the log difference between the current number of employees and number of employees three years prior to the survey.

The statistical analysis included checks for heteroscedasticity and multi-collinearity. The problem of heteroscedasticity arises if the error terms in the regression equation are distributed unevenly across firms of different age and size. This possibility is tested in this study using White's test. White's test involves regressing  $\hat{u}_i^2$  on the size and age variables and their squares and cross products. When  $R^2$  for this regression is highly significant, the test rejects the hypothesis of homoskedasticity.

The issue of multi-collinearity arises if the independent variables are highly correlated. A common method to detect multi-collinearity is through the use of the tolerance number, defined as  $(1-R^2_i)$ , where  $R^2_i$  is the squared multiple correlation coefficient between  $x_i$  (the independent variable) and the other explanatory variables. It is clear that while there is no strict cut-off value, a tolerance value below 0.4 is suggestive of multi-collinearity.

### **6.2.2 Variables or Factors of Enterprise Growth and Hypotheses**

The dependent variable is measured as the average annual growth rate of employment. Hence the firm's growth rate, the dependent variable in this case, is calculated based on the number of employees at present and three years prior to the survey. The following part discusses the independent variables, which are used to construct relationship with the dependent variable in this study.

#### **i) Gender and age of the owner**

It has been proposed in the literature that women may have fewer opportunities to develop relevant experiences, may have fewer networks to get assistance and may have greater difficulty in assembling resources.

There is some evidence that banks may impose more stringent requirements on women business owners in regard to collateral for loans, and therefore limit their ability to grow. Women may also be more family oriented and be less keen in pursuing economic goals related to expansion of the firm. According to some authors like Papadaki and Chami (2002) and Buvinic (1993), being female had a negative impact on the growth of small ventures but had no impact on the survival of the firm. It is also suggested in the literature that younger individuals may be more willing to assume risks and grow their business.

#### **Hypotheses**

- Male - owned businesses exhibit higher growth than female - owned enterprises
- Growth is higher for enterprise owners who are less than 31 years old.

## **ii) Education**

Education is presumably related to knowledge and skills, motivation, self-confidence, problem solving ability, commitment and discipline. Higher education is expected to increase the ability of the entrepreneur to cope with problems and seize opportunities that are important to the growth of the firm. Many authors in the area found a positive relationship between prior level of education and firm performance.

### **Hypothesis**

- Enterprises whose owners have a post-secondary education (diploma and above) exhibit higher growth than enterprises whose owners had only secondary education.

## **iii) Industry - specific know how: prior paid - employment experience in business**

Empirical evidence suggests that business similarity can have a significant impact on the success of a business venture in terms of both the survival and growth of the business. It is assumed that industry - specific know - how, ranging from tacit knowledge of the products, processes and technology, to specific human capital investment in relationships and good will with specific customers, supplier or stakeholders; reduce the "liability of newness" associated with new entrepreneurs and hence enhances their ability to obtain credit, develop sales and achieve other forms of co-operation.

### **Hypothesis**

- Enterprises whose owners had experience in business in the same industry exhibit higher growth than enterprises whose owners did not have such an experience.

## **iv) Partnerships**

The presence of partners who can offer the owner - manager support with the management of growth can be a positive influence. Partners may add to the resources and skills bases of the venture. They may also enhance the credibility of the venture to potential lenders and other

constituents. Benefits associated with the presence of partners include capital, functional expertise and a broader range of management experience.

### **Hypothesis**

- Growth is higher for enterprises that at start - up shared ownership with other partners, such as other family members, other employees of the enterprise and business partners.

#### **v) Sources of financing**

Empirical evidence suggests that retained earnings are the predominant source of financing among growing SMEs. However, more successful SMEs use more external sources of financing, such as financial institutions, venture capitalist and individual investors, than do less successful firms. Therefore, as Harabi (2003) explains, the source of financing is an indicator of financial capital available to the firm and is expected to have an impact on the growth performance of the business.

### **Hypothesis**

- Growth is higher for enterprises that have used debt financing in the form of bank and/or government loans.

#### **vi) Market size**

A number of empirical studies have confirmed the importance of market demand for a firm's growth and innovative activities. Dynamic economic theories also suggest that growth demands strategic flexibility and the ability to change market focus, which may require introducing new product or entering new markets. It is, hence, concluded that there is a positive correlation between market size and firm growth.

### **Hypothesis**

- Growth is higher for firms with relatively large market size

## vii) Firm's age and size

Many empirical studies in the developed countries have found that there is a negative relationship between firm growth, age and size. Recent empirical studies suggest a negative correlation between firm age and firm growth - younger firms grow faster. Decreasing returns to learning over time is one major reason for this (Harabi, 2003). A study by Brock and Evans (1986) concludes that firm growth decreases with firm age for firms with fewer than 25 employees, but increases with firm age for firms with more than 25 employees. Given that our study consists of small firms (around 96 % of them own less than 25 employees each), we would expect to find a dominantly negative relationship between growth and age of the firm. Likewise, firm size in 2002 might have a negative impact on expected firm growth in the subsequent years (2003-2005): the larger a firm was in 2002, the smaller the probability of it being expected to grow in the next three years.

### Hypothesis

- ◆ Firm growth decreases with firm age and size.

### 6.2.3 Estimation and Interpretation of the Regression Results

As mentioned in model specification part, the firm's growth rate is calculated as the log difference between the current number of employees and number of employees three years prior to the survey. Three years time or specifically year 2002 was selected not only because it became easy for them remember their number of employees (since the year is relatively not far) for most of the enterprises approached during the survey (and particularly for those which did not have records) but also large number of them reported 2002 to be year of their establishment. The independent variables are age and size of firms where size is understood in terms of number of employees. Dummy variables that represent owner-manager characteristics and business practice characteristics were added to make the model more sound in its prediction. Dependent and independent variables specifications and descriptions are presented in Table 6.10.

Since our objective is estimation as well as inference, we have assumed that the  $u_i$  follow some probability distribution. In this model the  $u_i$  follow the normal distribution with zero

mean and constant variance  $\sigma^2$ . This is shown in Appendix 1.1. The coefficient of determination ( $R^2$ ) is equal to 0.607, which implies that the model has good predictability.  $R^2$  is not very high may be because the data were cross-sectional. The coefficient estimates are shown in Table 6.10. No multi-collinearity, i.e., no strong relationship between the chosen independent variables was detected. Indeed, the tolerance value for all the explanatory variables are well above 0.4, except for first and second order terms, i.e.  $\ln AGE$ ,  $(\ln AGE)^2$ ,  $\ln SIZE$  and  $(\ln SIZE)^2$ . Tolerance values for all variables are displayed in Table 6.11. The high multi-collinearity among the first and second order terms is expected and is of no consequence to the results. In fact, two of the first and second order terms are statistically significant and they are found to be helpful and included to capture non-linearity. Similarly, the model passes White's test: the  $R^2$  for the regression of  $\hat{u}_i^2$  on the size and age variables and their squares and cross products is equal to 0.1024. This value multiplied by the sample size i.e. 76 is equal to 7.7824, which has a chi-square distribution with 5 degree of freedom (df). The 5% critical chi-square value for 5 df is 11.0705 while the 10% critical value is 9.2363. Therefore, we can conclude that the observed value is insignificant and that there is no heteroscedasticity.

It is evident that the results indicate that some variables, which were statistically significant, supported the direction of influence suggested by the hypotheses. In what follows I examine in detail the results obtained for each individual variable and the findings of the analysis.

**Table 6.10 Definition of variables**

VARIABLE NAME	DEFINITION
<i>1. Dependent Variable</i>	
EMPGR	Employment Growth [ $[\ln S(t') - \ln S(t)]/\mu$ ]
<i>2. Independent Variables</i>	
<b>FIRM CHARACTERICS</b>	
In SIZE	Beginning -of-period employment [ $\ln S (t)$ ]
In AGE	Age of the firm
<i>3. Dummy Variables</i>	
<b>OWNER-MANAGER CHARACTERISTICS (O)</b>	
SEX	If owner is a male then 1; else 0
YOUNG	If owner's age is less than 31 then 1; else 0
OLD	If owner's age greater than 49 then 1; else 0
EDUC	If owner has a college diploma or above then 1; else 0
EXPRNC	If owner has previous experience in similar industry then 1; else 0
BUSPART	If owner had other employees or business partners share ownership at start-up then 1; else 0
<b>BUSINESS PRACTICES (B)</b>	
BUSDEBT	If source of financing was bank or government loans then 1; else 0
MKTSZE	If the enterprise reports that it has markets in towns other than Bahir Dar then 1; else 0

Source: Author's model specification on the basis of the Evan's model

## **A. Owner-manager characteristics**

**Age of the owner has a significant impact on growth of the venture, but level of education and gender do not.**

- The coefficient for age (YOUNG) is statistically very significant. Holding other owner and business characteristics constant, being young, i.e. less than 31 years old, affects growth performance positively. The results show that young males dominate the scene in young growing major firms. This is, in fact, not surprising for at least one reason: young males are known to be more proactive, innovative and risk taking than other parts of the adult population. However, being greater than 49 years old has no influence because its coefficient (OLD) does not reach statistical significance at 10 percent level.
- Education or having a college diploma or above (EDUC) does not have a significant impact on venture growth as far as small manufacturing enterprises are concerned. It is not statistically significant.
- No evidence was found that gender of the owner affects growth. In other words, the coefficient for gender (SEX) is not statistically significant.

**Business partnership (BUSPART) and prior paid employment experience in the same industry (EXPRNC) have no significant impact on small enterprise growth**

- The coefficient for sharing ownership with a business partner, at start up, (BUSPART) is small and not significant which suggests that it has no impact on business growth. However, it has been argued by many writers that partners at different stages of development contribute capital and moral support. They also provide complementary expertise in areas of management or other functional areas of business. But, the result obtained or the coefficient of partnership reveal that this has not been the case for small enterprises operating in the study area.

- The other factor relating to the owner's previous paid-employment experiences did not explain the growth of business. The coefficient for owner's previous experience (EXPRNC) has a positive sign, but is statistically insignificant. It is likely that this factor may contribute to the successful start-up of a small enterprise, but not necessarily to its growth, when more specific skills necessary to managing growth may be required. More specifically, it means that the experience alone without regard to the position held or the degree of relatedness to the new venture, may not be an important advantage.

## **B. Business practice characteristics**

**Both of the variables used to describe the business practices of the small enterprises had predictive power over their growth. Market size and external sources of financing (loan) have a significant impact on the growth of the enterprise.**

- The estimated coefficient for market size (MKTSIZE) is positive and statistically significant i.e. it is significant at the 5% level. The larger the size of the enterprise's market, the higher the growth of the enterprise. The finding that expanding to distant markets does positively contribute to the enterprise growth gives support to theories that suggest growth requires strategic flexibility and the ability to change market focus, which may require introducing new products or entering new markets.
- The estimated coefficient for source of financing or debt financing (BUSDEBT) is positive and statistically significant at the 1% level. Holding other factors constant, the rate of growth is higher for enterprises that use external finance in the form of Bank loan. The finding is consistent with the theory that holds more successful growing small and micro enterprises use more external sources of financing, such as financial institutions and individual investors, than do less successful firms as argued by Harabi (2003) and Papadaki and Chami (2002).

### C. Firm characteristics

**Firm's age has a significant impact on enterprise growth but size of an enterprise has no as such significant impact on the growth of the enterprise.**

- There is, in fact, consensus among many writers on the subject that there is a negative relation between enterprise growth and age of the enterprise. The partial derivative of  $(\ln \text{Growth})$  with respect to  $(\ln \text{AGE})$  is negative over the enterprises considered in the study. The coefficient for firm age  $(\ln \text{AGE})$  is significant at the 1% level. The positive sign of the coefficient for  $(\ln \text{AGE})^2$  is statistically significant, indicating that in the case of my sample, growth decreases at an increasing rate with the age of the firm which is consistent with models of firm growth.
- Similarly, firm growth theories hold that there is a negative relationship between growth and size of the firm. The partial derivative of  $(\ln \text{Growth})$  with respect to  $(\ln \text{SIZE})$  is negative over the sampled enterprises but it is statistically insignificant to explain the relationship. Like wise, the negative sign of  $(\ln \text{SIZE})^2$  does not suggest firm growth to decrease at a certain rate when the size of the firm increases which does not support the theory on the relationship between enterprise size and growth.

**Table 6.11 Coefficient Estimates**

<b>Variable</b>	<b>Parameter Estimate</b>	<b>Standard Error</b>	<b>t-values</b>	<b>Tolerance Value</b>
Constant	.447*	.143	3.134	
SEX	.071	.038	.818	.846
YOUNG	.355	.031	3.446	.596
OLD	.068	.035	.671	.611
EDUC	.018	.050	.204	.773
EXPRNC	.133	.034	1.172	.494
BUSPART	-.019	.048	-.221	.818
MKTSIZE	.198	.030	1.995	.645
BUSDEBT	.290	.036	2.648	.529
ln (AGE)	-1.771	.137	-2.715	.015
ln (SIZE)	-.305	.074	-.949	.060
[ln (AGE)] <sup>2</sup>	1.298	.029	2.253	.018
[ln (SIZE)] <sup>2</sup>	-.294	.023	-.860	.054
ln (AGE) * ln (SIZE)]	.504	.026	1.540	.054
R-Squared = .607, Adjusted R-Square = .525 and F = 7.372				

Source: Author's calculation

\*Unstandardized

## CHAPTER SEVEN

### SUMMARY, CONCLUSIONS AND POLICY IMPLICATIONS

#### 7.1 Summary and Conclusions

The aim of this paper was to understand what factors contribute to small enterprise growth in Bahir Dar Town and draw their policy implications. The research work, which is mainly based on cross sectional data collected through survey, is believed to add to our understanding of how small enterprises grow. While some of the findings support commonly held arguments, others suggest that some popular concepts regarding small business growth may need to be re-examined with a good number of enterprises or large sample size. The size of the sample in this study has obviously limited the inclusion of more variables and hypothesis that could have been tested with the given empirical model. Despite that, the analysis has enabled to draw some important findings and conclusions on the issue of small enterprises' growth determinants.

Small as well as micro enterprises are becoming an important area of emphasis for many developing countries in general and to Ethiopia in particular, primarily for its immense potentials as a source of employment. Besides, from a number of directions donor agencies and development analysts are converging in small enterprise development policy in developing countries in general.

However, the development of the small enterprise sector, which is considered to be one of the prerequisites for building strong industrial base, is constrained by diverse problems. According to the CSA's survey reports conducted on small scale manufacturing industries in major towns including Bahir Dar in 2002, the sector's performance is hindered by various structural and institutional related problems. Similarly, as it is also discussed in the other part of this paper, the major bottlenecks currently facing the small enterprises in the study area are high level of tax, shortage of working capital and credit, lack of working premises, lack of market demand and low level of competitive power.

Some of the major findings and implications of this study are some how in line with what are reported by the small enterprise operators in the study area as far as the problems of enterprise growth are concerned.

Brick and cement pipes and furniture producing enterprises deserve special support, as more than 76% of them constitute enterprises that exhibit better growth compared to the other group of small enterprises studied.

The study supports the idea that business practices, which include market size and source of financing, have strong association with growth performance of small enterprises. It follows that small enterprises entering new markets and using external sources of finance such as bank loan exhibit growth. The study found no evidence to support a common perception linking formal higher education with higher incidence of business success and growth. More specifically, the inference support the conclusion that post high school diploma level of education does not affect the growth prospect of a small enterprise. In fact, this finding refers to highest level of education completed and did not include consideration of the impact of higher level of training programmes such as university degree which in this case is reported by none of the entrepreneurs approached.

Age of the entrepreneur has been important to the success of growing small enterprises. Small enterprises operated by young owners enjoy growth but those operated by old entrepreneurs do not. The reasons that may contribute to low growth performances of enterprises owned by old entrepreneurs compared to those operated by young owners is that as it is argued in many literatures old owners are risk averters than takers compared to young people and as a result they are less concerned about growth but survival. However, the findings suggest that women are just as successful as men are and there is no exceptional factor that could be assigned to females as far as low performance in small firms' growth is concerned.

Sharing ownership with business partners does not seem important for small enterprise growth. This might lead to the conclusion that individual or sole ownership in contrast to joint ownership (partnership) at business start-up could be attached to growing enterprises although it has to be confirmed through further investigation. The finding rather seem to support to the

belief held by many small business owners that it is their ability to maintain control of all business functions that allow the success of their business.

Enterprise size, though its coefficient is negative, did not prove to be significant to explain its negative relation with firm growth as opposed to findings of other studies in the literature. However, the other factor of firm characteristic i.e. firm age, was proved significant. That is age of an enterprise has a negative impact on its growth probability.

The fact that many of the effects of owner-manager characteristics are weak and offer limited explanatory power compared to business practices means that efforts directed towards the promotion and development of markets and access to finance and also other firm-related activities for small enterprises can overcome most of these effects and help find opportunities to achieve growth.

## **7.2 Policy Implications**

The above conclusions lead us to draw the following policy implications. The findings are important in that they have relevance to the development of the sector and are capable of suggesting policy measures. Hence, if confirmed by further analysis, the results have important policy implications and meanings for both small business owners and policymakers working in the study areas.

- ♦ Policy makers have a role in dispelling the myth, particularly among finance or credit providers (mainly banks), that small enterprises in general and women owners in particular are high-risk borrowers of capital. However, it is clear that according to the findings of this study, it should not necessarily follow a recommendation that special strategy targeting female operators has to be sought for as far as small enterprises are concerned. However, this doesn't imply that women are actively involved as operators (only 13.2 percent) in the small enterprise sector. Hence, measures directed toward encouraging women's participation in the sector (women-owned enterprises start-up) need to be strengthened in order to enable them make economic contribution through employment and entrepreneurship.

- ♦ The findings also call for public policies such as the youth employment strategy, which among others encourages the young entrepreneurship in small enterprises, as they are proved to be growth-oriented in their business performance.
  
- ♦ Market size proved to be one of the important growth determinants of small enterprises in the study area. Due emphasis need to be given to establishing strong system of market information and research. In this regard, institutional support will be crucial. Also, small enterprise owners need to look for means and ways by which they can expand their market size, for instance, through product diversification and entering new market places.
  
- ♦ Blanket policy approaches to small enterprise growth may not be effective. Policies targeted at small enterprises that are willing to take risk and able to grow are preferable. Accordingly, the administrative and regulatory framework has to be designed in such a way that it is more responsive to the needs of firms which are willing and able to grow.
  
- ♦ Government policy measure has to include provision of easy access to financing at low cost. Other organized sources of finance particularly targeting small enterprise need to be put in place to enable urban-based small enterprises to have access to commercial finance for their working capital and long-term investment requirements, if growth of small enterprises is sought for. The problem is key and the model result is also further substantiated by the fact that, as indicated in the discussion in chapter six, low access to credit and working capital has been one of the major problems encountered by the small enterprises. A guarantee schemes to support small-sized enterprises who can not meet bank and financial collateral requirements can be considered. This mechanism has been proved to be effective in some developing countries.
  
- ♦ As it has been outlined in the small enterprise development strategy, the support framework include a series of support programmes to help micro and small enterprises overcome the specific commercial obstacles they face and exploit available opportunities effectively. However, regular evaluations of the support institutions and

programmes should be carried out to ensure their continued relevance and effectiveness so that the supports could be provided in line with the needs of the target enterprises. This is because as it is explained in chapter 6, almost all of the operators of the enterprises surveyed reported that they can't witness any support that has been provided to them.

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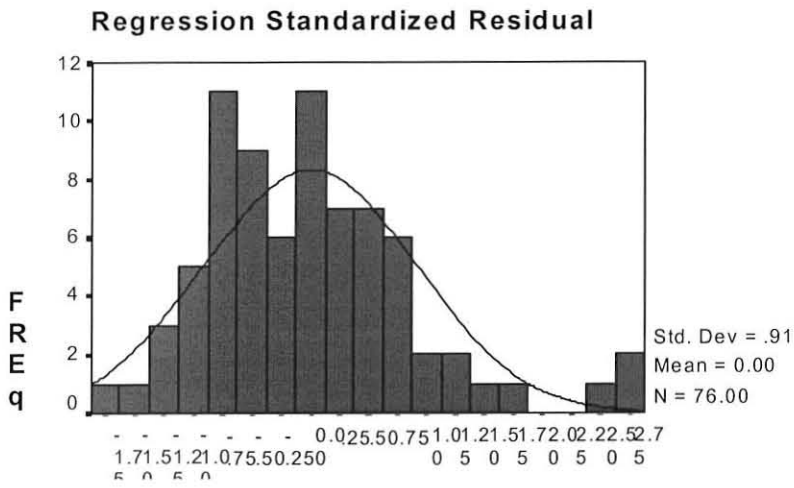
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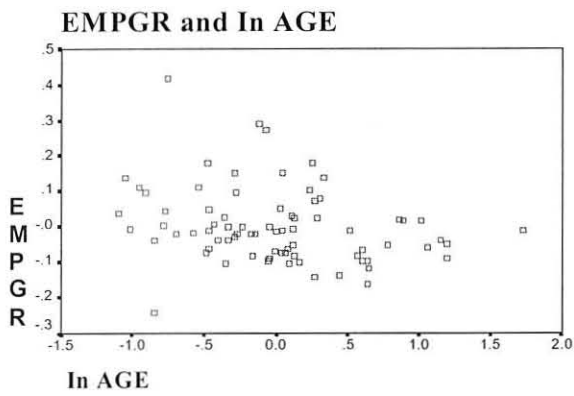
# APPENDICES

## Appendix 1: Partial Regression Plots

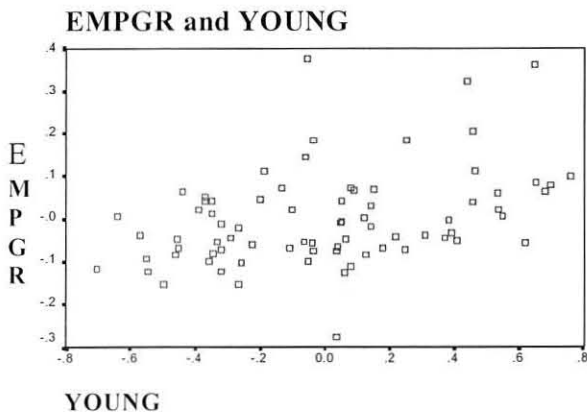
Histogram 1.1



Partial Regression Plot -1

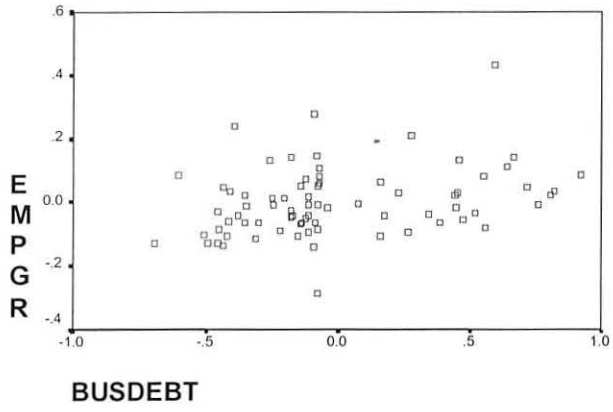


Partial Regression Plot -2



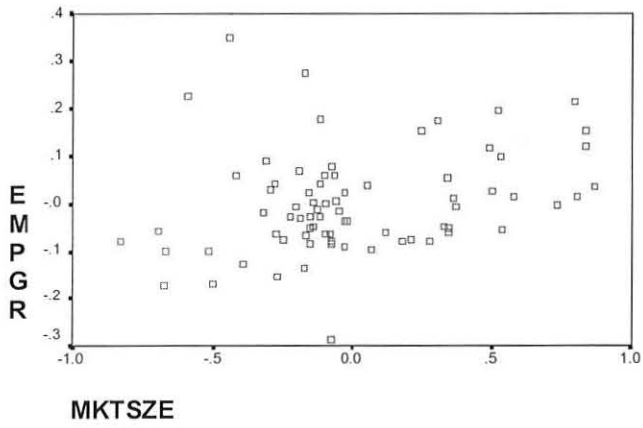
### Partial Regression Plot -3

EMPGR and BUSDEBT



### Partial Regression Plot -4

EMPGR and MKTSZE



## Appendix 2: Survey Questionnaire

### Determinants of enterprise growth: the case of small manufacturing enterprises in Bahir Dar

Date: \_\_\_\_\_

Name of the Firm: \_\_\_\_\_

Woreda: \_\_\_\_\_ Kebele: \_\_\_\_\_

Respondent's Number/Code: \_\_\_\_\_

Interviewer's Name: \_\_\_\_\_

#### A. Operator's characteristics

1. Sex (put a "✓" mark) male \_\_\_\_\_ Female \_\_\_\_\_
2. Age: \_\_\_\_\_
3. Marital status (please circle one among the choices)  
1) Married 2) Divorced 3) Widow (widower) 4) Bachelor
4. Level of education (in grade):  
1) 1-4 2) 5-8 3) 9-12 4) 12+1 5) 12+2 (diploma) 6) First degree  
7) Other (Specify) \_\_\_\_\_
5. If diploma and above, please mention your field of study \_\_\_\_\_
6. What other major training courses have you taken and when, if any?  
\_\_\_\_\_  
\_\_\_\_\_
7. What was your occupation before engaging your self in this enterprise? \_\_\_\_\_  
\_\_\_\_\_
8. Have the experiences and skills acquired from previous employment contributed to your current career? 1) Yes 2) No
9. Is there any one in the family who was entrepreneur or owner of some related business activities? 1) Yes 2) No
10. If yes, what is your family relation with him/her?  
1) Father 2) Mother 3) Brother 4) Sister 5) Grandfather  
6) Grandmother 7) Husband/Wife 8) Other (specify) \_\_\_\_\_

11. Have you ever lived abroad? 1) Yes            2) No
12. If yes, for how long and where? \_\_\_\_\_
13. Why did you choose your current business? Because,
- 1) I have got the experience            2) I have enough money to run it
- 3) I saw prospects for growth            4) Other
14. Who initialed and started the business?
- 1) My self alone            2) With the family
- 3) With a friend/partner            4) other (specify) \_\_\_\_\_
15. How did you acquire the skill for running your enterprise?
- 1) Through formal training            2) From past experience
- 3) From family            4) other (specify) \_\_\_\_\_
16. What preparatory works did you undertake before starting the enterprise?
- 1) Assessed the market (market survey)    2) Got the project studied
- 3) Taken formal training            4) Got the enterprise registered
- 5) No any
17. Is the owner at the same time the manager of the establishment? 1) Yes    2) No
18. If No, or if the manager is different from the owner; what is his/her level of education? \_\_\_\_\_
19. What is his/her field of study (if he/she is a graduate) \_\_\_\_\_
20. What is the age of the Manager? \_\_\_\_\_
21. Sex of the manager: Male \_\_\_\_\_ Female \_\_\_\_\_
22. When was the manager hired? \_\_\_\_\_

## **B. Firm Characteristics**

23. When did the enterprise start operation? (Specify year) \_\_\_\_\_
24. How much was the capital of the firm at the start up? \_\_\_\_\_
25. What were the main products of the enterprise at the beginning? \_\_\_\_\_
- \_\_\_\_\_
26. Are the current products different? 1) Yes    2) No
27. If yes, in what respects are the products different?
- 1) Products diversified

- 2) The quality of the products up graded
- 3) The products (out puts) totally changed
- 4) The method of production markedly changed
- 5) Other changes
- 6) Variety reduced

28. Currently what are the main products of the enterprise? \_\_\_\_\_

29. Is the enterprise registered? 1) Yes 2) No

30. If yes, when did the enterprise get registered? \_\_\_\_\_

31. What is the legal ownership status of the establishment?

- 1) Sole ownership
- 2) Joint ownership
- 3) Family business
- 4) Cooperative
- 5) Other (specify) \_\_\_\_\_

32. What was the status of the machinery at the start-up?

- 1) Manual and old
- 2) Manual and new
- 3) Mechanical and old
- 4) Mechanical and new
- 5) Mixed type
- 6) other (specify) \_\_\_\_\_

33. How was the machinery obtained?

- 1) Gift
- 2) Bought using my own saving
- 3) Bought through borrowing
- 4) Male (modified) at home
- 5) Bought with partner contribution
- 6) Other (specify) \_\_\_\_\_

34. When did you buy major piece of equipment? \_\_\_\_\_

35. Why did you buy it?

- 1) To replace obsolete equipment
- 2) To expand production of existing product
- 3) To introduce a new line of production

36. What number of employees did you start out with? \_\_\_\_\_

How many employees did your firm have in 2002? \_\_\_\_\_

37. Currently, how many permanent employees does the enterprise have? \_\_\_\_\_

38. What are the reasons for the decrease/increase in the number of permanent employees \_\_\_\_\_  
\_\_\_\_\_
39. Does the enterprise employ casual workers? 1) Yes      2) No
40. If yes, how many are they at a moment (considering very recent occasions)? \_\_\_\_\_  
\_\_\_\_\_
41. Currently, do you have a family member employed in the enterprise?
- 1) Not at all
  - 2) Yes, but without payment/salary
  - 3) Yes, with payment/salary
  - 4) Yes, but some are paid and some others are not
42. How many family members are employed?
- 1) With payment \_\_\_\_\_
  - 2) With out payment \_\_\_\_\_
43. What are the negative (positive) aspects of having family members as employees in the enterprise? \_\_\_\_\_  
\_\_\_\_\_
44. Sex composition of the present employees  
Male \_\_\_\_\_      Female \_\_\_\_\_
45. What is the level of education of the employees (excluding the manager)?
- 1) 1-4 \_\_\_\_\_      2) 5-8 \_\_\_\_\_      3) 9-12 \_\_\_\_\_      4) 12+1 \_\_\_\_\_
  - 5) 12+2 \_\_\_\_\_      6) First degree
46. What is the average age of the employees? \_\_\_\_\_
47. What are the sources of initial capital at the start of the business?
- 1) Own saving
  - 2) Borrowing from relatives
  - 3) Borrowing from bank
  - 4) Borrowing from credit and saving institutions
  - 5) Gift from relatives
  - 6) Joint investment with a partner
  - 7) Other (specify) \_\_\_\_\_











## Declaration

The Thesis is my original work and has not been presented for a Degree in any other University and that all the sources of materials used for the Thesis have been dully acknowledged.

Name: Endeshaw Mulatu H/Wold

Signature: \_\_\_\_\_

Date: \_\_\_\_\_

Confirmed by the Advisor:

Name: Dr. Farida Siddiqui

Signature: \_\_\_\_\_

Date: \_\_\_\_\_ 12.7.05