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*Assessing Institutional Frameworks Contributing to Entrepreneurship
Development: The Case of Selected Woredas of Kolfe Keraniyo, Lideta
and Gulelle Sub Cities*

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This is to certify that the thesis prepared by Tigiste Deresse Gebre entitled “Assessing Institutional Frameworks Contributing to Entrepreneurship Development: The case of selected woredas of Kolfe Keraniyo, Lideta and Gulelle sub cities”, which is submitted in partial fulfillment of the requirements for the Degree of Public Management and Policy (MPMP), complies with the regulations of the University and meets the accepted standards with respect to standards to originality and quality.

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Abstract

This study is concerned with assessing the institutional framework that can develop entrepreneurship with taking three sub cities of Addis Ababa namely Kolfe Keraniyo, Lideta and Gullele as a case. The study is geared towards answering key questions related to policies and strategies in place to facilitate and encourage entrepreneurial activities among Micro and Small enterprises, assistance provided by Woredas' SME development bureaus responsive to the needs of the enterprises, the linkage and coordination among Woredas' SME development bureaus and other government and non-government institutions involved in entrepreneurship development process and problems related to the Woredas' SMEs' development bureaus' institutional framework that entrepreneurs are operating under and has made endeavors on identifying the major problems of the current institutional environment. Data have been collected from 100 respondent enterprises and also interviews were conducted with FeMSEDA officials and the Woreda officials operating under the selected sub cities. The policies, strategies and procedures of entrepreneurship development in the country have been reviewed. Data analysis revealed significant differences in the needs of the entrepreneur and the encouragement of the Agency in the success of the enterprises. The study findings have revealed that though the strategy and procedures indeed encourage small firms, the institutional framework and way of implementation still need to be improved to promote entrepreneurship.

Key words: Institutional Framework, Entrepreneurship, Federal Micro and Small Enterprise Development Agency

Definitions of Important Terms and Concepts

Certain terms in this research have been defined by different authors in various ways and have different interpretations that can lead to confusion. So it is best to clearly define the terms and to put their appropriate meaning in the context of this research.

Institution - are commonly defined as „rules, norms, and beliefs that describe reality for the organization, explaining what is and is not, what can be acted upon and what cannot (Hoffman, 1999).

Institutional Framework – is generally understood to mean the systems of formal laws, regulations, and procedures, and informal conventions, customs and norms that broaden, mold and restrain socio-economic activity and behavior (Donnellan, Hanrahan, & Hennessy, 2012). In this research only the formal institutions are reviewed.

Entrepreneurship - different scholars have different perspectives towards this concept. *Richard Cantillon* states that entrepreneurship is considered as a self-employment of any sort i.e. buying at a certain price and selling it at uncertain price in the future. *Jean Baptiste* another author in the field defined entrepreneurship as combination of inputs to produce output or simply production is considered as entrepreneurship. The third definition by *Joseph Schumpeter* relates entrepreneurship with innovation i.e. introduction of new or improved products. In this research we follow more of the definition given by the first scholar.

Micro and Small Enterprise

The revised SME strategy provides a separate definition for micro and small enterprises based on the number of members and the capital accumulation.

Micro Enterprises - are enterprises engaged in the industry sector which operate with 5 or less persons under them and their total asset is not exceeding Birr 100,000. Whereas, enterprises engaged in service delivery sector are those with 5 or less persons working under them and with a total asset of Birr 50,000 or less.

Small Enterprises - are enterprises engaged in the industry sector which operate with 6 to 30 persons under them and their total asset is ranging between Birr 100,000 and Birr 1.5 million. Whereas, enterprises engaged in service delivery sector are those with 6 to 30 persons working under them and with a total of paid up capital ranging between Birr 50,001 to Birr 500,000.

Chapter 1

1 Introduction

1.1 Background

Entrepreneurship is widely acknowledged as a channel for poverty reduction and economic development. Studies show that new firms and Small and Medium Enterprises (SMEs) play an increasing role as drivers of growth and job creation in an economy. However, the growth of these enterprises depends on their innovation capacity and engagement in an entrepreneurial act. To fulfill their potential for job creation and long run growth, governments must ensure an institutional environment that stimulates entrepreneurship, encourages innovative SMEs and sets structural policies addressing financing, access to markets and knowledge networks, the management of intellectual assets and entrepreneurial human capital. (Alvarez & Barney, 2008)

Recognizing the role of SMEs on the socio-economic development of the country, the Ethiopian government, has given due attention to strengthen SMEs and took measure for the development of the sector. Accordingly, it has re-structured and re-established what is known to be FeMSEDA (the Federal Micro and Small Enterprises Development Agency) in 2006. This Agency has a mission to facilitate economic growth and lay foundation for industrial development through providing direct and indirect support for SMEs all over the country.

Nonetheless, despite the efforts directed towards developing SMEs, there is still a lot to be done regarding the institutional framework under which these enterprises are operating. In the context of this study, such conditions entail capability (Skills and business knowledge), financial services, market availability and government policies.

This study focuses on policy and support schemes adopted by government to develop SMEs and how entrepreneurship can be enhanced in SMEs through improved institutional environment.

1.2 Statement of the Problem

Entrepreneurship is viewed as critical to a nation's economic growth and development since it creates both employment and wealth for the country. There is a strong linkage among SMEs,

innovation and entrepreneurship; the development of one can influence the growth and expansion of the other. However, innovation and the role of entrepreneurship in development are neglected subjects in Ethiopia. Government policies and support schemes only focus on facilitation of mere establishment of SMEs and didn't embrace the concept of making them centers for innovation and entrepreneurial ventures. Individuals and groups with innovative business ideas are not empowered to start small businesses. Support for business research and development activities is also negligible and confined to universities and research centers. Nonetheless, in order for small business to exist and be successful in gaining local, regional and international market share, be profitable and contribute to the nation's development, they have to accompany new innovative products and services and also add new values on existing products. (Shane & Eckhardt, 2003)

One probable reason for the constrained entrepreneurship development is lack of conducive and well-designed institutional framework. Enabling institutional framework for small business and individuals unleash their innovative potential to contribute to the nation's development. Therefore, this research analyses the formal institutional frameworks affecting entrepreneurship development. The strategy designed for SMEs' development and the services and assistances rendered to these enterprises are also identified and reviewed. Linkages among key participants in the entrepreneurship process were studied. Finally recommendations and suggestions are given on ways to improve entrepreneurship development process.

1.3 Research Questions

This research will try to answer the following basic questions:

1. What policies and strategies are in place to facilitate and encourage entrepreneurial activities among Micro and Small enterprises?
2. Is the assistance provided by Woredas' SME development bureaus responsive to the needs of the enterprises?
3. Is there a strong linkage and coordination among Woredas' SME development bureaus and other government and non-government institutions involved in entrepreneurship development process?
4. What are the problems, if any, with the Woredas' SME development bureaus institutional framework that entrepreneurs' are operating under?

5. What should be done to improve Woredas' SME development bureaus institutional framework in order for entrepreneurs to function efficiently?

1.4 Objectives

The main objective of this study is to analyze the institutional framework affecting entrepreneurship development by identifying the works of the selected Woredas of the sub cities under studied. The research has also a purpose of identifying the major institutional problems and challenges in development entrepreneurship and generating recommendations which can be applied to improve the existing conditions.

More specifically the study is to:

1. Identify and review policies and strategies in place to facilitate and encourage entrepreneurship among Micro and Small Enterprises.
2. Evaluate if the assistances provided by Woredas' SME development bureaus are responsive to the needs of entrepreneurs.
3. Study the linkage of Woredas' SME development bureaus and other government and non-government institutions involved in entrepreneurship development process.
4. Identify problems, if any, with the Woredas' SME development bureaus institutional framework that entrepreneurs' are operating under.
5. Recommend on how to improve Woredas' SME development bureaus institutional framework in order for entrepreneurs to function efficiently.

1.5 Significance of the Study

The study will be important for improving the literature in the field and practice of using institutional approach to entrepreneurship in Ethiopia. Since abundant empirical literature regarding Ethiopia's institutional environment and entrepreneurship are rarely present, this research can contribute to broaden the knowledge in the field. It can also serve as a spring board for other researchers interested in this area for further investigation and detailed analysis.

This paper has also important implications for public policy and for the design and implementation of programs to develop entrepreneurship. Generally, the primary role of the government and other agencies is to increase opportunities, to develop the motivation of potential entrepreneurs to go into business, and to enhance potential entrepreneurs' ability to start a

business. Hence this research may be significant for the government institutions to identify weak areas and then formulate policies and programs to strengthen the weaker areas regarding entrepreneurship development.

1.6 Methodology

A. Research Design

A combination of quantitative and qualitative methods was used in this study by utilizing a two phase design approach. The qualitative method was used to investigate the supply side of the institutional framework by giving due emphasis on the works of Woredas“ SMEs“ development bureaus of Lideta, Kofe Keraniyo and Gullele sub cities. Since these are the most important institutions which are involved in SME assistance, more in-depth information could be obtained using this method. Besides, the Policies, Procedures and Programs developed towards entrepreneurship will be examined using this method. The demand side of the institutional framework was studied using the responses of entrepreneurial individuals and enterprises that operate within the institutional environment. Due to the size of the population, for studying the demand side of the institutional framework quantitative method, in particular, the survey method is the most economical and efficient one.

B. Population and Sample

In research there are two groups of population – the target Population and the accessible or survey population. The target population is the entire group of people or objects to which the researcher wishes to generalize the study findings. Whereas the accessible population is the portion of the population to which the researcher has reasonable access; may be a subset of the target population (Hubbard). In this study the target population is considered to be entrepreneurial enterprises and individual all over the country. However, certain elements of the target population are difficult to reach or exhaustively know like individuals that are not organized in an officially known organization but are striving to bring new business into the market. Besides, it is hard for a single researcher to cover all the population under the study. Therefore, among other institute and centers involved in entrepreneurial activity Small and Micro Enterprises (SME) in Kolfe Keraniyo, Lideta and Gullele sub cities are taken to be the accessible or survey population from which the sample frame is designed and samples are taken. This is

because; most business in the country is under these enterprises and also can give a better insight on the procedures of startup businesses and creation of a new venture.

The survey population is all enterprises engaged in micro and small businesses of manufacturing and construction sectors in Lideta, Kolfe Keraniyo and Gulelle sub cities. These sub cities are selected as a case because of the degree of the density of SMEs population compared to other areas. Stratified sampling was used to group the population into manufacturing and construction. Then simple random sampling was used to select samples from the population in each group. The manufacturing and construction sectors are selected since these sectors are major focus areas of government to develop the nation through SMEs.

This list of population was generated using the 2013 list of establishments from the FeMSEDA’s database. Out of the survey population 100 SMEs are included in the sample using simple random sampling. 30 of the samples are from the construction sector and the rest are from the manufacturing sector. The samples from the manufacturing sector are divided into 5 categories or sub sectors which the government has given due focus to.

Table 1 Distribution of Sample According to Industry Sector

| <i>Industry Sector</i> | <i>Distributed</i> |
|------------------------|--------------------|
| Construction | 30 |
| Manufacturing | |
| Textile & Garment | 14 |
| Metal & Wood Works | 14 |
| Leather Products | 14 |
| Shoe Making | 14 |
| Food Processing | 14 |
| Total | 100 |

C. Data Collection and Analysis

Data for this research were collected using both primary and secondary sources. As primary sources of information semi structured interviews were held with FeMSEDA’s and Woreda representatives to know the support system and the overall framework. The representatives were selected by their degree of affiliation to the subject under study and are employees working under the major departments performing the job related to SME s development. Questionnaires were distributed to the sampled enterprises through data collectors to be acquainted with their perceptions towards the institutional environment they are operating in. The nation’s Policies and

Strategies developed have also served as a source of data. Secondary data were collected from books, brochures, pamphlets, reports, magazines and other publications and databases. The data collected through interviews were analyzed qualitatively using descriptive method. The questionnaires collected were also analyzed using simple statistical tools i.e. Percentages.

Chapter 2

2 Literature Review

2.1 Entrepreneurship – concept and theories

There are several perspectives and school of thoughts on the concept and theories of entrepreneurship. Many associate entrepreneurship with innovation and the development of new product, technique, service, or business model. This school of thought defines entrepreneurship based as offering something new or a new way of doing things for the betterment of mankind and making profit in the process. However, others define entrepreneurship from the perspective of identifying needs and turning them into opportunities by providing solutions.

According to Rae, (2007) this could be a gap in the market, a future possibility, a more effective or efficient process/product or an innovation for the future. This view perhaps has a more encompassing perspective of entrepreneurship because it identifies efforts of many in emerging economies that provide essential product and services that are not necessarily new. It should be noted however, that every new business venture that starts – big or small are necessarily not the result of entrepreneurship. Entrepreneurship should fundamentally represent bringing about change that is driven by the identification of opportunities Drucker, (2007), although it might result in new venture or business (Hodgson, 2006).

Whilst many differ on the outcome of entrepreneurship, one area that most seem to agree on is that entrepreneurship is a process. Kaplan & Warren, (2010), describe it as “*the process of planning, organizing, operating and assuming the risk of a business venture*”. Entrepreneurship is a behavioral phenomenon by looking at it as identifying and taking advantage of opportunity without being limited by the availability of resource or non-availability thereof. Thus, one could look at entrepreneurship not only as a process, but also at the entrepreneur’s unique approach in creating, managing a venture, managing risks, mobilizing and effectively deploying resources. Furthermore, this view could imply a behavioral pattern of the entrepreneur that identifies and acts on opportunities despite all odds by taking a step further than what others would have done, perhaps by combining innovation (Rae, 2007). One could

therefore argue that might a convergent of the different perspectives on entrepreneurship when the entrepreneur is considered (Ramsey & Amenta, 2010).

2.2 The Entrepreneur

Going by the aforementioned that entrepreneurship is more a behavioral pattern than a personality trait. Empirical research has shown that there is no significant personality difference between successful entrepreneurs and successful managers who are non-entrepreneurs, but the study identified behavioral pattern where they differ significantly (Dyer, Gregersen, & Christensen, 2008). It thus means that entrepreneurship can be learned by developing the right characteristics or induced by proving the right environment. In a study of how and what makes people become entrepreneurs, Farrington, Venter, & Neethling, (2012) suggest that the attributes of an entrepreneur can be developed through education, thereby promoting intentions that produce entrepreneurs. However, it is important to note that the class room education alone might not be enough to be successful as an entrepreneur in the real business environment (Rae, 2007).

Based on the review of literature, the description of an entrepreneur as one that identifies, creates and acts on opportunities or the one that innovates can be traced to identified pattern of behavior in entrepreneurs. Some of the behaviors identified include strong problem solving ability, a strong desire for achievement, flexibility, creativity and independence (Rae, 2007). Others include high tolerance of risk, leadership, ability to deal with ambiguity, ability to execute and they know how to build and maintain the right relationships (Kaplan & Warren, 2010).

2.3 The Origins of Entrepreneurial Opportunities

Entrepreneurship occurs when an individual acts to take advantage of a profit opportunity that presents itself in the economy. In its simplest form, the entrepreneur might notice that one person is willing to sell something for less than someone else is willing to pay for it, so the entrepreneur can act as a middle man, profiting from buying at the lower price and selling for more. The profit, which is the return to the entrepreneur's alertness to the opportunity, was created entirely by the entrepreneur's activity, because the sale would not have taken place without someone having noticed the profit opportunity (Boaz, 2003). The entrepreneur's activity benefits the buyer, the

seller, and more generally, the entire economy. Furthermore, the entrepreneur's profit signals potential suppliers and demanders about their market opportunities, and even signals other potential middlemen of the profit opportunity for facilitating exchanges. Eventually the ability to earn above-normal profits will be competed away, but only after those profits have served their role in signaling a way in which resources could be more efficiently allocated in the economy. Entrepreneurship is indispensable for economic progress, but entrepreneurial activity is possible only when profit opportunities are available to the entrepreneur. The entrepreneurial process is often more complex than simply having an entrepreneur notice that something can be purchased from one party and sold at a profit to another. Two complicating factors are production and time. For example, the entrepreneur might conjecture that if several inputs are purchased today and combined in a production process that occurs over time to produce some new output, that output could be sold in the future for more than it costs to purchase the inputs today. Yet these complexities do not alter the fundamental nature of entrepreneurship. While entrepreneurial opportunities are more difficult to spot when they involve production and time, and while they also involve some uncertainty about the outcome, the essential entrepreneurial act is still the noticing and acting upon a profit opportunity. Kirzner, (1973) has emphasized the role of entrepreneurship in equilibrating an economy and leading to a more efficient allocation of resources, but Kirzner's model of entrepreneurship has focused on the behavior of entrepreneurs in response to profit opportunities. This paper discusses where those profit opportunities originate, thus making Kirzner's model of entrepreneurship more complete.

If one views the economy as tending toward equilibrium, and accepts Kirzner's entrepreneurs as the economic agents who act on profit opportunities that exist in disequilibrium in order to equilibrate the economy, then eventually all of those profit opportunities will be competed away, and the economy will remain in equilibrium. What produces the profit opportunities to begin with? Three major categories of factors that create profit opportunities are identified: (1) Factors that disequilibrate the market; (2) Factors that enhance production possibilities; and (3) Entrepreneurial activity that creates additional entrepreneurial possibilities. An analysis of each of these categories leads to the conclusion that by far the most significant cause of entrepreneurial opportunities is prior entrepreneurial activity. Entrepreneurship creates the opportunity for more entrepreneurship, which leads to economic progress. Entrepreneurship provides an important equilibrating function, but also is the crucial element in economic growth.

After discussing the theoretical relationship between entrepreneurship and economic growth, the paper considers the institutional framework that is most conducive to entrepreneurship and growth (Holcombe, 2003).

2.4 Entrepreneurship in Economic Models

Paradoxically, while entrepreneurship has been becoming an increasingly important part of the economy in the twentieth century, it has been becoming increasingly less important as a part of economic theory. Entrepreneurship occurs when an individual notices and acts on a profit opportunity, but in the equilibrium models that dominate economics at the end of the twentieth century; all profit opportunities have already been exploited, meaning that there is no role for entrepreneurship in this type of model. To capture the role of entrepreneurship, economists must focus their attention on the process that leads individuals to seek profit opportunities, rather than on a state of equilibrium in which, by assumption, no profit opportunities exist. The benefits of studying the process by which economies adjust while moving toward equilibrium should be obvious, because even the staunchest equilibrium theorist will agree that while economic forces always pull the economy toward an equilibrium, equilibrium is a moving target that the economy always approaches but never reaches. It makes sense, then, to devote attention to the process that always is occurring, rather than focusing exclusively on the result that never occurs (Boaz, 2003). In contrast to the economic mainstream, (Kirzner, 1973) has consistently focused his attention on the role of entrepreneurship in the equilibrating process. Kirzner has focused mainly on the equilibrating role of entrepreneurial action, but the central role of equilibrium to Kirzner's vision of entrepreneurship indicates that the concept of equilibrium is important to understanding the concept of entrepreneurship. In a perfectly competitive economy in a condition of equilibrium, there are no above-normal profits that can be exploited, and there are no entrepreneurial activities occurring. There is still a role for good management in equilibrium, to ensure that firms are combining their inputs at lowest cost to produce their outputs, but this management, as depicted in models such as those by Coase, (1937) and Alchian & Demsetz, (1972), is not entrepreneurship. Entrepreneurship occurs when individuals act upon previously unnoticed profit opportunities, whereas management works to make the production process as efficient as possible by maximizing the amount of output that is produced by a given level of input. Note that in equilibrium there is no entrepreneurial activity, but management is still necessary to prevent

shirking and other forms of resource waste.

By studying the characteristics of markets and economies in equilibrium, economists forego the opportunity to examine the nature of the equilibrating forces that lead toward equilibrium, and it is this emphasis on equilibrium concepts that has pushed entrepreneurship out of most economic models. Yet entrepreneurial activity, which is often assumed away in order to focus on the nature of equilibrium, is the force that drives the economy to allocate resources efficiently and to increase its productivity over time. Thus, an examination of the origins of entrepreneurial opportunities is not just a digression into an unimportant detail, but rather is aimed at understanding one of the most important activities in an economy (Henisz, 2000).

2.5 Entrepreneurship and Knowledge

One of the assumptions underlying the neoclassical model of perfect competition is that everyone in the economy has perfect knowledge about all economic opportunities. This assumption rules out the possibility that any unrecognized profit opportunities could exist in the economy, but also points toward the perfect knowledge assumption as the key assumption to relax if one is trying to understand the origins of entrepreneurial opportunities.

Superficially, it might appear that the production and dissemination of knowledge by itself will produce more of the entrepreneurship that will equilibrate the economy, and while an increase in knowledge will help foster entrepreneurship, the production of knowledge is not by itself an entrepreneurial undertaking. This might appear obvious when stated so plainly, but the new classical models of economic growth, such as those by Lucas (1988) and Romer (1990) cited in Holcombe, (2003), emphasize the importance of human capital and the production of technological advances in their growth models, without capturing at all the role of entrepreneurship. When entrepreneurial opportunities arise, they are not plainly visible for all to see. Rather, as Hayek (1945, 1949) cited in Holcombe, (2003) has suggested, all individuals have some knowledge specific to time and place that is not available to others. In many cases, that knowledge is not easily transferable to others. It may be the ability to recognize certain patterns in market behavior a simple example would be seasonal patterns, subtle differences in quality of goods, or ways to identify whether resources are being used efficiently. Such knowledge might be acquired by experience, and may be difficult to articulate to others. Thus, certain entrepreneurial opportunities will be more available to some people, while a different set of

opportunities will be more available to others. Because the ability to recognize an opportunity will often come only from some specific knowledge of time and place, perfect knowledge, in the sense assumed in the neoclassical model of perfect competition, will never exist. (Kirzner, 1973), depicts entrepreneurial insight as the recognition of a profit opportunity that was previously unnoticed, and as such, does not require, or even involve, any outlay of resources on the part of the entrepreneur. In this way, entrepreneurial opportunities are differentiated from mere information, which people can and do seek out. Yet, as Harper, (1996) explains, it is possible for people to invest in activities that create a more fertile environment for observing entrepreneurial opportunities. Seeking information, investing in human capital, and systematically searching through promising ideas are not entrepreneurial acts in themselves, as Kirzner defines entrepreneurship, but they can create an environment where entrepreneurial insights are more likely to be generated. Similarly, as Holcombe, (2003) explains, research and development activity is not entrepreneurship. But such investment in the advancement of knowledge can create an environment in which entrepreneurial opportunities are more likely to be generated. Furthermore, knowledge is necessary for the entrepreneur to recognize an entrepreneurial opportunity when one appears. There is a direct connection between entrepreneurship and knowledge.

When one looks at the entrepreneurship that occurs in high-tech areas such as medical care, pharmaceuticals, and electronics, it is apparent that entrepreneurial insights are more likely to come to individuals who have an intimate knowledge of the area. It is unlikely that a baker will stumble across a better method for etching circuits in electronic devices, or that an auto mechanic will discover a more effective medication for lowering cholesterol. Of course, the baker and the auto mechanic have their own specific knowledge of time and place, but the point of picking high-tech examples is to illustrate that while entrepreneurship is not directly produced by knowledge, knowledge is a key ingredient in the production of entrepreneurial insights. Without knowledge, how could one recognize whether the opportunity to take some action was likely to result in profit? Furthermore, Harper, (1996) notes that marketing research can aid entrepreneurs in identifying the most promising ideas, and tailoring their offerings to more closely fit the actual entrepreneurial opportunity. Henry Ford seized a very profitable opportunity when he began mass-producing automobiles at a cost much less than the other available alternatives, but missed

the chance to maintain his lead by not seeing the market for new models and more options for his cars.

Innovation and technological advance are not entrepreneurship. For example, most of the innovations introduced to the market on Macintosh computers, and that later migrated to Microsoft's Windows environment, including the use of on-screen windows and the computer mouse, were developed by Xerox, but the company that produced the innovation failed to capitalize on the entrepreneurial opportunity. At the time that Xerox developed this technology, no other entrepreneur had the opportunity to use it, because nobody else knew about it. However, apparently lacking the entrepreneurial insight, Xerox failed to capitalize on the entrepreneurial opportunity that only it had, and instead revealed the idea, leading to other entrepreneurs making use of it. In this case, it is easy to separate the innovation and technological advance from the entrepreneurship.

This example illustrates that entrepreneurial opportunities can be divided into two categories. Some opportunities might arise as a result of the innovative activity of the potential entrepreneur, making the innovator the only one who is in a position to observe the existence of the opportunity. The people at Xerox could have, had they been more entrepreneurial, recognized that they had a good idea for a computer interface, and brought a product to market (or sold the idea to another company). As the innovator, they had the first chance to seize the entrepreneurial opportunity from their innovation. Other opportunities arise because people see that the market offers an entrepreneurial opportunity, perhaps as simple as buying something cheaply in one location and selling for more elsewhere, or perhaps as complex as buying inputs, combining them in a new manufacturing process, and selling a new product for a profit. The first type of opportunity is open only to the innovator, because nobody else is in a position to observe the innovation, whereas the second type of opportunity is open to anyone, because it relies only on seeing an unexploited market using generally available information.

Entrepreneurship, as described by (Kirzner, 1973) is more in the spirit of the second type of activity. For it to take place, however, there must be a market in which the profit opportunity can be realized. The first type of entrepreneurship, resulting from innovation undertaken as a private activity, also depends on a market. Partly, this is because the innovation cannot be capitalized upon without a market (in the case of Xerox, they did not even recognize the market value of

their innovation, but others did), and partly this is because there is little incentive to invest in innovative activity unless, eventually, there is a way for the activity to generate a return to finance it. Thus, (Harper, 1996) emphasizes the close connection between the advance of knowledge and the production of entrepreneurial activity, and emphasizes that when entrepreneurship can be profitable, people have the incentive to invest in the advance of knowledge, which eventually can produce a payoff if it produces entrepreneurial opportunities. The production of knowledge is not entrepreneurship, but the two are closely linked (Boaz, 2003).

2.6 The Origin of Entrepreneurial Opportunities

The information needed to seize some entrepreneurial opportunities comes from sources available in principle to everyone, although recognizing that information that a person acquires constitutes an entrepreneurial opportunity may also require some specific knowledge of time and place. For example, Ray Kroc turned MacDonald's into a global fast food empire by buying an existing restaurant started by someone else, and recognizing its potential, expanding into new markets. Many people had the same information Ray Kroc had, but Kroc was the one with the entrepreneurial insight, built partly on his experience in the restaurant industry. Other times the information is not generally available. This will be the case with most private research and development. But as already noted, technological advance is not entrepreneurship. Entrepreneurship is a market activity that arises solely within the context of markets. A profitable opportunity is spotted by an entrepreneur, and acted upon (Holcombe, 2003).

Regardless of whether the information about an opportunity is privately held or more generally available, entrepreneurial opportunities arise from three general sources. First, they can come from factors that disequilibrate the market. Second, they can come from factors that enhance production possibilities. Third, they can come from the activities of other entrepreneurs.

2.7 Source of Entrepreneurial Opportunity

As important as factors that disequilibrate the market and factors that enhance production possibilities are to the production of entrepreneurial opportunities, the most important source of entrepreneurial opportunities is the activity of other entrepreneurs. When an entrepreneur takes advantage of a previously unnoticed profit opportunity, this creates new profit opportunities,

allowing other entrepreneurs to act, and the process continues cascading through the economy creating additional profit opportunities. The process of entrepreneurship itself is the most common source of new entrepreneurial opportunities. (Kirzner, 1973), depicted entrepreneurship as the recognition of previously unnoticed profit opportunities, and emphasized, in contrast to cited in (Holcombe, 2003), the equilibrating nature of entrepreneurship. Kirzner focused on how entrepreneurial activity exploited previously unrecognized profit opportunities to pull the economy toward equilibrium, rather than considering how these profit opportunities had been created, or why they had gone unrecognized. In fact, most profit opportunities had not been previously recognized because they were relatively new, and once created, they were rapidly exploited. By filling in the details about how profit opportunities are created, Kirzner's story becomes more complete. Kirzner described the process of entrepreneurship in response to those entrepreneurial opportunities that had not yet been noticed, and this paper complements Kirzner's story by describing the origins of those entrepreneurial opportunities. Because most entrepreneurial opportunities are created by the actions of entrepreneurs, the same theory of entrepreneurship explains both the origins of entrepreneurial activity and the way in which entrepreneurs act on available opportunities (Holcombe, 2003).

If one concentrates only on the response of entrepreneurs to a stock of entrepreneurial opportunities, it appears as if there is a pool of opportunities from which entrepreneurs can draw, but as entrepreneurs act, the remaining number of entrepreneurial opportunities is reduced as the economy approaches equilibrium, and at equilibrium all of the entrepreneurial opportunities have already been exploited. Looked at in this way, the more entrepreneurial activity there is, the fewer entrepreneurial opportunities will be available. However, just the opposite is true. Each entrepreneurial action creates more entrepreneurial opportunities, increasing the pool of entrepreneurial opportunities as entrepreneurship takes place. Olson, (1996), in a paper titled "Big Bills Left on the Sidewalk," argues that people just do not pass by easily exploited profit opportunities. Olson is considering why some economies grow more rapidly than others, but he makes the important point that when the incentives are right, profit opportunities do not remain unexploited long. If Olson is right, continuing entrepreneurial activity requires a continuing source of new entrepreneurial opportunities, and the key point of this section is that those new opportunities are created by entrepreneurs as they exploit existing opportunities.

In one way, this positive feedback mechanism where entrepreneurship creates additional

entrepreneurial opportunities might be viewed as a kind of network externality, as discussed by (Bygrave & Minniti, 2000). Bygrave and Minniti focus on the way that the culture of entrepreneurship can spread, which is undoubtedly correct, but as this section notes, independent of any cultural effects (such as some entrepreneurs serving as role models for others) or community characteristics that might make people more likely to act entrepreneurially, entrepreneurial actions simply produce more entrepreneurial opportunities that will then be available to be exploited. Independent of any network effects, entrepreneurial actions create more entrepreneurial opportunities. Network effects work in the same direction, however, so the effects of entrepreneurship discussed in this section are reinforced by the network effects insightfully modeled by Bygrave and Minniti.

To see how entrepreneurship can create additional entrepreneurial opportunities, consider an example in one of the most entrepreneurial industries at the end of the twentieth century: microcomputers. Somebody had the idea that rather than have the microcomputer mouse tethered to the computer with a cord, the mouse could transmit an infrared signal to the computer, enabling the mouse to be wireless. Why had nobody acted on this entrepreneurial opportunity before? The answer is that it had not existed very long before it was exploited.

The opportunity had not been lying in wait for decades; rather, shortly after the mouse became a popular input device for computers, this opportunity was observed and acted on. The opportunity was created by the development of the computer mouse, itself an earlier act of entrepreneurship, and computer users know that pointing sticks, trackballs, and touchpads are other input devices developed by entrepreneurs. But this particular pool of entrepreneurial opportunities only existed after the development of the mouse as an input device. The entrepreneurial activity of the developer of the mouse did not use up an entrepreneurial opportunity; it created many more entrepreneurial opportunities.

Similarly, the mouse was not an opportunity that went unnoticed for long either. Computer mice came into widespread use shortly after microcomputers became powerful enough to use them as input devices, so the entrepreneur who developed the mouse was building on an opportunity that was the product of the entrepreneurs who developed the microcomputer. Without microcomputers the opportunity to profit from the sale of mice would not exist.

The more complete story is slightly more complex, but shows again how the entrepreneurial actions of some produce opportunities for others. The mouse was actually developed by Xerox,

but Steve Jobs at Apple Computer recognized the potential of the input device and popularized it. Then, seeing how well the device worked, Bill Gates at Microsoft built an operating system using the idea, and became the richest man in the world. But there would have been no opportunity to develop the infrared mouse (and touch pad and pointing stick and track ball) had the mouse not first been developed as an input device. In turn, this entrepreneurial act depended upon entrepreneurs seeing that microprocessors could be used as the basis for microcomputers, an entrepreneurial discovery that could not have taken place without the invention of the microprocessor. And that entrepreneurial act could not have occurred without the invention of the transistor. The example illustrates the idea that entrepreneurs do not use up entrepreneurial opportunities, they create them. One act of entrepreneurship creates many more entrepreneurial opportunities. One can analyze a single act of entrepreneurship, but to do so overlook the cumulative nature of the ongoing process of entrepreneurship in the economy. In an economy that is relatively stagnant, or in a model in which the economy is in equilibrium, there are little or no entrepreneurial opportunities to be exploited. With little in the way of entrepreneurship, few new opportunities are being added to the pool, and it does not pay to be very entrepreneurial. Omniscient observers can tell real profit opportunities from apparent opportunities that look better than they really are, but in the real world entrepreneurs may take losses as a result of erroneously perceiving what appeared to be an opportunity. When few opportunities exist, the chances of being wrong increase and entrepreneurial activity will be almost nonexistent.

On the other hand, when there is much entrepreneurial activity, many new opportunities are being added to the pool, and entrepreneurial activity is more likely to pay off, creating an incentive to be more entrepreneurial.

Entrepreneurship is an integral part of the process of economic growth, as Holcombe, (2003) explains, but when considering the origins of entrepreneurial opportunities, growth and past entrepreneurship differ in important ways. Growth creates entrepreneurial opportunities by changing the type and mix of output demanded, and creating the opportunity to take advantage of scale economies. These opportunities are exogenous to the entrepreneurial process, and are eliminated as entrepreneurs act on them. Entrepreneurial opportunities created by entrepreneurship change the nature of the production process, so generate additional entrepreneurial opportunities, making them an endogenous process that produces continuing growth.

2.8 The Environment of Entrepreneurship

Entrepreneurship begins with the observation of a previously unnoticed profit opportunity, but as the previous section has shown, profit opportunities are just not waiting for the ordinary person to observe and act upon. Once the opportunity is created, typically it is acted on rapidly, by those who are in the proximity of the opportunity. It makes sense, for example, that those working in the computer industry are the people most likely to observe an opportunity in that industry. As Hayek (1945) cited on (Holcombe, 2003) noted, everyone has knowledge specific to their own activities, and the economy will be most productive when the economic system gives everyone an incentive to act on the specific knowledge they possess. Hayek stressed the advantages of a market economy, which allows individuals to act on their own specific knowledge of time and place, and also provides the incentive, in the form of entrepreneurial profits, to act entrepreneurially. Entrepreneurial activity depends to a large degree on allowing entrepreneurs to keep the profits from their entrepreneurial actions (Hawk, Morck, Yeung, & Fogel, 2006).

This is well-recognized. Entrepreneurs also respond to the availability of entrepreneurial opportunities. The more opportunities available, the more alert entrepreneurs will be toward finding them. Noticing an entrepreneurial opportunity might be compared to finding money on the sidewalk. A person walks by and is alert to the fact that the money is there, and picks it up and profits from it. Few people keep a vigilant lookout for money on the sidewalk, for the simple reason that there is not much lying about to be picked up. If finding money on the sidewalk were a more frequent occurrence, surely people would be walking with their eyes down, more alert to the opportunity. So it is with entrepreneurship. The entrepreneur notices an opportunity nobody else has seen before, but often it is because the entrepreneur is trying to be alert to upcoming opportunities. And like the money on the sidewalk, entrepreneurial opportunities do not lie around for long before they are picked up by someone. Here the analogy stops, however. Once the money is gone, nobody else has the opportunity to find it. However, when an entrepreneur acts, more entrepreneurial opportunities are created, making it more likely that one can find a profitable opportunity by following in the tracks of other entrepreneurs. Entrepreneurship creates more opportunities and gives potential entrepreneurs more of an incentive to look for them.

People rarely search the sidewalks in hope of uncovering treasure, but it is not uncommon to see people methodically scavenging on a beach, perhaps with metal detectors, because finding valuable lost objects on the beach is a more common occurrence than finding items on the

sidewalk. Similarly, entrepreneurs more actively seek new profit opportunities in the computer industry than in textiles, because opportunities are more likely to be found there. In Kirznerian fashion the entrepreneur stumbles upon a previously unnoticed profit opportunity, but as notes, successful entrepreneurs are often trying to be alert to opportunities. In the Kirznerian framework, there is a key distinction to be made between trying to be alert to entrepreneurial activities, which is really a type of search behavior, and entrepreneurial acts themselves. Potential entrepreneurs can engage in search activities in order to increase the probability that they will come upon an entrepreneurial opportunity.

In an environment where opportunities frequently arise, remaining alert is profitable, which gives people an incentive to search for and be alert to entrepreneurial opportunities, and creates more entrepreneurial alertness.

Because entrepreneurial activity is the most common source of entrepreneurial opportunities, entrepreneurship tends to be clustered. Certain industries are more entrepreneurial than others, as are certain geographic areas and certain nations. Entrepreneurship creates an environment where more entrepreneurship can thrive. Silicon Valley in California provides an example where entrepreneurship is clustered as some entrepreneurs remain on the lookout for opportunities created by past entrepreneurial acts. If past entrepreneurship used up opportunities rather than creating them, one would expect the most promising opportunities to lie far afield from recent entrepreneurial successes.

This view of entrepreneurship as the creator of entrepreneurial opportunities completes Kirzner's model of entrepreneurship. Kirzner focuses on how entrepreneurs respond to entrepreneurial opportunities, and this paper explains how entrepreneurial opportunities arise as a result of the actions of entrepreneurs themselves. The act of entrepreneurship creates more entrepreneurial opportunities, initiating a perpetual process of entrepreneurial discovery.

2.9 The Role of R&D in the Entrepreneurial Environment

Kirzner's entrepreneurs happen upon entrepreneurial opportunities that have not yet been noticed by others. This entrepreneurial act uses no resources, and requires no investment. The entrepreneur is simply alert enough to notice something that has not been noticed previously.

However, as the previous section observed, people will be more alert to entrepreneurial opportunities when they are more readily available. Furthermore, they may be able to produce an

environment themselves where entrepreneurial discoveries are more likely to be made. This is the role of research and development. Research and development does not by itself produce entrepreneurial opportunities, but it does produce an environment in which profit opportunities are more likely to exist. Thus, by undertaking research and development, individuals are more likely to find themselves in an environment where entrepreneurial insights can occur. This does not have to be the case. Consider two examples. The former Soviet Union, perhaps taking neoclassical growth models too seriously, invested heavily in research and development, as well as physical and human capital, which are the inputs that should produce economic growth. Yet their R&D did not lead to growth, because despite the technical advances that were made, there was not the economic environment that allowed those advances to be employed entrepreneurially. To draw on a previously used example, the fundamental building blocks of the Apple Macintosh computer, including the use of windows and the use of a mouse, were developed by Xerox, which totally failed to capitalize on them. Had Xerox been in the Soviet Union, its R&D efforts would have been wasted. However, in the United States, entrepreneurs from another company were able to seize the entrepreneurial opportunities created by the first.

These examples show that research and development is not entrepreneurship and does not necessarily lead to entrepreneurial insights. It can, however, produce an environment within which entrepreneurial opportunities are more likely to be discovered. As noted earlier, and as emphasized by Harper (1996), the growth of entrepreneurial opportunities is intimately connected with the growth of knowledge, so generating new knowledge can increase the possibility of finding entrepreneurial opportunities. Furthermore, if a firm has its own proprietary R&D activities, it can search an environment likely to have entrepreneurial opportunities to which nobody else has access. Entrepreneurship cannot be produced, but an environment within which entrepreneurial discoveries are more likely can.

The argument is sometimes made that research and development should be subsidized, because the resulting knowledge that is produced is a public good. Thus, the argument goes, there will be underinvestment in the production of knowledge, and when knowledge is produced, it will be underutilized for two reasons. First, if it is covered by patents or copyrights, its availability will be restricted by the monopoly power conveyed by the producer of the knowledge. Second, if it is privately produced, those who have the knowledge have an incentive to withhold it from others who could use it profitably, in order to reap the benefits themselves. Thus, the optimal policy is to

undertake R&D with public funds, and make the knowledge produced through R&D freely available to the public. These arguments apply to the products of research and development, once the research has been done, but treat research output as if it is a free good. As the section above noted, there is an incentive to engage in research activities to further the state of knowledge because it creates an environment that produces potential entrepreneurial opportunities. If the activity were subsidized, the researchers would have less incentive to undertake those research projects most likely to lead in the direction of welfare-enhancing innovation.

The argument against subsidization is that private activity provides the incentive to create an environment most likely to lead to profit opportunities, as opposed to merely engaging in the interests of the researchers themselves. The arguments favoring subsidization contain the implicit assumption that the same research activities would occur whether they were done privately and produced proprietary results, or whether the subsidized research results were available to all. But there is no reason to think that subsidized research and development will resemble privately financed R&D, any more than the consumer products of the former Soviet Union resembled consumer products in the United States. Subsidies to some research do not necessarily prevent others from engaging in their own independent research, but subsidies do take away from some of the profit potential of non-subsidized research. If there is the chance that insights could be produced first by a subsidized operation that reduces the incentive to engage in unsubsidized research, even if the unsubsidized research is likely to be more productive. Furthermore, if research in an area is subsidized, potential entrepreneurs might free ride off the subsidized research, waiting to see what the subsidized research produces rather than engaging in their own independent research. When one views research and development as an activity that creates an environment conducive to entrepreneurship, rather than an activity that produces technical advances, the argument for subsidization fares badly. Thus, the distinction made earlier between knowledge and entrepreneurship has important policy implications. A theory of economic growth based on technological advances will look upon subsidized research and development more favorably than a theory of economic growth based on entrepreneurship.

2.10 Institutions and Entrepreneurship

One can see, from a theoretical standpoint, that when markets are disequibrated, when production possibilities are enhanced, and when the economy already has a substantial amount of

entrepreneurship, the economic environment is conducive to continuing entrepreneurial activity. An important policy question then becomes, how can an environment in which entrepreneurship thrives be created? In response to the neoclassical theory of economic development that has emphasized investment and technological advances, with poor results, economists have recently developed an increasing interest in trying to understand how economic policy can create an environment conducive to entrepreneurship and economic progress. Scully, (1988; 1992) has noted the importance of free markets in the creation of an environment conducive to economic growth, and Barro, (1996) argues that it is the protection of economic freedom rather than democracy and political freedom that creates a productive economic environment. In a comprehensive empirical examination of the issue, (Gwartney, Lawson, & Block, 1996) relate economic freedom to economic growth, and identify those particular market institutions that appear most closely associated with economic growth.

Along the same lines, Gwartney, Lawson, & Block, (1996) show the close relationship between market institutions and economic growth, holding constant factors such as human and physical capital, and political institutions. These examples are representative of an extensive literature on the importance of market institutions to the production of economic growth. A complete discussion of the institutional factors that create an environment conducive to entrepreneurship would require another paper, and is somewhat peripheral to the subject of this paper. The key point for present purposes is that market institutions are important because without them, the environment within which entrepreneurship takes place is missing. Entrepreneurship is a key ingredient to a prosperous economy, and while this requires a vibrant private sector, government policies can have a major effect on the amount of entrepreneurship that takes place. Government can encourage entrepreneurship by providing a stable economic environment and by protecting property rights. Market institutions are vital as a foundation for entrepreneurial activity, and excessive government interference through taxation, regulation, and redistribution, can kill the incentives for entrepreneurship. If one takes a production function approach to the economy, it appears that the route to prosperity is through increasing inputs, requiring investment and technological advances. This approach ignores the entrepreneurial role involved in combining inputs most effectively. Entrepreneurship involves noticing previously unexploited profit opportunities, and is not so amenable to mathematical modeling as the relationship between inputs and outputs. Yet over the long run it is much more important to nurture entrepreneurship

than it is for public policy to encourage investment. An economic environment conducive to entrepreneurship provides private incentives to invest in human and physical capital, and to make technological advances, without any explicit policy. Investment and productivity increases follow automatically in an environment that allows entrepreneurship to thrive. Entrepreneurial acts have a certain amount of mystery surrounding them. But creating an environment within which entrepreneurship thrives is not a mystery. Stable market institutions are the key.

2.11 Debates in Entrepreneurship: Opportunity Formation

The field of entrepreneurship has struggled since the 1970s to define itself as field and gain legitimacy as a valid academic area of research. Much of the work in entrepreneurship was either theoretical or used the phenomena as a context in which to observe other theories (Alvarez & Barney, 2008). This led to a “land grab” mentality almost a rapaciousness regarding entrepreneurship research among many of the established disciplines economics, sociology, organization behavior, strategy, organization theory looking for something new to study. However, during this time there were scholars devoted to entrepreneurship as a core research field. This focused research has led to a unique defining question for the field of entrepreneurship: where do opportunities come? Moreover, there have been at least three special issues on this topic in Strategic Entrepreneurship Journal. This question of where opportunities come from has generated significant debate (Alvarez & Barney, 2008). This debate is embedded in a larger philosophy of science debate about realist and constructionist paradigms that has plagued organizational science scholars for at least the past four decades (Moldoveanu & Baum, 2002). Moreover, it is at the core of the debate between discovered realist opportunities and created evolutionary realist opportunities (McMullen & Shepherd, 2006). On the one hand, realists assume that reality has an objective existence independent of individual perceptions (Popper, 1979). On the other hand, constructionists argue that reality is a social product based on the social interactions of individuals and does not have an existence independent of individual perception (Berger & Luckmann, 1967; Kuhn, 1970; Weick, 1979) cited on (Alvarez, Barney, & Young, 2010). Recently, scholars have begun to identify ways that apparent conflicts between realists and constructionists can be resolved. One such way is the evolutionary realist approach, which assumes that reality is as individuals perceive it but that it is tested against an objective and external, albeit potentially unobservable, reality which is a reliable guide to action (Azevedo,

2002). For example, Campbell (1974) cited on Alvarez, Barney, & Young,(2010) argues that there is a reality that is independent of an individual's perception and that this reality plays a part in the selection and editing of individual's beliefs and perceptions. Perhaps not surprisingly, up to this point in the evolution of the field of entrepreneurship the realist perspective of how opportunities are formed and exploited has dominated, while the constructionist and evolutionary realist approaches have received much less attention (Venkataraman, 2003). This is not to say that constructionist or evolutionary realist work has not been done in the field of entrepreneurship. However, realist views of entrepreneurship labeled as either the individual/opportunity nexus approach or discovery have to this point been more systematically developed as approaches to opportunity formation (Shane S. , 2003; Alvarez, Barney, & Young, 2010).

2.12 Entrepreneurial framework conditions in Ethiopia

A. The Trajectory of MSE Development Policies and Strategies in Ethiopia since 1950

Examinations of attempts institutional involvement to support MSEs' development in Ethiopia came late after 1950s. Teshome (1994) cited in (Assefa, Zerfu, & Tekle, 2014) points that the focus of government policy was to lay foundation of basic administrative and institutional infrastructure of the state during the 1940's and 1950's, in order to consolidate the gains of reforms to accelerate the process of industrialization. As a result, several reforms related to the development of MSEs were made during this period.

The Business Enterprise Registration Proclamation No.184/1961 required business enterprises to register under the Ministry of Commerce and Industry. By the Industrial Regulation Legal Notice No.292/1971 manufacturing enterprises were required to acquire a temporary license of six month validity and a permanent license, if fully formed (Assefa, Zerfu, & Tekle, 2014). The Investment Proclamation No. 242/1966 provided MSE's tax relief, access to land and buildings, public utilities and other facilitations of advisory and administrative nature.

The period 1974 to 1991 started with socialist proclamations and nationalization of businesses and firms throughout the country. By Proclamation No.26/1975 the government implemented these socialist proclamations and ended up owning and controlling the means of production and

“the commanding heights of the economy”. Proclamation No.26/1975 classified all economic activities into private and government leaving room to joint undertakings by government with foreign investors.

The proclamation crippled private sector development in the country. This process of down-scaling the role of private economy continued and according to Proclamation No.76/1975, acquisition of private businesses was restricted to a single license and capital ceiling set at 300,000 birr for wholesale trade, 200,000 for retail trade and 500,000 for industrial establishments. The process of crowding out private industry was strengthened by Proclamation No.19/1975 which established the Ministry of National Resources Development with a mandate to promote public enterprises. The Public Enterprises Proclamation No.20/1975 (amended by Proclamation No.35/1975) further strengthened the Ministry of National Resources Development by mandating it to reorganize, consolidate and manage nationalized and new public enterprises. The marginalization of private sector development in the area of MSEs continued well into 1977: in late 1977, for example, the Handicrafts and Small Scale Industries Development Agency (HASIDA) was established by Proclamation No. 124/1977. The objective of HASIDA was to give further boost to the development of the public economy by encouraging cooperative development in the small scale sector. HASIDA issued licenses to cooperatives, regulated their activities, and assisted in the provision of inputs and training.

During the 1980’s HASIDA achieved very little in its objectives. Few service and producers’ cooperatives were formed, their numbers increased and then decreased through bankruptcy, lack of imported inputs, and eventual closure and at the same time private investment in the sector virtually ceased.

Following policy failure over two decades, the Derg, declared a new program of mixed economy development. Accordingly, it issued two declarations in succession: the Small Scale Industry Development Special Decree No.9/1989 and Special Decree on Investment No.17/1990, both by Council of State.

Decree No.9/1989 allowed establishment of small-scale enterprises by business organizations, cooperatives and individual entrepreneurs. This Decree replaced the restrictive Proclamation No.76/1975 and unlike this proclamation, the Decree allowed participation by the Diaspora and

raised the capital ceiling for small scale enterprises from birr 500,000 to between two and four million birr. Decree No.17/1990 lifted the restriction of private sector participation to single license (by Proclamation No.76/1975) and allowed individuals to undertake investment in unlimited number of enterprises, and attempted to provide incentives to do so.

Further enhancement was given by the new Regulations No.8/1990 which was aimed at operationalizing the two aforementioned Decrees. According to the Regulations, prospective investors in the MSE sector were required to have a temporary license which permitted completion of the establishment phase of their projects and eventually own permanent license when the investment reached the production phase. However, the adventure into mixed economy development was short lived. The Derg was overthrown in 1991.

The new régime led by the Ethiopian People Revolutionary Democratic Front (EPRDF), immediately proclaimed the Emergency Recovery and Reconstruction Program (ERRP) and started a program of private sector development. In 1991, the ERRP, with the support of the World Bank and the international community to bring about economic stabilization, launched public sector reform and private and market economy development. Several other supporting proclamations were also issued which include the new labor law (Proclamation No. 42/1993 and its amendments), the Encouragement, Expansion and Coordination of Investment Proclamation No.15/1992, and Administrative Reform Proclamation No.31/1992, and its amendment, Proclamation No.15/1992 (Regional State Governments were empowered to establish their respective regional investment offices to receive review and decide on investment applications).

Proclamation No.41/1993: Definition of Powers and Duties of the Central and Regional Executive Organs of the Transitional Government of Ethiopia provided for the establishments of Industry and Handicrafts Bureaus in the Regional Governments has replaced the HASIDA proclamation (Proclamation No.124/1977). Nonetheless, the change doesn't seem to have a lasting impact on the status of MSEs development in the country. The issue of temporary licenses proceeded without restraint and at a nominal charge and resulted in an oversell of such licenses. Individuals obtained the temporary licenses to take advantage of the access to land; public utilities and credits that such license were expected to give them. However, these temporary licensees failed to graduate to permanent license holding and were unable to get the access to land, utilities and credits as they expected. The result had been lack of growth of investment in

MSEs development and the in formalization of the few investments that obtained license in the process. As a consequence, most temporary license holders withdrew their licenses and most of the few that reached the stage of production (permanent license holding) withdrew from the process and started working underground (Assefa, Zerfu, & Tekle, 2014).

One of the measures taken to enhance the operation of MSEs is the issuance of the licensing and supervision of micro financing institutions proclamation in 1996 (Proclamation No. 40/1996). The principal aim of this proclamation is to enable MSEs have access to credit facilities, counseling services and income generating projects through micro-finance institutions. By building the capacity of MSEs, this legislation provides opportunities and security for the informal sector operators through enhancing legality and formalization.

The EPRDF adopted Agricultural Development Led Industrialization (ADLI) and private sector development strategy in 1995. An element of these strategies was focused on MSEs development: Federal Micro and Small-Scale Enterprises Strategy (FMSES) and Regional Micro and Small- Scale Enterprises Strategies (RMSES) were formulated in 1997. Federal Micro and Small-Scale Enterprises Development Agency (FeMSEDA) and Regional Micro and Small-Scale Enterprises Development Agencies (RMSEDA) were established by the Council of Ministers of Ethiopia Regulation No.33/1998, and supportive financial sector reforms were made. Among the principal objectives of the FMSES and RMSES are exploitation of local raw material, creation of productive job opportunities, adoption of new and appropriate technologies, and enhancement of the development of MSEs which have wide-ranging backward and forward linkages.

In order to operationalize FeMSEDA and RMSEDA and address the major issues and problems constraining MSEs development, the government issued an Industrial Development Strategy in 2003, which was aimed at providing a package of material and technical government support to the MSEs including, inter alia, provision of utilities and infrastructure, raw materials, access to credits, etc.

At the early 2000's, the World Bank introduced poverty reduction strategy for Less Developed Countries which is in line with the Millennium Development Goals. For Ethiopia, the program has two phases: the Sustainable Development and Poverty Reduction Program (SDPRP) and the Plan for Accelerated and Sustained Development to End Poverty (PASDEP).

SDPRP was aimed at creating an enabling environment for accelerated development and attainment of improvements in the standard of living of the people and it lasted from year 2000/01 to 2003/04. PASDEP is designed for the years 2005 to 2010 and identified development of MSEs as a best venue for job creation and to mitigate the pervasive youth unemployment observed in the country. According to PASDEP, MSEs would get extended basic trainings, upgraded business development services and enhanced market linkages with foreign importers through FMSEDA and RMSEDA in the planned period.

GTP (Growth and Transformation Plan), which is the successor of PASDEP and the current development strategy of Ethiopia (2010 -2015), has also given a priority to MSEs development. The GTP has put the MSEs development as one of the seven identified growth pillars of the country. The MSEs to be a development pillar, they have to be formal to get the necessary support.

The excursion made in the MSE strategy of Ethiopia in brief reveals the vastness of the role MSEs in the entire economy has been immense. Some studies in these areas rightly point out that MSEs have been on the forefront in employment creations, poverty reductions, proliferations of entrepreneurships and thus economic development concurrently (Central Statistics Agency, 2004; Growth and Transformation Plan, 2010). From this point of view, two MSE strategy documents could come into attention from most recent attempts the current government has been making. These are: the MSE Development Strategy of 1997 and 2011 (Assefa, Zerfu, & Tekle, 2014).

As indicated in the preceding parts, the MSE Development Strategy formulated in 1997 clearly enlightens a systematic approach to alleviate the problems and promote growth of enterprises. The primary objective of this national MSE development strategy has been to create enabling environment for MSEs to operate. Thus, it is expected that hundreds and thousands of MSE, will, themselves be responsible for the operation, growth and progress of their enterprises given such an enabling environment. The specific objectives of the 1997 strategy framework were to facilitate economic growth and bring equitable development, create long term jobs, strengthen cooperation between MSEs provide the basis for medium and large scale enterprises promote export and balance preferential between MSEs and bigger enterprises. The new MSE Strategy (2011) included fresh band of target groups, the graduates, (in addition to its classical emphasis on the poor and less skilled people) and is also hoped to bring about the technological transfer

and new corporate management skills to the nation. In this strategy also new set of areas are identified as requiring attention and priority from the government. The other new and important concept raised in the new MSE strategy is about the stage of growth of the MSEs. According to this strategy the supports these enterprises receive is dependent up on their level of growth and is relatively a tailored one.

B. Ethiopia's Current MSE Promotion Policy

Ethiopia has launched various bold initiatives and development policies and plans to spur economic growth. Three major development plans have been executed so far, the last one being the first Growth and Transformation Plan (GTP) of 2010. The common and overarching objective of these development plans has been to ensure broad based economic growth. This is so because broad based economic growth is the main route to poverty reduction through employment generation. The role of Micro and Small Enterprises (MSEs) is indispensable in poverty reduction through employment generation. Cognizant of this, a national MSEs Development Strategy was formulated in 1997. Ethiopia's MSE Policy envisages not only reducing poverty in urban areas but also nurturing entrepreneurship and laying the foundation for industrial development. The strategy was revised in 2010/11 with renewed interests and more ambitious targets on employment and number of entrepreneurs and transition to medium size level.

MSE development, being one of the key focus areas of the country's development strategy, receives massive support from the government in the form of access to finance, market, technology, training and working space. The government strongly believes that MSEs are the right solution to reduce urban unemployment and hence reduce poverty. This ambition is reflected in the GTP (Growth and Transformation Plan, 2010). Therefore, MSE promotion and support is the vital strategy to fulfill this national plan of employment creation in the short-run and achieving industrialization in the long- run. Ethiopia adopts a layered policy support in which MSEs are categorized into start-ups, growing-middle and maturity. Start-up stage enterprises refers to those enterprises found at their establishment stage and comprises a group or individual aspiring entrepreneurs that seek various supports to make their enterprise operational. The basic challenges at this stage include lack of initial and working capital, poor knowledge of business management and entrepreneurship and lack of knowhow about the different government

policies and directives related to the sector. In order to mitigate these challenges, FeMSEDA has designed a strategy that focuses on facilitating access to initial capital, supporting MSEs in formalization and legalization process and provision of training on business management, entrepreneurship and production technique (Assefa, Zerfu, & Tekle, 2014).

Growing stage enterprises refers to those enterprises that are competent in the market in terms of price and quality and successfully utilize the various government support packages and are profitable in their business. However, enterprises at this stage also suffer from different challenges like financial constraint, lack of appropriate technology and technical skill, absence of sufficient working and sales premises and rent seeking behavior. To alleviate these specific challenges, FeMSEDA has formed a national strategy that focuses on facilitation of financial support and skill and technological development program. On the other hand, enterprises are considered to have reached the maturity stage when they are fully profitable and engaged in further expansion and investments in the sector. At this stage FeMSEDA has a strategy that aims to strengthen enterprises in terms of productivity and product quality. Moreover, at this stage, knowledge of international standards and better production technology are disseminated to enterprises. We discuss each of the direct government support to MSEs in subsequent sections.

C. Financial Support

Critical to the development of any new business is the existence of accessible funding that provides entrepreneurs with the financial resources to start their businesses. In this regard, FeMSEDA has designed a national micro credit and saving directive that primarily focuses on alleviating the financial constraint of MSEs operating in the country. The priority areas of the national micro credit system include those MSEs that are engaged in import substitution, construction and export. This national micro credit and saving facility designed for MSEs has three different requirements. These are the credit requirement for start-up, growing and matured micro and small enterprises. First, MSEs at the start-up stage are required to save 20% of the loan within six months. For those who cannot afford saving 20% from their own sources or from their parents, the government provides them with job opportunities to raise seed money. Second, similar to start-up enterprises, growing MSEs that are engaged in priority sectors are expected to save 20% of the credit within six months. However, growing enterprises that are involved in export activities are obliged to save only 15% of their credit demand. On the other hand those

growing MSEs that are neither engaged in export nor in priority sub-sectors are forced to save 25% of their credit need within six months.

The third category of the credit requirement is for MSEs which are at maturity stage. Under this category, those matured MSEs that are engaged in export are obliged to save 15% of the required credit in six months period. Whereas those matured MSEs that are involved in priority areas are required to deposit 20% of the loan. Nevertheless, those MSEs at maturity stage and neither engaged in export activity nor in priority sub sectors are required to save 30% of their credit demand in six months period. The incentive to work hard and use the loan appropriately increases when MSEs pool at least 20% as equity in the form of minimum saving requirement. Higher equity also lowers delinquency rate. (MSE Development Strategy, 2011)

D. Education, Training and Technological Support

The ability of an entrepreneur to go from an idea to the commercialization of a business base on this idea requires particular competencies (Knowledge, experience and skills). These may be developed through formal education in grade school or university courses, informal methods like books or websites, or training programs offered by private or government sources. Such education is critical to the initial success and sustainability of any enterprise.

In this regard, the national MSE promotion and development strategy paid due attention to human resource and technological development. Pertinent to human resource development, the government intervenes in the sector through two mechanisms. On the one hand, the government directly provides various skill trainings to potential entrepreneurs of the sector. On the other hand, the government also strengthens and supports MSEs through TVETs by producing skilled manpower that could satisfy the manpower demand of the different subsectors of MSEs of the country.

Regarding technological development, the government has been prioritizing those MSEs that are engaged in the manufacturing, construction and mining sub-sectors. The technological development strategy focuses on facilitating appropriate technology and production materials to MSEs in the form of purchase and lease. To this end, the government has proclaimed a new machinery lease policy in 2013. The Lease Company is planned to provide rental machines that are expensive for MSEs to own on their own. The government has also established a system that

motivates individuals and other institutional actors to supply technology with fair price. It is also planned to provide on sight maintenance to machinery and equipment that are owned by MSEs through TVETs. The government also supports in the process of converting prototypes into commercially viable products (Assefa, Zerfu, & Tekle, 2014).

E. Non-Financial Support

One of the major challenges that hampers the growth and development of MSEs in Ethiopia is access to sufficient and sustainable market. From our consultation meetings with various stakeholders, we identified the following support packages that the government is implementing towards mitigating this challenge. The government tries to solve marketing problems in at least three ways: firstly, the government itself buys goods directly from MSEs. Federal Public Procurement Administration Agency has set a rule that enforces public institutions to source certain portion of their annual procurement from MSEs. That is, MSEs are given priority in government procurements. Secondly, the government tries to link MSEs with large and medium enterprises in the market in the form of subcontracting and input suppliers. Large private enterprises were also noted as private market linkages that have significantly involved the subcontracting of some of their works to MSEs. However, most of the market linkages created so far are government induced. Most of the government induced linkages create temporary employment opportunities. (Assefa, Zerfu, & Tekle, 2014)

Thirdly, a number of bazaars and trade exhibition have been organized by MSEs' development agencies to promote MSEs' products and to link them with large and medium enterprises and foreign buyers.

As (Assefa, Zerfu, & Tekle, 2014) stated the main challenge with regards to market linkage is that MSEs depend to a great extent on the government to market their products. The government is the largest buyer and market linkage creator for their products. This has made MSE operators to develop dependency and hence this kind of market linkage cannot be sustainable. MSEs need to gradually shift to market-driven market linkages on their own

Another critical factor for MSE growth is working space. In response, although the government has massively built working spaces for MSEs in major cities and towns, working space still remains a critical challenge. Rent is extremely high in major cities especially Addis Ababa. The

supply of working spaces is small relative to demand. The problem is not only shortage, working spaces are built arbitrarily – for example, they are far from industrial zones. Market linkage may become easier if MSE are located near medium and large enterprises or industrial zones in general. MSEs can benefit from proximity to industrial zones.

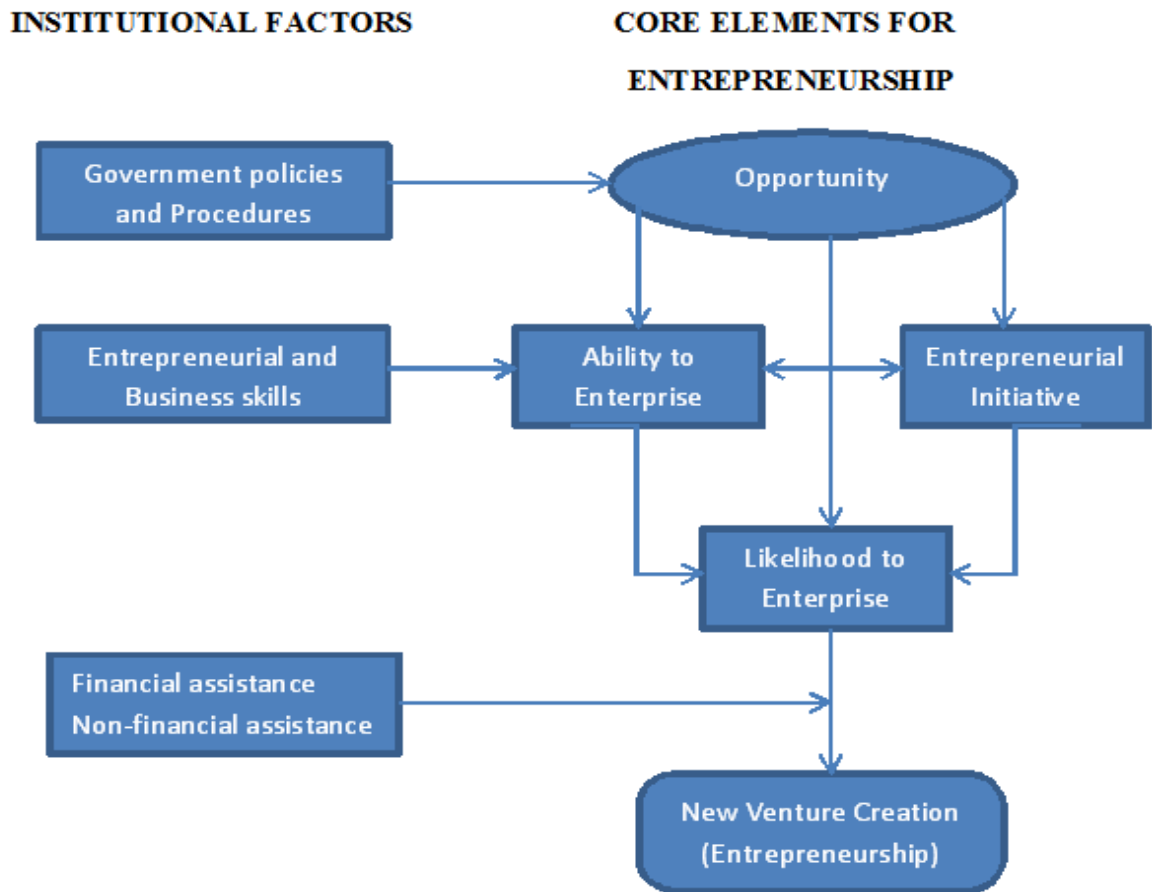
2.13 Conceptual Framework

Institutions which arise because of uncertainties associated with human interaction provide structure and order, and the rules of the game to human exchange, be they political, social or economic (North, 1991). Formal institutions, specifically government and support institutions provide opportunities for individuals to be engaged in entrepreneurship through setting up different programs and policies. Institutions create the incentive structure in an economy, and organizations will be created to take advantage of this kind of opportunities provided within a given institutional framework.

Some key factors may lead to an increase in a person's desire and decision to start a business. Vesper identified four elements in venture creation: a profitable business opportunity, technical know-how of the entrepreneur, business know-how of the entrepreneur, and entrepreneurial initiative (Vesper, 1990). Opportunity refers to the extent to which possibilities for new ventures exist. People with certain behavioral characteristics are able to perceive the opportunities available in the environment, seize such opportunities, and then turn such opportunities into profitable ventures. Yet, a personality or behavioral profile is not a sufficient condition for people to go into business. An individual should feel confident in his or her ability to enterprise which is the sum of technical and business capabilities required to start and manage a business.

Figure 1 shows the interrelationships among the different institutional factors with a specific aspect of the core elements of new venture creation. Generally, the availability of opportunities is a primary element for enhancing the propensity and ability to enterprise and consequently the likelihood to enterprise. The dimension of the institutional factor that directly relates to the opportunity is macroeconomic policies and procedures. The better the legal framework for efficient functioning of the markets and the fewer the barriers that constrain people to pursue business opportunities, the greater the likelihood of business start-up.

Figure 1 A Model of Institutional Factors Influencing the Likelihood of Starting Business



The dimension of the institutional factor that related to the likelihood to enterprise is the level of entrepreneurial and business skills. The greater the availability of technical and business-related training, the greater the ability of the potential entrepreneurs to start and manage a business. Thus, if people have a high entrepreneurial initiative but a low ability to enterprise, institutional intervention will need to develop the entrepreneurial and business skills of these people.

The above analysis suggests the following propositions.

- The higher the opportunity, propensity to enterprise, and ability to enterprise, the higher the likelihood to enterprise.
- The greater the entrepreneurial and business skills, the grater the ability to enterprise.

- The more favorable the government policies and procedures, the higher the opportunity to enterprise.

As argued earlier, a person with high propensity to enterprise may enter into business; yet the person is likely to fail either at the start-up stage or afterwards if he or she lacks the ability to enterprise. Conversely, a person with high ability to enterprise but low propensity to enterprise lacks adequate motivation to venture into business. Successful entrepreneurship thus requires high levels of propensity and ability to enterprise. Therefore, the higher the likelihood to enterprise, the higher the new venture creation.

The figure shows that financial and non-financial assistance appears important only if the overall likelihood to enterprise is high. Previous studies (Davidsson, 1991) have shown that tax and other incentives were important when people had higher motivation to go into business. Therefore, the higher the likelihood to enterprise and the greater the availability of financial and non-financial assistance, the higher the new venture creation.

2.14 Summary of the Revised Literatures

Entrepreneurship can be interpreted in various ways and can have different meanings. The institutional theory developed by North primary analyses economic structures by explaining how institutions and institutional changes affect performance of economies. Theory of entrepreneurship emphasizes the equilibrating role of entrepreneurship. When the market is not in equilibrium, profit opportunities exist, and entrepreneurs discover and act on these profit opportunities to equilibrate the market. Because Kirzner focuses on entrepreneurial actions when profit opportunities exist, and does not describe where they come from, one could imagine a fixed stock of profit opportunities that get used up as entrepreneurs discover them. But as the literatures explained new profit opportunities are being created constantly. Classification of the origins of entrepreneurial opportunities includes factors that disequilibrate the market, factors that enhance production possibilities, and most notably, opportunities created from previous acts of entrepreneurship. Entrepreneurial actions do not use up profit opportunities, but create them, and the critical role of entrepreneurship in the creation of new profit opportunities is emphasized. This line of reasoning leads directly to policy implications regarding the institutional environment conducive to entrepreneurial discovery and the role of government in research and

development. In many cases however, the lack of an enabling framework and scarcity of support structures for new business can undermine entrepreneurial endeavor.

Chapter 3

3 Lideta, Kolfe Keraniyo and Gulelle Sub Cities' Institutional Framework Contributing to Entrepreneurship Development

3.1 Respondents' General Profile

General profile of SMEs like the years of their stay in business, the form of business ownership they are operating under, the kind of sector they are involved in and the educational background of their members can greatly affect the type and degree of support they need to receive from government. Having this view in mind, SMEs strategy designed to develop the sector also specifies the fact that assistances provided should take SMEs' current stage of development. However, the researched enterprises' needs doesn't show that much difference relating to these variables except sector wise variations. The following tables present the respondents' general information.

Table 2 Enterprises' Year/s of Stay in Business

| Year/s of Stay in Business | Sectors | | | | | | Total |
|-------------------------------|-------------------------------------|--------------------------|---------------------|----------------|--------------------------------|--|-------|
| | Number of Manufacturing Enterprises | | | | | Number of Construction Enterprises | |
| | Textile & Garment | Metal & Wood Works | Leather Products | Shoe Making | Processed & Packed Foods | | |
| 1 - 2 Years | 5 | 2 | 7 | 7 | 7 | 24 | 52 |
| 3 - 5 Years | 6 | 1 | 5 | 3 | 7 | 6 | 28 |
| Above 5 Years | 3 | 11 | 2 | 4 | | | 20 |
| Total | 14 | 14 | 14 | 14 | 14 | 30 | 100 |

Numerous empirical literatures explained the relationship between firm age and growth of firms but with mixed findings. Nichter & Goldmark,(2005) in their review of empirical studies in Africa and Latin America asserted that the relationship between enterprises' stay in business and

firm growth is imprecise, because it is logical to firms gain productivity from learning by doing on the one hand; and older firms fail to acquire improved machineries on the other hand.

Enterprises which have stayed doing business for the last 1 up to 2 years share the largest portion (52%) of the surveyed MSEs. Whereas, firms with business service from 3 up to 5 years and above tend to have similar and compatible aggregate.

Table 3 Types of Ownership

| Ownership Type | Sectors | | | | | | Total |
|---------------------|-------------------------------------|--------------------|------------------|-------------|--------------------------|------------------------------------|-------|
| | Number of Manufacturing Enterprises | | | | | Number of Construction Enterprises | |
| | Textile & Garment | Metal & Wood Works | Leather Products | Shoe Making | Processed & Packed Foods | | |
| Sole-Proprietorship | 11 | | 4 | 9 | 2 | 12 | 38 |
| Partnership | | 2 | 7 | 5 | 9 | 18 | 41 |
| Cooperative | 3 | 12 | 3 | | 3 | | 21 |
| Total | 14 | 14 | 14 | 14 | 14 | 30 | 100 |

Studies reveal important finding related to the relationship between growth of capital and forms of ownership. The study shows that more proportions of MSEs formed by the support of the government tend to register stronger growth than other forms of ownerships meaning the combinations of those supports extended by different government organs might have appeared to be more effective in promoting growth for those MSEs organized by the government. As per the survey of (Ministry of Urban Development & Construction, 2013), government initiated enterprises have registered more annual capital growth than sole proprietorship enterprises showing the strength of capital growth is more pronounced among the MSEs organized by the government than other forms of establishments.

As can be seen from Table 3 without showing much difference among the sub sectors the majority of these businesses are organized as partnership and sole proprietorship. The third place is occupied by those cooperatives which the local governments organize. However, enterprises

form the sub sector of metal and wood works show a unique pattern than others since most of them are organized under the form of ownership of cooperatives compared to other sub sectors. This urges the need to coordinate small and fragmented efforts of small sole proprietors and bring union among them so that expected improved results can be achieved.

Table 4 Employment Created Other than Members

| Number of Employees | Sectors | | | | | | Total |
|---------------------|-------------------------------------|--------------------|------------------|-------------|--------------------------|------------------------------------|-------|
| | Number of Manufacturing Enterprises | | | | | Number of Construction Enterprises | |
| | Textile & Garment | Metal & Wood Works | Leather Products | Shoe Making | Processed & Packed Foods | | |
| Nil (0) | 10 | 3 | 7 | | 7 | 7 | 34 |
| 1 - 5 | 4 | 4 | 7 | 8 | 7 | 17 | 47 |
| 6 - 10 | | 5 | | | | 6 | 11 |
| Above 10 | | 2 | | 6 | | | 8 |
| Total | 14 | 14 | 14 | 14 | 14 | 30 | 100 |

Several studies indicated that micro and small enterprises are characterized by family based business firms employing hardly over two employees often owners and unpaid family workers. Micro and small enterprises are also characterized by lower productivity and income as compared to bigger enterprises. Yet, their larger population enables them to employ the largest labor force in less developing economy next to agriculture. (Ministry of Urban Development & Construction, 2013)

The survey results indicate that 34% of the operators are self-employed, 47 % have employed a one up to 5 workers, 11% employed 6-10 employees and only 8% employed more than 10 employs demonstrating typical features of micro and small enterprises.

Table 5 Educational Background

| Level of Education | Sectors | | | | | | Total |
|------------------------|-------------------------------------|--------------------|------------------|-------------|--------------------------|------------------------------------|-------|
| | Number of Manufacturing Enterprises | | | | | Number of Construction Enterprises | |
| | Textile & Garment | Metal & Wood Works | Leather Products | Shoe Making | Processed & Packed Foods | | |
| Illiterate | 1 | | 4 | 5 | 1 | 1 | 12 |
| Reading & writing | 1 | | | | | | 1 |
| Primary | 4 | 3 | 5 | 5 | 5 | 11 | 33 |
| High school | 6 | 8 | 4 | 2 | 6 | 11 | 37 |
| Technical & Vocational | 1 | 1 | 1 | 2 | 1 | 3 | 9 |
| University Degree | 1 | 2 | | | 1 | 4 | 8 |
| Total | 14 | 14 | 14 | 14 | 14 | 30 | 100 |

An empirical evidence regarding the relationship between educational attainment of owners and operators of MSEs and firm growth revealed significant relationship between these two variables. Owners/ managers and members with better educational background tend to be more productive and formal education enables them enhance their production, management, and marketing skills (Nichter & Goldmark, 2005). The researchers further explained that the overall educational level in developing countries and the very educational characteristic feature of small firm owners happens to dictate firm growth.

The survey result indicated in

Table 5 shows most (37%) of member of sample micro and small enterprises surveyed have attended high school as a highest level of education, next to primary school (33%). Members of very few micro and small enterprises, i.e. 9% have attended TVET education, which indicates that very few MSEs have adequate educational and technical background needed for production and graduates of TVET colleges has not been absorbed in the MSEs sector. Besides 8% of the

members of the MSEs under study have university degree implying only a small portion of the workforce of MSEs have a higher level education attainment.

Disaggregation of members' educational status data by sector shown in

Table 5 indicates that most members of enterprises from both manufacturing and construction sectors have attended at least high school. Moreover, proportion of micro enterprises whose members are illiterate is higher for leather products and shoe making than their counterpart small enterprise members.

3.2 Government policies and procedures

Government can influence the market mechanisms and make them function efficiently by removing conditions that create market imperfections and administrative rigidities. They can also create an "enterprise culture" that enables firms to take reasonable risks and seek profits.

Entrepreneurs may be discouraged to start a business if they have to follow many rules and procedural requirements, if they have to report to many institutions, and if they have to spend more time and money in fulfilling the procedural requirements (Dana, 1987; Young & Welsch, 1993).

Although different policy documents of the country have embraced statements to encourage how entrepreneurship should be developed the major focus of this study will be the revision of the recently approved Micro and Small Enterprises Development Strategy, provision framework and methods of Implementation.

A. MSE Development Support Frameworks

The MSE development strategy has put various support frameworks in order for it to be implemented. These support frameworks are based on the nature of enterprises and the level of growth they are at. The frameworks aim at giving support on major areas that startup businesses need including industry extension services, providing market, supply of credit on fair interest base, technology and production development, expansion of production and sales centers and

also development of a strong one center service or one stop shop centers. These supports are elaborated one by one in the following sections.

B. Human Resource and Technological Development Support

Human resource development combines two concepts; one is striving for the SMEs to be technically competent and productive by providing training and education on the specific areas they are engaged in. The other one incorporates shaping enterprises to develop an entrepreneurial attitude. The technological support given includes facilitating appropriate technologies to be transferred to these enterprises and also providing different manufacturing/production materials in the form of purchase, rent or lease. The third type of support included is the industry extension services which will be solely performed by TVET institutions.

C. Market Development and Marketing System Support

Although searching for potential markets belongs to the SMEs themselves, there are different types of schemes that support the enterprises to have access for market. Strengthening system of subcontracting, outsourcing, franchising and out grower among higher and medium and small enterprises is one scheme. Systems are arranged for SMEs to provide raw materials for higher enterprises and incentives like giving credit services are provided for higher and medium enterprises in order for them to work with the SMEs. Market centers are also constructed and organized for the enterprises for them to display their products and services. Another support for SMEs to get market network is thorough organizing exhibitions and bazaars which are held seasonally at national, regional and zonal levels. The other type of assistance provided under creating a website which is specifically designed to disseminate information to the small enterprises. The website consists of information about current technologies, policies and strategies, best practices of other countries and the likes

D. Finance and Credit Service Support System

Assistance under this category includes developing the saving culture financial skill of the enterprises. Credit is one of the major inputs for startups and business expansion. Credit and other financial service are provided by local micro finance institutions. The focus areas are for those enterprises with good credit history, enterprises that produce exportable items, and which are engaged in the construction sector. The enterprises should first fulfill the criteria set by the

agency before taking any loan. Micro Finance Institutions and public officials are responsible to collect the non-paid loan for checking whether the enterprises used the money properly or not.

The Lease machine program is also another support intended to solve SMEs that have capital and collateral problem to enable them get machinery by primarily saving 40% of the machine's price and by borrowing the rest 60% from a bank. Lease financing program is run by Commercial Bank of Ethiopia and Micro Finance Institutions jointly and it is accessible for all MSE found in urban and rural.

E. Production and sales center development

Production and sales center development is organized to provide and coordinate those enterprises engaged in production and service businesses in towns and other areas. The advantage of these centers is that all kinds of supports can be given reciprocally to a number of enterprises. Users of these centers are enterprises running similar or interconnected businesses since this kind of support enables them develop within shorter time.

F. System of one center service

One center service is a service established with the objective of ensuring the legitimacy of new startups, facilitating their growth through providing an effective and transparent assistance. The service is organized and provided at districts, sub-cities and city level on the basis of the existing environment and actors size/number. The service center encompasses experts who facilitate credit service delivery, information distribution and advice and linkage with TVET institutions. Regulations, manuals and documents are also organized for implementation.

Legal services delivered at one center include identification of unemployment, registration and provision of trade license, giving tax paying identification number (TIN) and facilitation of bookkeeping and auditing services. Government also facilitates and utilizes products and administers cluster centers, consolidates credit paybacks and savings, gathers and delivers data to users. Beneficiaries are also allowed to participate in government development projects. Small enterprises' products are also introduced through bazaars and they can share experiences and get access to markets over the bazaars.

G. Strategy Implementation Methods

The method followed for the strategy to be implemented follows an integrated approach that calls for the coordination of the major actors and stakeholders. Since the three basic things to start a business are financial capacity, knowledge or skill and interest, the strategy considers the integration of TVET and Micro Finance Institutions and government organs involved in industrial sector development with SMEs. First and foremost capacity building of support providers is considered as one method of implementing the strategy. This scheme includes building the capacity of TVET institutions, federal and regional micro and small enterprise development agencies, Micro Finance institutions and officials (the management). Executive bodies at both federal and regional level are also expected to play their own role in the implementation process. Affiliated organs like NGOs, research centers and higher education institutions are also included to be as implementers. Structuring the system and framework that FeMSEDA is operating under is also another method put in the strategy document. The Agency is divided into two major sectors; the business developments sector which deals with market planning and development and the capacity building sector. Participation and involvement of major stakeholders and SMEs themselves is also an additional method strategy implementation. As stated in the strategy document this is done through forming SME development councils at federal, regional, Woreda and town level.

3.3 Financial Assistance

Generally, entrepreneurs require financial assistance for at least one of three purposes: to diversify or spread the start-up risk, to accumulate start-up capital, and to finance growth and expansion. While availability of financial resources appears to be a major predictor of the frequency of new business start-ups, many lenders seem to be unwilling to invest in high-risk projects or tend to withhold support until the firm has been established successfully (Pennings, 1982) .Research has shown that creation of investment companies, provision of low-interest loans, and availability of credit guarantee schemes for small business financing have all contributed to the establishment of new businesses (Dana, 1987; Harrison & Mason, 1988; Hawkins, 1993) .

Although the degree and means of generating it depends on the creativeness of an entrepreneur financial capacity is one of the basic things to start and run a new venture. In this research financial assistance includes the loans and credit provided by MSE bureaus at woreda level.

Table 6 Access to Financial Assistance from Woredas' Micro Finance Institution

| Sectors/ Sub-sectors | Count and percent | Access to financial services form woredas'' Micro Finance Institutions | | Total |
|--------------------------|-------------------|--|---|-------|
| | | Number of enterprises who have accessed financial assistance | Number of enterprises who haven't accessed financial assistance | |
| Construction | Count | 4 | 26 | 30 |
| | % | 13% | 87% | 100 |
| Textile & Garment | Count | 5 | 9 | 14 |
| | % | 36% | 64% | 100 |
| Metal & Wood Works | Count | 7 | 7 | 14 |
| | % | 50% | 50% | 100 |
| Leather Products | Count | 3 | 11 | 14 |
| | % | 21% | 79% | 100 |
| Shoe Making | Count | 10 | 4 | 14 |
| | % | 71% | 29% | 100 |
| Processed & Packed Foods | Count | 1 | 13 | 14 |
| | % | 7% | 93% | 100 |

It is clearly indicated in the strategy that the government facilitates provisions of loan services at preferential interest rate to small and micro enterprises in the nation during the specified time. Though such instruments are very supportive for the growth of MSEs, availability and quality of this support instrument has its own impact on their growth. The data collected on this issue reveals that the majority of the MSEs had not received any credit service in all the surveyed sub cities. The picture is relatively better in sectors like shoe making where only 29% indicated that they had no access to credit services. Enterprises engaged in sectors like metal and wood works and leather products have also reported a better access to financial services when compared to the rest.

This may provide rooms to look into why these MSEs failed to access loan services or as to what was wrong with the system. There are some enterprises complaining about the existing system, for instituting a number of different criteria on borrowers to be eligible for the service including enterprises' obligation to save about 20 % of their revenue to be eligible for borrowing from micro financial institutions.

3.4 Entrepreneurial and Business Skills

A low level of technical and business skills could prevent motivated entrepreneurs from starting a new venture (Vesper, 1990; Davidsson, 1991). Similarly, unless entrepreneurs are well equipped with technical and business skills, they may not be able to overcome various problems they encounter at different stages of their business development. Some research evidence has shown that successful entrepreneurs can be developed through educational and short-term training programs (McClelland & Winter, 1969; Management Systems International, 1990).

Data collected on availability and type of training show that still many of them had not received any of it so far. Table 7 presents the degree of training requirements by the surveyed enterprises and the percentage trainings which are actually given to them. When compared to other types of supports needed and given training needs greatly coincide with the percentage provided or even at some sectors surpassing the need of the enterprises as the figures show. Nonetheless, exceptionally the construction sector and the metal and wood works sub sector again show a huge gap of demand when compared to the supply side. Only 17% of the respondent enterprises acquired what they needed. Also from respondent enterprises engaged in metal and wood works only 21% have obtained the training the needed.

Table 7 Access to Entrepreneurial & Business Skill Development from Woredas' Micro Finance Institution

| Sectors/ Sub-sectors | Count and percent | Access to financial services form Woredas' Micro Finance Institutions | | Total |
|----------------------|-------------------|---|---|-------|
| | | Number of enterprises who availed entrepreneurial & business skill development services | Number of enterprises who haven't availed entrepreneurial & business skill development services | |
| Construction | Count | 5 | 25 | 30 |

| | | | | |
|--------------------------|-------|-----|-----|-----|
| | % | 17% | 83% | 100 |
| Textile & Garment | Count | 7 | 7 | 14 |
| | % | 50% | 50% | 100 |
| Metal & Wood Works | Count | 3 | 11 | 14 |
| | % | 21% | 79% | 100 |
| Leather Products | Count | 8 | 6 | 14 |
| | % | 57% | 43% | 100 |
| Shoe Making | Count | 7 | 7 | 14 |
| | % | 50% | 50% | 100 |
| Processed & Packed Foods | Count | 5 | 9 | 14 |
| | % | 36% | 64% | 100 |

Beyond these figures the respondents also commented that the trainings are scheduled without any consideration for their work time. They also suggested about the quality of the trainings for being too elementary for them and advocating that they need more advanced trainings. The surveyed enterprises also noted that the trainings seem to be given not to develop their skills and knowledge but only done pretentiously.

The officials interviewed tell that the needs of SMEs is assessed through TVET institutions found in each district/woreda since they have the technical ability to identify the capacity gaps of the enterprises. Their financial need is also assessed by local Micro Finance Institutions at woreda level. Hence, this kind of administrative system implies that the structure and procedures in place are directed to support SMEs development. However, the results of the questionnaires differ from what the interviewees have said. As depicted on the charts found at chapter three the demand for supports and the supplies provided have gaps in both ways i.e. enterprises get a certain type of support while their need for that specific assistance is little and the vice versa although some type of supports are equivalent with the needs.

3.5 Linkages and Networks

Entrepreneurs spend nearly half of their time during their start-up phase in making contacts and networks with other entrepreneurs and related agencies (Aldrich, 1986). Therefore, networks are useful mechanisms to enhance business capability of entrepreneurs. Networks provide four

essential ingredients to entrepreneurship (Manning, Birley, & Norburn, 1989): support and motivation; examples and role models, expert opinion and counseling and access to opportunities, information and resources. The forms of network include trade fairs, entrepreneurial fairs, associations and clubs. Formal institutions specifically government organs’ coordination is important for entrepreneurship development and is necessary to ensure the prompt and effective delivery of services to the entrepreneur. In this research SMEs relation with government institutions is diagnosed by focusing on two basic institutional linkages which are the coordination with research and training institutions and the market linkage.

A. SMEs Linkage with TVET and Research Institutions

Subsidies for research and development are also important for entrepreneurs (Goodman, Meany, & Pate, 1992). Certain infrastructural elements like the existence of universities and research and development programs seem to make substantial impact on the entrepreneurial environment (Bruno & Tyebjee, 1982; Gartner, 1985).

Table 8 Are Relationships facilitated to cooperate with TVET institutions and research centers?

| Response | Construction | Textile & Garment | Metal & Wood works | Leather products | Shoe making | Food processing |
|----------|--------------|-------------------|--------------------|------------------|-------------|-----------------|
| Yes | 27% | 64% | 79% | 57% | 21% | 71% |
| No | 73% | 36% | 21% | 43% | 79% | 29% |
| Total | 100% | 100% | 100% | 100% | 100% | 100% |

As depicted in Table 8 above most of the enterprises conveyed that they have relationships with TVET institutions. However, 73% of respondents from the construction sector have no cooperation with educational or research institutions. This case is even greater when we come to shoe making enterprises that 79% of them have no relationship established with such kind of institutions. Respondents also stated that the only area of cooperation with these institutions is training. The trainings provided by the agency & its representative Woreda MSE bureaus mostly focus on technical skill development. There are also trainings focusing on developing business management skills. Kaizen, bookkeeping, business plan preparation are included under this category. Nonetheless, the respondents haven’t forwarded their views on why such kind of

cooperation is not established between them and TVET or research centers. The surveyed enterprises have also commented on the trainings given by TVET institutions. They noted that the trainings are elementary that they wouldn't add any value for them. A number of respondents also noted that certain trainings are even given once every three months.

As per the discussion above the SMEs have linkage with TVET institutions only on the area of trainings which are even rated as poor by the enterprises. However, these institutions should serve to be the centers of technological transformation and change. Besides, no enterprise has mentioned its relation to a research center. Again these centers can play a great role by designing projects that can bring better products or production systems.

B. SMEs' Market Linkage

Entrepreneurs need support services in addition to financial assistance. In particular, entrepreneurs need most assistance in conducting market studies, in preparing business plans, and in getting loans.

Local Market Linkages

The access and facilitation of local market opportunity is also a critical condition for the success of an enterprise. Results from the questionnaires distributed indicate that the enterprises access their local customers through different ways. For enterprises of construction sector a government entity i.e the Housing Development Agency is their key customer which consumes their products. But for manufacturing sub sectors the enterprises directly hunt customers using a door to door search or they may give their products to wholesalers which in turn retail the products for profit. As noted by the responding enterprises the other way to get a local market is using Bazars organized by different bodies.

Foreign Market Linkages

Table 9 Has there been any linkage created to supply your products for foreign market?

| Response | Construction | Textile & Garment | Metal & Wood works | Leather products | Shoe making | Food processing |
|----------|--------------|-------------------|--------------------|------------------|-------------|-----------------|
| Yes | - | - | 7% | - | - | 14% |

| | | | | | | |
|---------|------|------|------|------|------|------|
| No | 100% | 100% | 93% | 100% | 100% | 64% |
| Missing | - | - | - | - | - | 22% |
| Total | 100% | 100% | 100% | 100% | 100% | 100% |

Table 10 Reasons behind not supplying products for foreign market

| Reasons | Construction | Textile & Garment | Metal & Wood Works | Leather Products | Shoe Making | Food Processing |
|---|--------------|-------------------|--------------------|------------------|-------------|-----------------|
| My products are not competent in the foreign market | - | 2 | 2 | | | 4 |
| Unavailability of access/opportunity | 27 | 5 | 5 | 11 | 13 | 2 |
| Lack of information about foreign market demands | - | 3 | 3 | 6 | 8 | 1 |
| Capacity gaps | - | 1 | 1 | | | - |
| Never thought of exporting my products | - | 4 | 6 | | | 1 |
| Missing | 4 | 1 | 1 | | | 6 |

In their study of the Czech and Slovak entrepreneurs, (Swanson & Webster, 1992) found that many entrepreneurs need better information services, especially in rural areas, including data on the foreign sector.

Foreign market linkages haven't been facilitated for almost all enterprises surveyed. The case of the enterprises from metal and wood works has a slight difference from the rest since 7% of them have access for foreign market. Most of enterprises have identified inaccessibility of opportunity and lack of information about foreign market demands as the major justifications for not exporting their items to international markets. Critical number of respondents from textile and metal sub sectors also noted that they have never thought of exporting their products.

Enterprises cannot be successful without having a market access. There are certain facilitations made in order for them to have potential local markets through organizing bazaars and also preparing market centers at lower rent prices. However, the foreign market linkage is almost not present. Most of the enterprises put the lack of access or opportunity as a justification for not exporting their items to international markets. Officials who are interviewed also told that there is no direct involvement of the SME development bureaus to supply their products to foreign markets rather they give a technical advice and also disseminate information about the procedures of exporting a product to a foreign market.

Chapter 4

4 Summary of the Findings, Conclusion and Recommendation

4.1 Major Findings

1. There isn't comprehensive and detailed policy document designed to promote entrepreneurship development. The subject of entrepreneurship development is reflected on various policies of the nation like the education policy, science and technology policy and the industry policy.
2. The government has tried to minimize various procedures and red tapes involved through a one stop shop services that are provided in every Woreda enabling entrepreneurs to access all the services needed to create a new venture.
3. Survey results show a high fluctuation and inconsistent figures between the supports supplied and demanded assistances with one being extremely higher or lower than the other.
4. The enterprises' attitude towards the services delivered, their expectation and responses to the questions forwarded various with the sectors they are engaged in.
5. The major consumers of the enterprises' products are house holders and retailers rather than higher or medium industries.
6. The only area of coordination between SMEs and TVET institutions is through the provision of trainings which the SMEs view as insignificant to upgrade or improve their skills.
7. It is also observed that there is no formal feedback mechanism in place to evaluate the effectiveness of the services provided to SMEs other than seasonal reports of local woreda bureaus. However closet to a formal evaluation process is the occasional surprise visits of selected SMEs.

4.2 Conclusion

As the results of this study revealed, there are certain areas that need attention and action from all concerned organs to improve the institutional environment that lets entrepreneurs grow. The research findings indicate that though there is no single policy or guideline to develop entrepreneurship, the strategy and procedures in place to develop SMEs are highly

supportive for the formation and growth of SMEs. However, their implementation is still poorly administered. The research has found out that there is a weak hierarchical link between Woreda officials and sub city bureaus. The study has also reach into conclusion that there is a problem in responding to the needs of SMEs.

The lack of coordination among various stakeholders also imply the fact that there is a weak or non-existent relation between the SMEs and other institutions like industries and educational and research centers. The fact that there is no formal feedback mechanism through with enterprises let SME development bureaus know their problem implies the lack of participation and involvement on their own wellbeing and development.

Therefore, all the responsible government organs have to address the above constraints and respond to the discontent of SMEs in order to develop entrepreneurship. Unless remedial measures are taken by coordinating with different entities that have a stake in entrepreneurship growth and development, the present institutional framework might not bring the change expected in the area.

4.3 Recommendations

A clear and comprehensive policy direction that specifically deals with the development of entrepreneurship in the country should be in place. The kind of policy environment can create a vivid image towards entrepreneurship development. It also creates an environment that lets entrepreneurs can survive and grow.

A proper system that will assess the needs of SMEs systematically and periodically shall be designed. Besides, the type of support to be given to different types of SMEs shall be studied. It is necessary to have a constant dialogue with entrepreneurs. Better ideas on how to support SMEs will emerge when agencies involved in supporting SMEs have an open mind to the suggestions of entrepreneurs. A formal feedback mechanism that crosschecks whether the needs of SMEs are properly fulfilled or not shall also be in place. The current system provides no place for accountability and transparency since FeMSEDA receives feedbacks of local Woreda officials. However a way for SMEs to provide their feedback should be arranged.

An institutional framework that can bring an efficient coordination of different institutions that take part in the development of small and micro enterprises shall be organized. One way of creating linkage can be the system of value chain management which enables to have an input-output relationship between different SMEs where one produces an input for the other. Educational and research institutes can also not only introduce but also exchange technologies and technical expertise with SMEs. Different government bodies working on this matter should consolidate their assistances. Continued interaction among the different agencies and entrepreneurs often leads to institutional change. Coordination and collaboration are necessary so as to ensure the prompt and effective delivery of support services to the entrepreneur.

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Appendix I Questionnaire for SMEs on “Assessment of Public Institutions’ Framework contributing to Entrepreneurship”

This questionnaire is designed for an academic research conducted in partial fulfillment of the requirement for the Master of Policy and Public Management. Its purpose is to analyze the views of SMEs regarding the policies, procedures and the support provided by MSE development bureaus are whether contributing for entrepreneurship development or not and recommend on how these can be improved. You are politely requested to respond to each question by providing a short answer and/or putting a tick mark in the box of your choice.

Thank you in advance for your cooperation

General Information

1. A. Type of Sector Construction Manufacturing
B. Specific activity your enterprise is involved in _____
C. Stay in business _____ years/months
D. Ownership type Sole proprietorship Partnership
E. Employment created other than members _____
F. Educational background of members
 - 10th/12th grade complete _____
 - Level I, II, III _____
 - Diploma holders _____
2. What are the kinds of assistances supplied by MSE development bureau in your local area? _____

3. What were the assistances you needed and supports supplied by MSE development bureau when you were planning to start your business?
 Loan Work Place Training Other _____

4. Is the assistance sufficient to enable you to be innovative?
 Significantly sufficient Sufficient Somehow sufficient Not Sufficient

5. What do you suggest to be included in the support scheme to enable you develop an entrepreneurial venture? _____

6. What was the most decisive assistance you secured from your MSE development bureau till now? _____
7. Are there any relationship facilitated for your enterprise to cooperative with research centers and TVET institutions? Yes No
If yes, please specify the areas of cooperation and if no, state the reasons

8. For whom do you supply your products for and how do you access your potential customers? _____

9. Has there been any linkage created to supply your products for foreign market?
 Yes No
10. If your answer for #9 is “No” what is the reason?
 My products are not competent in foreign market
 Unavailability of access/opportunity
 Lack of information about foreign market demands
If other, specify _____
11. What is the basic element for you to be an entrepreneur? _____

12. Have you ever added a certain value or new feature or made any modification on your product? Yes No
13. If your answer for #11 is “Yes” please state the kind of modifications you made _____

14. If your answer for #11 is “No” please state the reason(s)
 Lack of proper technical education & skill
 Lack of financial Capita
If other, specify _____

15. Please state any additional comment you would like to state regarding the matter

Appendix II Leading interview questions to be forwarded to FeMSEDA's and local Woreda officials

1. What kind of supports do you provide for SMEs?
2. What is the most challenging task that you've ever encountered in conducting your support schemes?
3. Is the system provided by the Woreda's SMEs development bureau well-structured and can lead the SMEs to be innovative and entrepreneurial?
4. Do you have a system that will assess the need of SMEs?
5. Do you have a feedback mechanism to observe and improve your performances to be responsive to SMEs' needs?
6. What are the criteria used to upgrade SMEs to a higher level enterprises?
7. Do you have a mechanism that facilitates foreign market access for SMEs?

Declaration

Student ID: GSE/0634/06

I declare that this Research Report on **‘Assessing Institutional Frameworks Contributing to Entrepreneurship Development: The Case of Selected Woredas of Kolfe Keraniyo, Lideta and Gulelle Sub Cities’** is my own original work with assistances and guidance from my Advisor and not submitted before for any institution and any purpose. I further declare that all the sources used in this research report have been properly recognized and acknowledged as in-text-citation and reference list.

Tigiste Deresse Gebre

Signature

Date