

POLICY AND REGULATORY CHALLENGES MILITATING AGAINST THE DEVELOPMENT OF YOUTH-OWNED MICRO- AND SMALL-ENTERPRISES IN ETHIOPIA

Wolday Amhaa^{*} and *Tassew Woldehanna*^{**}

Abstract

The study investigated the policy and business constraints influencing the growth and expansion of youth-owned Micro- and Small-Enterprises (MSEs) using mainly descriptive statistics and the econometrics framework of the Logit model on 909 youth-owned sample MSEs in Ethiopia. The findings showed that high collateral requirement of finance providers was a very severe problem constraining the growth of youth-owned MSEs, followed by limited access to credit, lack of business premise, lack of business support services, frequent interruption of infrastructure services (such as, telecom, power, and water), and lack of raw material inputs. However, since the youth-owned MSEs have heterogeneous characteristics, they are affected differently by the policy and business constraints. As per the econometric results, tax rate and administration, corruption, labour law, and licensing were found to be insignificant constraints influencing the growth of youth-owned MSEs. Although lack of access to finance and shortage of capital were identified as key challenges, they were found to be insignificant variables in influencing the growth of youth-owned MSEs. Policy predictability was found to have a positive and significant effect on growth of youth-owned MSEs. On the other hand, lack of marketing space for products and lack of business support services were found to have negative and significant effects on growth and expansion of MSEs. Owners attributes (household size, age and education), type of ownership structure and the sector the respondents engaged in were found to have a strong positive effect on the growth of youth-owned MSEs. Moreover, sole owners of MSEs were found to have higher likelihood of growth in employments. Contrary to the researchers' expectation, type of enterprise (micro or small enterprises) was found to have negative effect on the growth of MSEs. From the results of the study, it can be concluded that the growth of youth-owned MSEs was affected more by owner and firm attributes than by policy and regulatory constraints.

Keywords: policy and regulatory challenges, development of youth-owned MSEs, Ethiopia

^{*}CEO of the Association of Ethiopian Microfinance Institutions (AEMFI) and Ethiopian Inclusive Finance Training and Research Institute (EIFTRI).

^{**} Professor of Economics, Addis Ababa University.

1. INTRODUCTION

The role of Micro and Small Enterprises (MSEs) in providing employment opportunities and boosting entrepreneurship and innovation has attracted attention of policymakers and other stakeholders. MSEs serve as important sources for job opportunities not only for developing countries but also for developed economies. According to Carter and Jones-Evans (2004) in Gebre-Egziabher and Ayenew (2009), the MSE sector constitutes about 70 per cent of the total employment in EU countries; about 67 per cent in Japan; 62 per cent in US; about 22.3 per cent in China; and about 80 per cent in India. In developing countries, too, the informal sector is the main source of employment, particularly in urban areas. The share of informal employment (outside agriculture) to the total non-agricultural employment accounts for about 72% in sub-Saharan African countries (ILO 2002).

One of the essential elements of economic growth in developing economies is the dynamism of the private sector (particularly the MSE sub-sector), the performance of which is influenced by the policy, legal, institutional and regulatory frameworks. The removal of institutional obstacles to MSE might be a low-cost way of supporting the growth of MSEs. The key factors that positively contribute to the growth of MSEs include: (a) policy, regulatory and legal environment that is simple, fast, inexpensive and free from corruption; (b) finance that is accessible at low cost and does not require providing physical collateral; (c) access to affordable business development services; workers who are trained in appropriate skills, including basic health and education that strengthens human capital; (d) culture that supports and rewards entrepreneurship; (e) access to domestic and global markets on a fair and equal basis with large enterprises; and (f) reliable infrastructure (transport, energy, telecommunications, water, etc.) ILO (2002).

Regulatory challenges and underdeveloped institutions frequently entail a disproportionate burden on smaller businesses because larger firms are better able to manoeuvre around obstacles or cope with the high fixed costs they impose (Tybout 2000). According to De Soto (1989), strict regulations and high taxes may keep firms small and informal, thereby contributing to increased transaction costs from problematic property right protection and contract enforcement. In the Ethiopian context, with the objective of promoting investment, large firms are exempted from import duties on capital and benefit from other subsidies while small firms are denied similar support. Furthermore, some government policies that actually aim to benefit MSEs may provide disincentives. For example, India offers attractive incentives to small enterprises, but by some accounts, these measures backfire because growth beyond a specified level entails losing valuable benefits (Mitra and Pingali 1999). Since the manufacture of certain products in India is restricted for small firms, some owners even split up their MSEs into several enterprises in an effort to make them look smaller (Kashyap 1988).

The regulatory and institutional environment is burdensome in developing countries compared to developed countries and usually hinders the growth of small enterprises (Nuwagaba and Nzewi 2013). Liedholm (2002) argued that small firms may also be restricted from making growth-enabling investments due to the existing institutional and regulatory challenges. Moreover, import duties on capital equipment may disproportionately hurt MSEs while larger firms can simply bypass these duties by qualifying for investment incentives.

The availability of favourable legal frameworks, such as: (i) well-entrenched property rights; (ii) efficient business registration procedures; (iii) simple and transparent rules for operations; (iv) supportive taxation; (v) effective and cost-efficient contract enforcement; (vi) streamlined systems of arbitration and dispute resolution; and (vii) effective law enforcement and crime prevention, reduces the transaction cost of MSE operators. In other words, any intervention to promote MSEs should begin with a systemic overhaul of the legal framework. Moreover, having the right legal framework may have very little consequence if there is inefficient judiciary system, which fails to implement the legal framework. Hubner (2000) identified six fundamental barriers to the development of small and medium enterprises in central Asia: 1) burden and complexity of taxes; 2) difficulties in receiving licenses and permits for standing and developing own business; 3) excessive direct intervention by officials in business operation and the multi-layer corruption surrounding the business; 4) difficulty of obtaining adequate credit to set up and develop business; 5) insufficient knowledge of business and market economy rules by entrepreneurs; and 6) difficulty of accessing business information.

Ghanem (2013), in his study on MSEs development in Egypt, suggested the need for regulatory and institutional reforms in order to create a conducive business environment for small business, and implementing tailored interventions to support small enterprises and develop youth entrepreneurship. Joumard *et al.* (1992) revealed that the MSEs in Niger and Swaziland did not consider taxation and other regulations as the main hindrance to growth rather a lack of demand and/or difficulties in obtaining financing or raw materials, which were often the main constraints faced by the MSE operators. They also found that the regulatory environment, for most, is only a minor determinant of their economic viability though important for a few enterprises at particular stages in their life cycle. The results of Ishengoma and Kappel (2008) study indicated that investment obstacles, limited access to market and productive resources, and high tax as the key factors hindering the growth potential of MSEs in Ghana.

World Bank (2014) has identified a number of challenges in doing business in Ethiopia. As per the report, the country's rank in "doing business indicator" declined from 124th in 2013 to 125th in 2014. With regard to starting business in the country, Ethiopia's rank dropped from 162nd in 2013 to 166th, out of 189 in 2014. The cost of starting business in terms of per

cent of income per capita (100.1) was higher compared to Sub-Saharan Africa average, which was 67.4% (World Bank 2014). In other words, improving the licensing and tax regimes, reducing the cost of registration and licensing, and streamlining the procedures will have direct impact on the expansion of small businesses.

Putting in place the right enabling policies, strategies and regulatory frameworks will have a positive impact on competition, production and productivity of MSEs. On the other hand, Gebrehiwot and Wolday (2004) argued that creating the enabling policy environment alone is not enough to bring about the expected optimal results in Ethiopia; the degree to which MSEs can improve themselves by having access to support services, such as skill, technology, finance, infrastructure and market is also important. Unlike many other studies which focused on the overall challenges of MSEs, this study attempted to investigate the perception of youth MSE-owners on changes in the policy environment and assess how government institutions, policies, strategies and regulatory frameworks influence the growth and expansion of youth-owned MSEs.

1.1 Objectives of the Study

The overall objective of this study was to investigate the institutions, policies, strategies and business constraints and government support services in Ethiopia that influence growth and expansion of youth-owned MSEs. The specific objectives were to:

- (i) review the key policies, strategies, and government support services directly related with the development of youth-owned MSEs;
- (ii) assess the institutional, policy and regulatory constraints affecting the growth and expansion of youth-owned MSEs;
- (iii) investigate how the institutional, policy and regulatory constraints and other attributes influence employment growth of youth-owned MSEs; and
- (iv) identify the key challenges of youth-owned MSEs and the policy implications thereof.

1.2 Methods of Data Collection

Using stratified simple random sampling technique, 909 youth-owned MSEs were selected. Those MSEs were drawn from five regional states (Oromia, Amhara, SNNPR, Tigray and Harari), and two city administrations (Addis Ababa and Dire Dawa), where more than 95% of the MSEs in Ethiopia are found. Since the focus of the study was to understand the performance and challenges of the youth in starting new business and managing existing firms, attempts were made to stratify the sample by size (micro and small enterprises), sex of owner (male and female owners), and enterprise activities (manufacturing, construction,

urban agriculture, service, trade, etc). The sampled MSEs-owner youths were interviewed (between June 23, 2014 and August 15, 2014) using structured questionnaire. Out of the total sample of existing youth-owned MSEs, 543 were microenterprises, while the remaining 366 were small enterprises. To adequately understand and study the gender dimension, 153 and 57 women owners were sampled from micro and small enterprise categories, respectively. On the other hand, given the limited sample size and to reduce the possibility of taking higher number of enterprises in specific sectors, attempts were made to take proportional samples from the different sub-sectors. Out of the total 909 enterprises, metal and woodwork accounted for 28.7% of the sample size, followed by construction (19.5%), service (10%), trade (9.8%), urban agriculture (9.5%), food and food products (7.8%), textile and clothing (6.3%), leather and leather products (1.4%) and others (7.2%). The quantitative analysis was complemented by qualitative information from Yisak (2015).

1.3 Organization of the Paper

This paper is organised into three sections. Following from the introduction and objectives presented in Section 1, Section 2 reviews the policies and strategies designed and implemented in Ethiopia by the three subsequent regimes (the Imperial regime, Derg and the incumbent government). Section 3 analyses the perception of the MSE-owner youths on the institutional and policy constraints and the impact of the policy changes and government support programs on the growth of youth-owned MSEs. Section 4 examines the effect of the policy constraints on growth and expansion of youth-owned MSEs. The final section summarizes the key findings of the study and policy implications.

2. POLICIES AND STRATEGIES TO SUPPORT THE DEVELOPMENT OF MICRO- AND SMALL ENTERPRISES IN ETHIOPIA

Prior to 1974, there were limited attempts to support the development of MSEs in Ethiopia. According to Teshome (1994), the Imperial government made some efforts to establish the basic administrative and infrastructure in order to consolidate and accelerate the gains of reforms and process of industrialisation in 1940's and 1950's, where some initiatives related to the development of MSEs were implemented. The Investment Proclamation No. 242/1966 provided MSE's tax relief, access to land and buildings, public utilities and others to facilitate advisory and administrative issues. In line with the socialist ideology, the policies and regulations of the Derg regime (1974 to 1991) were aimed at curtailing or entirely destroying the private sector in Ethiopia by nationalising private businesses. Proclamation No.26/ 1975 gave the government the power to control all the means of production or the 'commanding heights' of the economy, and crippled the nascent private sector in the country. For example, according to the

Proclamation, acquisition of private businesses was restricted to a single license and capital ceiling set at 300,000 Birr for wholesale trade, 200,000 Birr for retail trade and 500,000 Birr for industrial establishments. On the other hand, the Derg regime established the Handicrafts and Small Scale Industries Development Agency (HASIDA) by Proclamation No. 125/1977¹ with the objective of boosting the development of the public economy by encouraging cooperative development in the small-scale industry sector (MUDC 2013).

The Derg regime, on its verge of collapse (1989–90), forced by external and internal factors recognised the importance of the private sector in the economic development of the country and introduced a mixed economy system of economic governance. To this end, it issued Decree No. 9/1989 which allowed the establishment of small-scale enterprises by business organizations, cooperatives and individual entrepreneurs and raised the capital ceiling for small scale enterprises from Birr 500,000 to 2 – 4 million Birr. Moreover, Derg issued Decree No. 1990, which lifted the restriction of private sector participation to single license and allowed individuals to undertake investment in unlimited number of enterprises (MUDC 2013).

Following the overthrow of the Derg regime in 1991, the incumbent government launched public sector reform, which focused on market and private sector development. Many of the macroeconomic reforms and restructuring efforts of the new government had direct or indirect influence on the development of MSEs. The broad policy framework of the government, “Agricultural Development Led Industrialization (ADLI) (1995)”, considers the private sector as the engine of growth, where MSEs were identified as instruments to create and expand the private sector. This was clearly indicated in the national MSE strategy issued in 1997, which was operationalised through the establishment of MSE development offices at federal and regional levels. The Industrial Development Strategy issued in 2003 also recognised the expansion of MSEs as an important instrument to promote private sector and entrepreneurship by providing infrastructure support (working premises and land), financial facilities, access to supply of raw materials, markets, and training among others.

The MSE strategy of 1997 mainly focused on creating conducive policy, legal, and institutional environments and other support programs, which promote the development of MSEs and address the structural problems constraining MSEs efforts in creating employment and contributing to the macroeconomic development of the country. The specific objectives of the Strategy include: (i) facilitating economic growth and bringing equitable development; (ii) creating long-term jobs; (iii) strengthening cooperation between MSEs; (iv) providing the basis for medium- and large-scale enterprises; (v) promoting export; and (vi) extending balanced preferential support to MSEs and large enterprises. Although the strategy had clear intentions to support MSEs, there were no institutional mechanisms,

earmarked resources and commitment to implement the strategy at all levels.

The five year (2005/06 – 2009/10) Plan for Accelerated and Sustained Development to End Poverty (PASDEP) also identified the development of MSEs as one of the venues for job creation and mitigating the pervasive youth unemployment observed in the country by supporting MSEs through the provision of basic technical training, upgraded business development services and enhanced market linkages. Similar to PASDEP, the Growth and Transformation Plan (GTP (2010–2015) gave due attention to MSEs and identified their development as one of the seven pillars of growth in order to ensure economic growth and transformation in the country.

The five-year MSE Development Strategy (2010/11–2014/15) was designed to complement GTP I in order to expand employment opportunities and lay the foundation for private sector development in Ethiopia. To this end, the federal government allocated huge budgetary resources to provide package of support services, such as providing working and marketing premises, building the capacity of MSEs through the provision of technical and management training, industrial extension, market linkages, technology transfer, and extending loans and other financial services through one-stop-service-centres. On top of providing incentives and support services depending on their stage of development (start-up, the growth stage and maturity phase), the MSE Development Strategy included assistance to fresh band of target groups, such as graduates from universities and TVETs, by developing the technical skills and innovation of the youth, changing their attitude and mindset towards blue collar jobs and self-employment and improving their culture of saving. As a result of government commitment to support MSEs, there had been phenomenal growth in the youth employment and number of MSEs and demand for the products of MSEs in the last five years (FeMSEDA 2014). The initiatives of governments at various levels have also created the foundation for the development of MSEs and medium enterprises. Despite the success in implementing the MSE Development Strategy, there are institutional, policy and regulatory constraints, which limit the expansion and performance of youth-owned MSEs.

3. PERCEPTION OF MSE-OWNER YOUTHS ON POLICY AND INSTITUTIONAL CONSTRAINTS AND THE IMPACT OF THE GOVERNMENT SUPPORT PROGRAMS

This section focuses on the profile of youth-owned MSEs and the perception of youth MSE owners on policy and institutional constraints. Attempts were also made to assess the changes and impact of the government support programs on the growth of the respondents. It uses descriptive statistics to analyse the characteristics of the MSE owner youths, the business environment and policy predictability, which could

assist policymakers and development partners in refining the interventions and support services required by the operators.

3.1 Profile of Sample Youth MSE Owners

As shown in Table 1, about 60% of the sample respondents were engaged in microenterprises, while the rest 40% were small enterprises². Male youth operators dominate the sample survey, where about 40% were male-owned enterprises, followed by mixed owners (37%), and female owners (23%). About 55% of the youth MSE owners were married while about 41% of the firm owners were single. Moreover, most of the sample MSE operators were engaged in metal and woodwork, followed by construction, services and trade sub-sectors. On the other hand, female-owned MSEs were mainly engaged in trade activities, followed by service sector.

A significant proportion of youth MSE owners (54%) had at least some high school education, while a good proportion (26%) attended primary education and about 17% attended higher education (schooling above Grade 12). Regarding the ownership type of the enterprises, about 42% of the respondents were organised as sole proprietorship, followed by partnership (28%), cooperative form of business organizations (25%), PLCs (3%) and share company (2%). As most of the microenterprises tend to operate on informal basis or as a sole proprietorship, it is difficult to make separation between finances of the owners and the households (Gebrehiwot and Wolday 2004)³. The evidence from the current study seems to support this argument, where significant proportion of the microenterprises (57%), organised in the form of sole business, is higher compared to small enterprise category (21%).

The literature on entrepreneurship reveals that the growth and performance of an MSE is related with the owners' motivation and aspiration in starting a business. If the owners' motivation to establish a business is to be self-employed (believing that he/she has the capability to capture the opportunities), there is a higher probability of growth and performance compared to an individual who starts a business out of necessity or meet her/his household's subsistence needs. In this study, respondents were asked why they were engaged in the specific business. The findings of the study in Table 2 show that the majority of the youth started their own business expecting higher profit and income in self-employment in a short-span of time. Having the capability and the skill to start new business was the second reason of the sample youth-owned MSE operators to engage in self-employment. The initial capital matching with the new business, motivated to start a dream job; and the influence of parents/relatives was equally an important reason for the respondents to start their own business.

Table 1. Profile of sample youth-owned MSEs

Characteristics	N	%	
Owner-Gender	Female	210	23.10
	Male	363	39.93
	Mixed	336	36.96
Type of enterprise	Micro	543	59.74
	Small	366	40.26
	Married	504	55.45
Marital status	Single	375	41.25
	Divorced	22	2.42
	Widowed	8	0.88
	Food and food products	71	7.81
Sector	Metal and wood work	261	28.71
	Leather and leather products	13	1.43
	Textile and clothing	56	6.16
	Construction	177	19.47
	Urban agriculture	86	9.46
	Trade	89	9.79
	Services	91	10.01
	Others	65	7.15
	None	21	2.31
	Education	Lower primary	39
Upper primary		199	21.89
High school		493	54.24
Above 12		157	17.27
Ownership type	Sole proprietorship	383	42.13
	Partnership	258	28.38
	Private Limited (PLC)	29	3.19
	Cooperative Company	223	24.53
	Share company	14	1.54
Other	2	0.22	

SOURCE: AEMFI, Survey on Youth-owned MSEs in Ethiopia (2014)

There were also youth MSE operators who indicated that they were forced to start their own business because they lacked other options (necessity-driven). In terms of gender, the proportions of respondents attracted to start their own business expecting quick return and skill considerations was higher for male respondents compared to female enterprise owners (Table 2). Besides, lack of other alternative options was cited by female-owned enterprises as the third reason to engage in self-employment, indicating that significant number of women involved in self-employment in order to meet their subsistence needs. Very limited proportion of the respondents reported that the existence of little or no regulatory requirement in the MSE sector encouraged them to be self-employed.

Table 2. Reasons of youth MSE owners to engage in self-employment (%)*

Reasons	Micro	Small	Female-owned	Male-owned	Total
Skilled in this activity	66.67	50.00	50.48	76.86	59.96
Parents/relatives in this business	26.70	25.96	21.90	27.82	26.40
Thought it would be profitable	82.69	81.69	77.14	83.47	82.29
Capital requirement matches with what I had	33.70	23.77	31.43	36.36	29.70
Little/ no regulatory restrictions to get into this line of business	13.26	13.39	14.29	11.85	13.31
I had no alternative	29.65	25.68	32.38	27.00	28.05
Other people's advice	24.68	28.14	22.38	22.59	26.07
It was my preference (dream)	33.15	21.04	20.00	33.06	28.27
Related with my level education	14.92	11.75	7.14	18.18	13.64
Others	1.66	3.01	4.76	0.28	2.20

SOURCE: AEMFI, Survey on Youth-owned MSEs in Ethiopia (2014)

*The per cent figures do not add up to 100% because the respondents were allowed to give multiple responses.

Owners of MSEs with higher years of experience before starting business have relatively faster growth than those without experience. The empirical study of Mead and Liedhold (1998) found that Kenyan entrepreneurs with at least seven years of experience expanded their firms more rapidly than those without such experience. The results from the current study showed that about 34% of the respondents had experience or apprenticeship in similar business before starting business, while about 52% of the operators had general business experiences. When the respondents were asked on the type of activities they were engaged in before the current business, about 51% reported that they were engaged as owners of business in any related or unrelated activities, wage-employed by others or apprenticeship. On the other hand, while about 21% of the respondents in school before starting their own business, about 8% had never been employed; and about 3% were employed in the public sector. Moreover, of those who reported that they had business experience, about 82% reported that the experiences they gained before starting their business were helpful for their current business.

About 97% of the respondents reported that they started their business from scratch. Less than 3% of the respondents acquired their business through inheritance and purchase. Moreover, about 70% of the sample youth MSE owners revealed that the primary source of funding for investment was obtained from own savings or retained earnings. When those who responded that they started their business from scratch were asked on why they started their own business, about 37% preferred to work for themselves than being employed as wage earners, while about 28% and

26% believed that small business provides better opportunities and had no better option, respectively. Regarding the issue of cooperation among enterprises, about two-thirds of the sample youth MSE owners reported that they had no networking or cooperation experiences.

3.2 Perception of the MSE Owners on Government Support Services, Policy Changes and Impact

Enabling institutional, policy and regulatory reforms are expected to have a positive impact on competition, production and productivity of MSEs. On the other hand, Gebrehiwot and Wolday (2004) argued that putting an enabling policy and regulatory environment alone is not sufficient enough to bring about the expected optimal results; the degree to which MSEs can improve themselves by having access to support services such as skill, technology, finance, infrastructure and markets is also important. Although the government implemented the first five-year MSE development strategy (2010/11– 2014/15) to extend institutional support services (including access to finance, providing marketing and production premises, market linkages, skill training, and industrial extension), the results of this survey indicated that availabilities and quality of the support services weren't satisfactory (Table 3). Only 30% of the respondents reported that they received support services from government and training providers and about 19% accessed the financial services of MFIs. Although the roles of donors and NGOs were relatively limited, about 12% revealed that they received support services from donors and from international and local NGOs.

Table 3. MSEs (%) receiving institutional support from diverse stakeholders

Support service providers	Yes	No
Donors	3.3	96.7
International NGOs	6.38	93.62
Local NGOs	2.42	97.58
Government projects/institutions	30.03	69.97
Training providers	30.36	69.64
Banks	1.32	98.68
MFIs	19.36	80.64
Cooperatives	1.43	98.57
Business Associations	1.65	98.35
Other institutions	1.32	98.68

SOURCE: AEMFI, Survey on Youth-owned MSEs in Ethiopia (2014)

The respondents were asked to identify the support services they received from government and assess the quality of the services. The survey findings in Table 4 show that about 42.8 % of the respondents accessed technical training. About 19.8%, 40.1% and 20.8% of the MSE owner youths rated the quality of the training sessions as very good, good, and satisfactory,

respectively. About 15% of the respondents reported that the quality of the training was inadequate and very low. Relatively, higher proportion of the respondents reported that they had access to extension services (30.8%), infrastructure support (power and water) (30.3%), production premises (28.2%), access to credit (24.7%), and business development training (23.4%). However, very limited respondents received technology support (5.6%) and one-stop services (5.7%). On the other hand, with the exception of market linkage to sell their products, the respondents ranked the quality of the services provided by government either as satisfactory or more than satisfactory (very good and good). The quality of the technical training, business development training, and access to production premises were given relatively higher rating compared to the rest of the support services. One-stop services, access to sub-contracting, technology support, market linkages, access to market premises and finance were reported to be of low quality.

Table 4. Access and quality of support services in the last three years

Support services	Access to support services	Quality of support services			
		Very good	Good	Satisfactory	Inadequate and very low
Technical training	42.79	19.79	40.1	20.82	15.42
Business development training	23.43	13.15	38.03	25.82	15.49
Extension services (follow up support services)	30.80	12.14	27.86	29.64	23.93
Production premises	28.16	22.27	28.13	22.66	18.75
Marketing premises	15.40	9.29	21.43	27.86	25.71
Infrastructure support (power and water)	30.25	12	29.09	22.91	26.91
Market linkages to access raw materials	11.44	9.62	23.08	25	27.88
Market linkages to sell your products	15.07	8.03	22.63	27.01	31.39
Access to sub-contracting	11.22	2.94	22.55	16.67	40.2
Technology support	5.61	3.92	25.49	23.53	33.33
Access to finance	24.64	9.82	21.43	28.13	29.91
One stop-shop services	5.72	3.85	17.31	36.54	28.85

SOURCE: AEMFI, Survey on Youth-owned MSEs in Ethiopia (2014)

When the respondents were asked whether they were aware of the five-year MSE development strategy, about 70% confirmed that they know the strategy and the government support services. However, the microenterprise operators were more aware on the strategy compared to small enterprise owners. About 61% of the sample MSE owner youths reported that the policy environment has improved supporting their business. Relatively, higher proportion of small enterprise owners (66%) indicated improvement in policy environment compared to microenterprise owners (57%). A similar survey by Gebrehiwot and Wolday (2004) showed

that about 33% of the MSE operators in Ethiopia reported improvement in the policy environment.

About 57% of the respondents reported improvement in the licensing and registration procedures after the implementation of the five-year MSE development strategy. The proportion of small enterprise owners who indicated improvement in licensing and registration procedures (64%) was slightly higher compared to responses of microenterprise owners (52%). However, compared to a previous survey by Gebrehiwot and Wolday (2004), the proportion of MSE operators who reported improvement in licensing improvement has declined by about 10 percentage points.

The sample MSE-owner youths were asked to identify the changes they observed after the implementation of the five-year MSE development strategy (2010/11– 2014/15). More than half of the respondents reported that investment, support of government, access to finance, domestic competition, infrastructure services and size of the market have improved after the implementation the strategy (Table 5). About 61% of the respondents reported increase in investment (such as, purchase of machinery, equipment, and expansion of working premise) after the implementation of the strategy. The proportion of respondents who perceived improvements in support of government, access to finance, domestic competition, infrastructure services and size of the market were 59%, 57%, 56%,54%, 56%, and 55% respectively. Capital shortage, inadequate business premises, inadequate/uncertain markets, and high taxes and inefficient tax administration were constraints to expand MSEs. Moreover, the respondents reported that policy predictability was quite low.

Improvements in the efficiency of tax administration and competition from imported goods were reported by about 36% and 38% of the respondents, respectively (Table 5). However, about 22% of the respondents revealed that they didn't observe any change in the efficiency of tax administration while about 21% indicated there wasn't any change in the tax rate. Gebrehiwot and Wolday (2004) showed that although there have been attempts by government to liberalise and improve the policy, regulatory and institutional support for MSEs, which resulted in increase in investment and competition and improvement in the licensing procedures, there were divergences between stated policies and directives and the outcomes on the ground.

The qualitative information from private business owners indicated that inefficient tax administration, lengthy process to renew licenses such as evidence of physical address and requiring title deed (if working in his/her homestead) or contract agreement (if the premise is leased), producing competency certificate, and trade name increase the cost of registration and licensing. This encourages small businesses to stay out of the formal economy and squeezes those MSEs that comply with the regulatory requirements. There is a tendency to rush for regulation or overregulation

in Ethiopia in recent years, and that affects the expansion of small businesses. According to the report of bkp Development Research and Consulting (2014) submitted to IFC, the business community in Ethiopia faces a serious challenge due to onerous licensing registration requirements and procedures. For example, there are 36 professional competency-certifying agencies in the country with overlapping mandates. The operations of these agencies are not properly coordinated or synchronised. Compared to international best practices and trends followed in many economies, the business-licensing regime in Ethiopia is unduly prescriptive: it establishes too many and too specific licenses. Moreover, compared to overall compliance costs (800 Birr per license), the total fees of licensing agencies was 8.3%. About 91.7% of the costs for business are the result of cumbersome documentation and other requirements as well as time-consuming procedures (bkp Development Research and Consulting 2014). There is a need to develop a tailored regulatory, licensing and registration system for small businesses in Ethiopia by introducing minimal compliance and reducing administrative cost (such as a simplified tax regime where small businesses pay taxes as per self-assessment and risk-based verification by tax authority). Addressing the regulatory constraints will require revisiting the regulatory and tax regimes and developing a simplified system. This will also require undertaking detailed cost and benefits studies (for the existing regulations and procedures) by focusing on their impacts on the growth of the private sector in general and MSEs in particular. However, there are opportunity costs to be considered in simplifying the procedures for small businesses such as reducing government revenue and abuses by relatively larger firms to take advantage of the incentives and exemptions provided to small businesses.

Table 5. Change observed by MSE operators after the implementation of the MSE development strategy

Changes	Increased a lot	Increased slightly	Decreased a lot	Decreased slightly	No change	NA	Total
Investment	24.09	36.85	1.98	1.10	5.06	30.91	100.00
Competition (imports)	12.32	25.96	2.97	2.42	14.19	42.13	100.00
Competition (domestic)	22.66	33.88	1.43	1.32	9.57	31.13	100.00
Infrastructure	21.89	33.88	2.31	1.76	9.35	30.80	100.00
Support of government	19.03	39.93	2.20	2.09	5.83	30.91	100.00
Access to finance	16.72	40.04	3.41	1.87	7.15	30.80	100.00
Tax rate	17.71	20.02	4.62	1.76	21.67	34.10	100.00
Tax administration	14.74	21.78	4.18	2.64	22.22	34.32	100.00
Size of the market	19.80	35.31	2.97	1.32	9.68	30.91	100.00
Price of product	19.36	28.60	5.39	2.42	12.87	31.35	100.00
Price of input	21.34	28.38	5.39	1.76	11.99	31.13	100.00

SOURCE: AEMFI, Survey on Youth-owned MSEs in Ethiopia (2014)

3.3 Institutional, Policy and Regulatory Constraints Affecting the Expansion of Youth-Owned MSEs

The sample MSE owner youths were asked to identify and rank the severity of the institutional, policy and regulatory constraints affecting the expansion of their businesses, given a four-point scale, ranging from 0 = “no problem” to 4 = “very severe problem”. As shown in Figure 1, high collateral requirements of finance providers were ranked as a very severe problem (by about 44% of the respondents), followed by limited access to credit (34%), lack of access to obtain business premise (33%), lack of business support services (30%), frequent interruption of power, water, telecom, etc. services (22%), and lack of raw material inputs (21%). On the other hand, constraints on free hiring, minimum wage laws, regulation related to consumer and environmental protection and quality control, limits on temporary hiring, and constraints on layoff/dismissal of employees were not considered as serious problems of expanding their businesses.

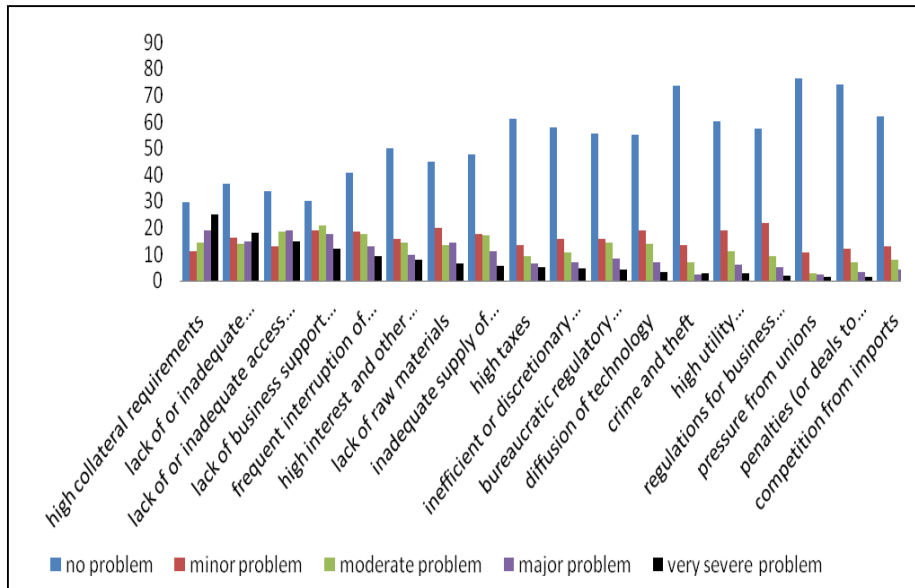


Figure 1. Constraints of MSE operators

The magnitude of institutional, policy and regulatory constraints varied among enterprises such as between microenterprises and small enterprises. The problems of youth MSE-owners may also vary from sector to sector. For example, limited access to long-term capital and lack of operation space are the major obstacles to the growth potential of Ugandan manufacturing MSEs in wood/furniture and metal; but not those in textile (Sengendo *et al.* 2001) and in trade and service sectors. Since MSEs are heterogeneous, assessing the relationship between their growth potential

and policy and business constraints, controlling other factors, is very important. To this end, the data from the survey results on policy and regulatory constraints of youth MSE owners was disaggregated by type of enterprise (Figure 2) and gender of the owners (Figure 3).

The results of the survey showed that high collateral requirements of finance providers (46%), lack of business premises (40%), lack of credit (39%), lack of business support services (34%), and frequent interruption of power, water, and other supplies (23%) were among the top five very severe problems identified by microenterprises. Likewise, high collateral requirements of finance providers (42%), limited access to credit (27%), lack of business premises (23%), lack of business support services (22%), and frequent interruption of power, water, and other supplies (22%) were also among the top severe constraints reported by the small enterprises. Gender wise, except for some order difference, the respondents (both male and female operators) identified similar constraints. For instance, the top three major problems identified both by female and male youth MSE owners included high collateral requirements of finance providers, lack of business premises, and lack of access to credit.

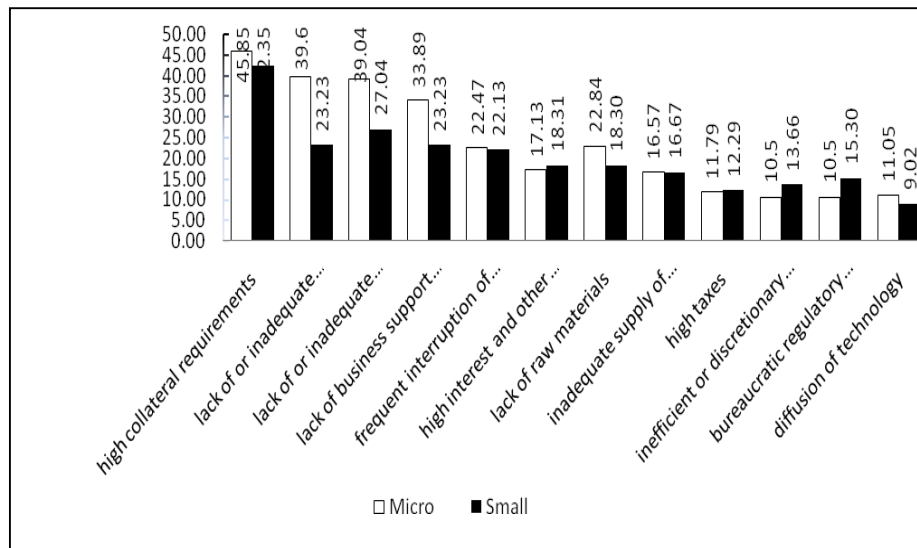


Figure 2. Severe constraints of MSE operators by type of enterprise

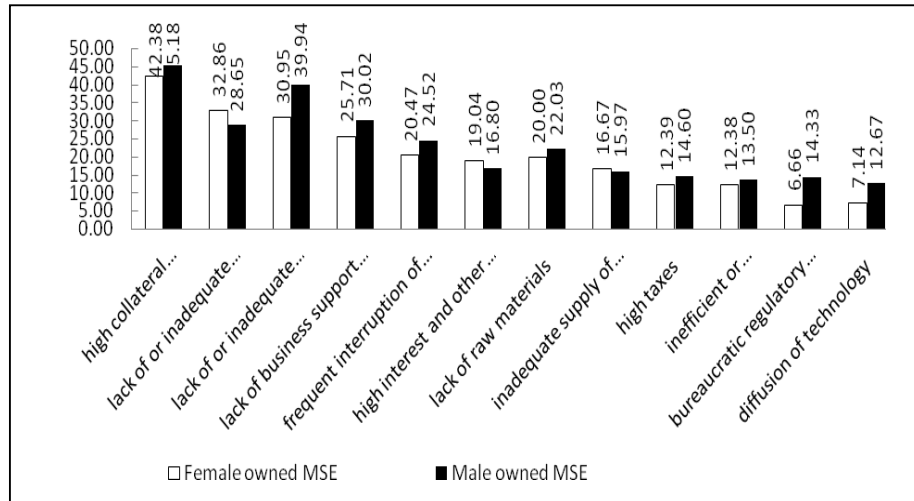


Figure 3. Major and/or severe constraints of MSE operators by gender

Youth MSE operators require a higher degree of policy predictability, particularly with regard to price movement (inflation), interest rates, availability of credit, and the like, which have direct impact on the costs and revenue side of their operations and manage their asset categories appropriately. According to World Bank (2005), smaller firms, reported government policies to be unpredictable; and this uncertainty may yet be another factor reducing growth-enabling investment. The MSE-owner youths were also asked to give their opinion on changes in policy, rule and law. As indicated in Figure 4, about 61.5% of the respondents reported that changes in government policies, rules and laws were predictable. About 35.3%, 17.7% and 8.5% of the MSE-owner youths revealed that the policy/rule changes were fairly, highly and completely predictable, respectively. On the other hand, about 38.5% of the MSE operators in the sample indicated that changes in policies, rules and laws were unpredictable. Moreover, about 15.7%, 8.8% and 13.9% of the respondents reported that the changes in policies or rules were completely, highly and fairly unpredictable, respectively. The findings were similar for small and microenterprises as well as for male-owned and female-owned enterprises. The predictability of policies, rules and laws reported by the youth MSE owners in this survey (61.5%) has shown a significant improvement when we compare the results of a sample survey by Gebrehiwot and Wolday (2004), which was about 34%.

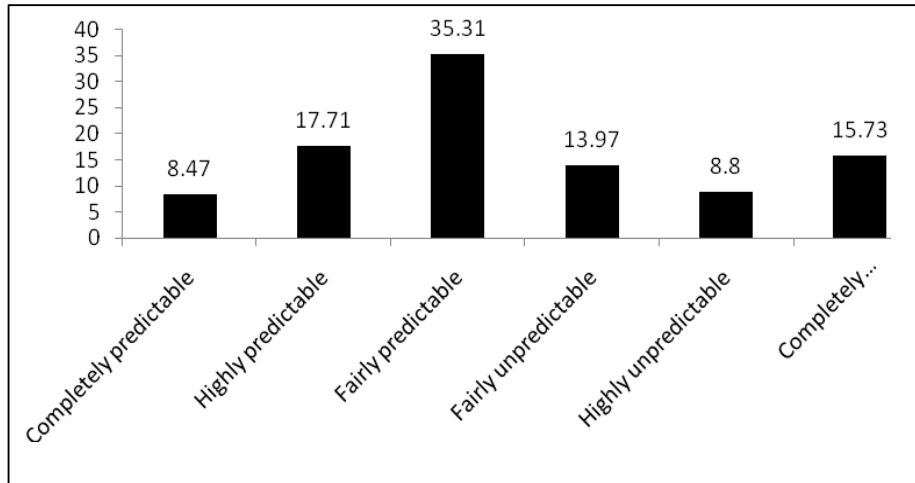


Figure 4. MSE operators perceived degree of predictability to changes in laws, rules and policies

The perception of MSE operators regarding the implementation of the strategies, laws, regulations and policies and the degree of their involvement in the design or planning stage is presented in Figure 5. About 27% of the respondents reported that government seldom or never adhere to the existing laws and/or policies; and about 59% of the sample youth MSE operators reported that they never or seldom participate in the process of designing new policies, rules and regulations. About 22% of the respondents reported that the government sometimes adheres to its laws and policies; and about 19% revealed that they had the opportunity to participate in the drafting of policies, laws and regulations. There is a need to improve the involvement of the MSE operators in designing, implementing, and monitoring strategies, policies, laws and regulations, which will have a direct impact on building the trust or confidence on government and developing a sense of ownership.

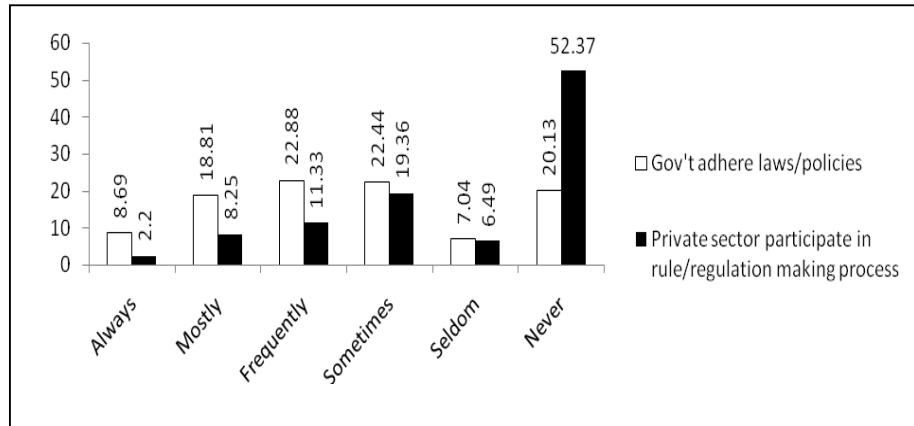


Figure 5. MSE operators' perception about participation and government's adherence to strategies, laws, regulations and policies

Table 6 shows that about 53.2% of the respondents indicated lack/inadequacy of business premises as a main obstacle limiting expansion of their business, followed by interruption of electricity (7.2%), and high tax rate (4.8%). Although lack/inadequacy of business premises was, by far, the main obstacle hampering the growth of youth-owned MSEs, there were some differences when the results of the survey are disaggregated by type of enterprise (micro and small) and gender. For example, access to business premises was relatively a serious challenge to micro enterprises and female-owned enterprises compared to small and male-owned enterprises.

Table 6. Rule/regulation related obstacles reported by MSE operators primarily

Obstacles	Micro	Small	Female-owned	Male-owned	Mixed	Whole sample
Lack of business premises	53.22	41.8	54.29	52.34	41.07	48.62
Interruption of electricity	5.34	9.84	5.71	8.26	6.85	7.15
Tax rate	4.42	5.46	5.71	3.31	5.95	4.84
Corruption	4.05	5.46	0.95	4.13	7.44	4.62
Lack of electricity	3.13	5.46	4.29	2.75	5.36	4.07

SOURCE: AEMFI, Survey on Youth-owned MSE in Ethiopia (2014)

Shortage of capital was reported as the primary obstacle of growth and expansion for about 62.7% of the respondents (Table 7). Inadequate or uncertain output market was reported as the second challenge of expanding business by 18.1% of the respondents, followed by limited access to credit (6.5%) and inadequate business support services (5.2%). The order of the obstacles were found to be consistent even when the data were disaggregated by gender and type of enterprise, except for small enterprises, where inadequate business support services (6.6%) was the third and limited access to credit (5.7) the fourth obstacle.

Table 7. Market-related obstacles reported by MSE operators

Obstacles	Micro	Small	Female-owned	Male-owned	Mixed	Whole sample
Shortage of capital	67.96	54.92	62.86	65.01	60.12	62.71
Inadequate or uncertain market	15.84	21.58	19.52	18.18	17.26	18.15
Access to credit	7.00	5.74	5.71	7.44	5.95	6.49
Inadequate business support services	4.24	6.56	2.86	3.58	8.33	5.17

SOURCE: AEMFI, Survey on Youth-owned MSEs in Ethiopia (2014)

4. RESULTS FROM THE ECONOMETRIC ANALYSES

After analysing the policy and regulatory constraints using descriptive statistics, attempt was made to examine the effects of the institutional, policy and regulatory constraints on growth and expansion youth-owned MSEs using econometrics method.

The Logit model was employed in this study to assess the relationship between the probability of youth owned MSE had positive employment growth ($\Pr(Y_i=1/X_i, Z_i)$) on one hand and individuals and firm level factors, institutional, policy and regulatory constraint factors on the other hand. This paper hypothesises that the probability of youth owned MSE had positive employment growth depends on the magnitude of the constraints (the explanatory variables).

The logit model is derived and specified as follow (Verbeek, 2008). Defining the latent variable of employment growth of youth owned MSE as y_i^* , the logit model of observed employment growth (Y_i) is fully described by:

$$\begin{aligned}
 Y_i^* &= \beta_0 + \beta_1 X_i + \beta_2 Z_i + \varepsilon_i, \\
 Y_i &= 1 \text{ if } Y_i^* > 0 \\
 Y_i &= 0 \text{ if } Y_i^* \leq 0
 \end{aligned}
 \tag{1}$$

where the ε_i has standard logistic distribution with mean zero and variance $\pi^2/3$ and are independent of all X_i and Z_i . Thus, we have:

$$P\{y_i=1\} = P\{y_i^* > 0\} = P\{x_i' \beta + \varepsilon_i > 0\} = P\{\varepsilon_i > -x_i' \beta\} = P\{\varepsilon_i \leq x_i' \beta\} = F(x_i' \beta), \tag{2}$$

We estimated the parameters by the method of maximum likelihood. In order to interpret the parameters we derive the marginal effects as the probability that Y_i equals 1 with respect to the k^{th} element in X_i and Z_i .

Table 8 shows the summary statistics and brief description of variables used in the regression. The independent variables in the regression attempt to capture the individual and firm-level attributes and institutional, policy and business constraints that affect the growth of youth-owned enterprises. The summary statistics show that about 37.4% of the sample youth-owned MSEs had a positive employment growth with standard errors of 0.48. The average household size and age of MSE owners were 4.14 individuals and 27.34 years, respectively. About 23% of the MSE-owner respondents were female and 40% were male, while the remaining 37% were jointly owned by both male and female operators. The average education level of the respondents was grade 10 with standard error of 3.2. Regarding firm characteristics, about 42% of the enterprises were organised in sole proprietorship and about 60% were engaged in microenterprise. On the other hand, while 28% of the operators were engaged in metal and woodwork sub-sector, about 30% of the MSE operators possessed relatively advanced or modern machineries. Tax rate (14%), licensing and registration (5%), tax administration (10%), corruption (10%), marketing production premises (60%), financial access (62%), business support services (39%), and shortage of capital (63%) were reported as the major constraints or obstacles to expand the activities of MSE operator youths. Only about 26% of the respondents perceived that the laws, policies and regulations were fairly and/or highly/completely predictable.

Table 8. Description and summary statistics of variables

Variables	Description	Mean	Std. errors
Dependent Variable			
Employment growth	1 if the firm had positive employment growth; 0 otherwise	0.374	0.484
Individual and firm level variables			
Household size (in no.)	Total number of members in a given household	4.140	2.175
Age of MSE owners	MSE owners age in years	27.336	4.332
Female dummy	Dummy equals 1 if the owner's gender is female and zero otherwise	0.231	0.422
Mixed dummy for owners gender	Dummy equals 1 if the firm is owned by both male and female and zero otherwise	0.370	0.483
Sole ownership dummy	Dummy equals 1 if the firm has sole ownership and 0 otherwise	0.421	0.494
Micro enterprise dummy	Dummy equals 1 if the firm is micro enterprise and 0 otherwise	0.597	0.491
Owners education level	Owners education level	10.182	3.190
Enterprise with Advanced or modern machineries	Dummy equals 1 if the firm has advanced or modern machineries and 0 otherwise	0.301	0.459
Metal and wood work	Dummy equals 1 if the firm is engaged in metal and wood work sector and 0 otherwise	0.287	0.453
Reasons to engage in MSE	Dummy variable equals 1 if the owner has engaged in MSE for better opportunity, and zero other wise	0.285	0.452
Constraint variables			
Tax rate as a major obstacle	Dummy equals 1 if the firm identified tax rate as a major obstacle for the business and 0 otherwise	0.142	0.349

Variables	Description	Mean	Std. errors
Licensing and registration problems	Dummy equals 1 if the firm identified licensing and registration as a major obstacle for the business and 0 otherwise	0.054	0.226
Tax administration inefficiency	Dummy equals 1 if the firm identified tax administration inefficiency as a major obstacle for the business and 0 otherwise	0.096	0.294
Labour regulation constraints	Dummy equals 1 if the firm identified labour regulation as a major obstacle for the business and 0 otherwise	0.009	0.093
Corruption constraints	Dummy equals 1 if the firm identified corruption as a major obstacle for the business and 0 otherwise	0.096	0.294
Policy predictability	Dummy equals 1 if the firm perceives policies are predictable and 0 otherwise	0.262	0.440
Lack of marketing space for products	Dummy equals 1 if the firm has lack of marketing space for its produce and 0 otherwise	0.597	0.491
Accessing finance	Dummy equals 1 if the firm has lack of accessing finance and 0 otherwise	0.617	0.486
Lack of business support services	Dummy equals 1 if the firm has lack of business support services and 0 otherwise	0.387	0.487
Shortage of capital	Dummy equals 1 if the firm has lack of shortage of capital and 0 otherwise	0.627	0.484

SOURCE: AEMFI, Survey on Youth-owned MSEs in Ethiopia (2014)

The regression results in Table 9 showed the effects of policy and regulatory constraints and individual attributes on employment growth of youth-owned MSEs using the Logit model. Panel A in Table 9 depicts the Logit regression results; panel B shows the Logit regression with robust standard errors to capture the problem of heteroscedasticity, the common problem of most cross-section dataset. Panel C reveals the marginal effects of the explanatory variables on the predicted probability of employment growth. Since the marginal effects are important, which provide not only the direction but also the magnitude of the effect of the explanatory variables on the probability of growth of the enterprise, the interpretations of the results of the study are mainly based on Panel C.

Panels A and B in Table 9 indicate that most of the constraints were found to have insignificant effect on the growth of employment, except policy predictability, lack of marketing and production premises, and inadequate business support services, which were found to have significant effects at 1%, 5% and 10% level of significance, respectively. On the other hand, most of the individual and firm-level characteristics were found to have significant effects on the employment growth of youth-owned MSEs.

As per the results in Panel C of Table 9, tax rate and administration, corruption, labour law, and licensing constraints were found to be insignificant variables influencing the growth of youth-owned MSEs, which implies that they were not serious challenges of the operators. On the other hand, although access to finance and shortage of capital were identified as key challenges, they were found to be insignificant variables in influencing the growth of youth-owned MSEs. Policy predictability was found to have a positive and significant effect on growth of youth-owned enterprises. Moreover, those MSE owners who believed that government policies were predictable had 7% higher probability of employment growth than those who perceived that the policies were unpredictable. On the other hand, lack of marketing and production premises was found to have a negative and significant effect on employment growth of MSEs. This implies that those MSE owner youths who reported that lack of marketing space for their produces were found to have 7% lower probability of growth in employment. Lack of business support services was also found to have negative and significant effect, indicating that youth MSE operators who reported lack of business support services as a major obstacle to business were found to have 6.7% lower likelihood of growth.

Table 9. Estimated results of logit model of youth owned MSEs had positive employment growth

VARIABLES	Panel A	Panel B	Panel C
	Logit	Logit (Robust SE)	Marginal effects
Household size	0.0731** (0.0352)	0.0731** (0.0344)	0.017** (0.00785)
Age of MSE owners	0.0510*** (0.0180)	0.0510*** (0.0188)	0.012*** (0.00428)
Female dummy	-0.155 (0.222)	-0.155 (0.220)	-0.035 (0.04896)
Gender of owners mixed dummy	0.402** (0.204)	0.402* (0.210)	0.093* (0.04882)
Sole ownership dummy	0.701*** (0.192)	0.701*** (0.196)	0.161*** (0.04464)
Microenterprise dummy	-0.615*** (0.174)	-0.615*** (0.173)	-0.142*** (0.03987)
Owners education level	0.107*** (0.0257)	0.107*** (0.0262)	0.024*** (0.00594)
Enterprise with Advanced or modern machineries	0.210 (0.167)	0.210 (0.162)	0.048 (0.03776)
Metal and wood work sector	1.363*** (0.177)	1.363*** (0.174)	0.321*** (0.03969)
Reasons to engage in MSE	-0.156 (0.174)	-0.156 (0.173)	-0.035 (0.03862)
Tax rate as a major obstacle for the business	0.0898 (0.241)	0.0898 (0.251)	0.021 (0.05845)
Licensing and registration problems constraining the business	0.221 (0.333)	0.221 (0.333)	0.052 (0.07974)
Inefficiency and discretionary enforcement in tax administration	0.0604 (0.283)	0.0604 (0.303)	0.014 (0.07017)
Labour regulation constraints	-1.358 (1.125)	-1.358 (1.252)	-0.232 (0.13738)
Corruption constraints	0.268 (0.264)	0.268 (0.273)	0.063 (0.0658)
Policy predictability	0.299* (0.173)	0.299* (0.173)	0.070* (0.04076)

VARIABLES	Panel A	Panel B	Panel C
	Logit	Logit (Robust SE)	Marginal effects
Lack of marketing space for products	-0.306** (0.155)	-0.306** (0.155)	-0.070** (0.03578)
Accessing finance among the three most important business problems currently	-0.111 (0.165)	-0.111 (0.165)	-0.026 (0.03793)
Lack of business support services as a major obstacle	-0.295* (0.160)	-0.295* (0.160)	-0.067* (0.03562)
Shortage of capital as the most important obstacle	-0.154 (0.165)	-0.154 (0.163)	-0.0354 (0.0376)
Constant	-3.543*** (0.644)	-3.543*** (0.687)	
Observations	909	909	
Predicted probability			0.353

Standard errors in parentheses

*** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$

When examining the effect of owner and firm-level attributes on the growth of the youth-owned MSEs, household size was found to positively affect firm growth: as household size increases by one unit, the likelihood of growth of firms in employment increases by 1.7% at 5% level of significance. Age of owners was also found to have a positive effect on employment growth of MSEs: as owner's age increases by one unit, the likelihood that firms would show growth in employment also increases by 1.2%. Furthermore, the level of education, type of ownership and sectors they engaged in were also found to have a strong positive effect on the growth of MSEs. As the level of education of the MSE-owner youths increases by one grade, the probability of growth in employment increases by 2.4%. Firms engaged in 'metal and wood work sector' were found to have 32% higher probability of growth in employment. Besides, MSE owner youths, who were sole owners, were found to have 16% higher likelihood of growth in employments. Contrary to our expectation, type of enterprise (micro and small enterprises) was found to have negative effect on the growth of firms and firms labelled as microenterprises were found to have 14% lower likelihood of growth in employment.

5. CONCLUSIONS

Enabling institutions, policies, strategies, legal and regulatory frameworks, and government support programs are critical inputs influencing the growth and expansion of MSEs in Ethiopia. The government has been active in designing and implementing various policies, strategies and regulations and allocated huge budgetary resources to provide package of support services, such as providing working and marketing premises; building the capacity of MSEs through training (technical and management training), industrial extension services, market linkages, and technology transfer; and extending loans and other financial services in one-stop-service-centres. Although the government took the entire responsibility of creating employment opportunities through the expansion of self-employment, particularly for the youth, there were no specific strategies, support and incentives for the private sector, such as holidays, and partial subsidy for youth training to employ and mentor MSE owner youths, who have very limited marketable skills, experiences, networks and knowledge.

The findings show that a significant proportion of the MSE owner youths accessed technical training through the government support programs. However, although many of the respondents (85%) indicated that they are satisfied with the training, only 15% reported that the quality of the technical training was low and inadequate. Relatively higher proportion of the respondents accessed extension services, infrastructure support (power and water), production premises, credit, and business development training. On the other hand, very limited respondents received technology support and used one-stop service centres. With the exception of market linkage to sell their products, the MSE owner youths ranked the quality of the services provided by government either satisfactory or more than satisfactory (very good and good). Technical training, business development training, and access to production premises were of relatively higher quality compared to the rest of the support services. One-stop services, access to sub-contracting, technology support, market linkages, access to market premises, and finance were reported to be of low quality.

High collateral requirements of finance providers was ranked as a major problem of youth-owned MSEs, followed by lack of access to credit, lack of business premises, lack of business support services, frequent interruption of power and water supply, and lack of raw materials inputs. As per the econometric results, tax rate and administration, corruption, labour law, and licensing were found to be insignificant policy and regulatory constraints influencing the growth of youth-owned MSEs. This implies that the above policy and regulatory constraints didn't affect the business expansion of youth MSE owners. Policy predictability was found to have a positive and significant effect on growth of youth MSE owners. Those MSEs who believed that policies were predictable had higher probability of registering employment growth than those who perceived that the policies were unpredictable. On the other hand, lack of marketing

space for products was found to have a negative and significant effect on employment growth of MSEs. This implies that those MSE owners who reported that lack of marketing space for their produces were found to have lower probability of growth in employment. Lack of business support services was also found to have negative and significant effect on employment growth of MSEs, indicating that youth MSE operators who reported lack of business support services as a major obstacle to business were found to have lower likelihood of growth. The result of the study also shows that putting an enabling policy environment alone is not sufficient to bring about the expected optimal results; the degree to which MSEs can improve themselves by changing owners and firm-level attributes rather more important. In other words, the growth of youth-owned MSEs was more affected by owner and firm attributes than by policy and regulatory constraints.

There is a tendency to rush for regulation or even overregulation in Ethiopia in the past five years. That affected the expansion of small businesses, by opening loopholes for rent-seeking practices. Inefficient tax administration, lengthy process to renew licenses, such as evidence of physical address and requiring title deed (if working in his/her homestead) or contract agreement (if the premise is leased), producing competency certificate, and trade name increased the cost of registration and licensing. This encourages small businesses to stay out of the formal economy and squeezes those youth-owned MSEs who comply with the regulatory requirements. There is a need to develop a tailored regulatory, licensing and registration system for small businesses in Ethiopia by introducing minimal compliance and reducing administrative cost (e.g., a simplified tax regime where small businesses pay taxes as per self-assessment and risk-based verification by tax authority). Addressing the policy and regulatory constraints will require revisiting the regulatory and tax regimes and developing a simplified system. There is a dire need to undertake detailed cost and benefits studies for all existing regulations, procedures, directives, and standards by focusing on their impacts on growth of the private sector (MSEs), benefits to government, rent-seeking opportunities for the bureaucrats, and the public. However, there are opportunity costs to be considered in simplifying the procedures for small businesses such as reducing government revenue and abuses by relatively larger firms to take advantage of the incentives and exemptions provided to small businesses.

Notes

1. HASIDA was replaced by the establishment of Industry and Handicraft Bureaus in the regional government by Proclamation No. 14/1993. The Federal Micro and Small-scale Enterprise Agency (FMSEDA) and Regional Micro and Small-scale Enterprises Development Agencies (RMSEDA) were established by the Council of Ministers of Ethiopia Regulation No. 33/1998.

2. The definitions of micro and small enterprises vary from country to country. However, as per Ethiopians' five-year MSE Development Strategy (2011), microenterprise category includes firms which have up to 5 employees (including the owner or family) and their total asset is less than or equal to 100,000 Birr for industrial sector and less than or equal to 50,000 Birr for service sector. On the other hand, small enterprises are firms which have 6–30 workers and their total asset is between 100,001 Birr – 1,500,000 Birr for industrial sector and between 100,001 Birr – 500,000 Birr for service sector.
3. The actual survey was conducted in 2004 in six major cities (Addis Ababa, Adama, Hawassa, Bahir Dar, Jimma, and Mekele), with the financial support of Ethiopian Development Research Institute (EDRI). The study used 974 randomly selected MSEs: 551 micro enterprises (with less than 5 workers) and 423 small enterprises (having 5–10 workers).

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