

# **Constraints to Small Firm and Medium's Contribution to Economic Growth in Zambia**

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### **Declaration**

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## Abstract

Small to medium scale enterprises (SMEs) arguably drive economic growth and job creation in developing countries, but factors that hinder their growth are generic or specific to sectors and remain a crucial area of research. This study examines factors constraining SMEs from optimally contributing to economic growth of Zambia. The study answered the following research questions; what factors act as constraints for SMEs to contribute towards economic growth; how conducive are the policy and institutional infrastructure for the SMEs to operate efficiently and to establish whether the evidence presented by these factors are specific to Zambia or apply elsewhere. For research design, the study adopted the mixed research approach. Both quantitative and qualitative research approaches were implored in order to produce the findings outlined in this report. Simple random sampling was used to draw a total of 250 SMEs to which structured questionnaires were administered. Semi-structured interviews were also conducted with three major stakeholders. The study used the statistical package of social science (SPSS) to analyse the quantitative data while qualitative data was analysed thematically- by identifying key themes and summarizing related information under each theme- for perspectives around SMEs contribution to economic growth. The study findings identify internal and external factors that constrain SMEs from contributing efficiently to economic growth and these include; 1) *poor access to finance*, 2) *competition*, 3) *lack/inadequate infrastructure*, and 4) *lack of skills and training* and these are similar across regions and other countries. On the other hand, it was stated that the high cost of production (as a result of high/multiple taxes and tariffs) prevent SMEs ability to effectively contribute to economic growth. The findings further show that institutionalised efforts created to ensure the SMEs flourish contribute effectively to economic growth. However, the correlation between targeting and segmentation of the SMEs for funding key areas of economic activities is not clear. Results show that the major factors according to the survey were the failure to access finance as attested by 160 of the 250 respondents who put this as the biggest impediment in success of their business and 65 of the respondents gave high taxes as the factor affecting them the most. The rest of the respondents gave competition and the absence of appropriate infrastructure to support business growth as a reason for poor performance and contribution to wider economic growth. Additionally, the findings show that there is no significant relationship between internal and external constraining factors and enterprise contribution to economic growth.



To ensure greater SME contribution to economic growth, this study emphasises government interventions in financial services and infrastructure development, clarity in the implementation of policy and institutional provisions, encouragement of SME value-chain and market linkages as well as creation of knowledge hubs.

*[Key words: Small to Medium Enterprises, Economic Growth, Economic Development]*

### Acronyms

CSO	Central Statistical Office
CEEC	Citizen Economic Empowerment Commission
DBZ	Development Bank of Zambia
DTI	Department of Trade and Industry
GCI	Global Competitive Index
GDP	Gross Domestic Product
GEM	Global Entrepreneurship Monitor
GRZ	Government Republic of Zambia
IFC	International Financial Cooperation
ILO	International Labour Organization
LCC	Lusaka City Council
MCTI	Ministry of Commerce Trade and Industry
MFEZ	Multi Facility Economic Zone
MSME	Micro Small and Medium Enterprise
NGO	Non-Governmental Organization
NCC	National Council for Construction
OECD	Organization for Economic Co-operation and Development
PACRA	Patents and Companies Registration Authority
PSDRP	Private Sector Development Reform Programme
RDA	Road Development Agency
SAPs	Structural Adjustment Programmes
SBR	Statistical Business Register
SEDB	Small Enterprise Development Board
SID	Small Industrial Development
SIDO	Small Industries Development Organization
SMEs	Small and Medium Enterprises
SOE	State Owned Enterprise
UNIDO	United Nations Industrial Development Organization

USA	United States of America
VIS	Village Industry Service
WB	World Bank
WTO	World Trade Organization
YWCA	Young Women Christian Association
ZCSMBA	Zambia Chamber of Small Medium Business Association
ZDA	Zambia Development Agency
ZGJP	Zambia Green Jobs Programme
ZIPAR	Zambian Institute of Policy Analysis of Research
ZRA	Zambia Revenue Authority

## CHAPTER 1: INTRODUCTION AND BACKGROUND

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### 1.1 Situating the Study

There is consensus among policy makers, economists and business experts that small and medium enterprises (SMEs) are key drivers of economic growth and development (UCS, 2011). SMEs make-up the largest proportion of businesses all over the world and play a tremendous role in employment, generation of higher production volumes, increasing exports, introducing innovation and entrepreneurship skills, provision of goods and services, creating better standard of living, as well as immensely contributing to the gross domestic products (GDPs) of many countries (OECD, 2000). ILO (2015:5) estimates that on the global level, there are 420 to 510 million SMEs, which account for 50 to 60 percent of employment (IFC, 2010) and contribute 60 to 70.0 percent of GDP (ILO, 2015:15).

Consequently, a vibrant and blooming SME sector is considered as one of the significant characteristics of a flourishing and growing economy (UCS, 2011). This is supported by facts that most of the emerging economies in the world such as the BRINCS Nations (Brazil, Russia, India, Nigeria, China and South Africa) and the MINT Nations (Mexico, Indonesia, Nigeria and Turkey) are characterized by the growth of SMEs. China for example, as the world's second largest economy and the largest exporter (Cunningham, 2011), SMEs are major engines for China's rapid economic growth. Every year, SMEs contribute around 59.0 percent of GDP, 50.0 percent of tax revenue, 68.0 percent of foreign trade volume and 75.0 percent of urban employment. They are also responsible for 65.0 percent of the invention patents and 80.0 percent of new products in China (Li Xue, 2014:6). The situation is not different from Indonesia where the economy boasts of having more than 57.9 million SMEs that contributes around 58.9 percent of GDP and absorbs 97.3 percent of workforce (Global Business Guide Indonesia, 2016). SMEs also play a significant driving force in the Brazilian economy where the sector conducts 98.0 percent of industrial, commercial and service operations; contributes to 20.0 percent of GDP and accounts for more than 50.0 percent of formal employment (OECD, 2017).

In Africa, SMEs are increasingly being recognised as being significant tools to the development of economies (Beck and Levine, 2003). This is backed by the fact that 90.0 percent of the businesses in the continent operate as SMEs, which account for more than 50.0 percent of employment and GDP (Saravanan et al, 2008). For example, Nigeria one of African largest

economies estimates that 97.0 percent of the entire enterprises in the country are SMEs. This figure accounts for an average of 50 percent of the workforce and supports up to 50 percent to the country's industrial output (Ihua, 2005). The case is not different from South Africa which estimates that 91.0 percent of formal business entities are SMEs and they contribute between 52.0 to 57.0 percent towards GDP and provide about 61.0 percent of employment (Abor and Quartey, 2010). In Mauritius, SMEs contributes about 40.0 percent to the country's GDP and account for 54.6 percent of total employment (Ministry of Business, Enterprise and Cooperatives). The scenario is not different from Zambia where SMEs contribute about 84.6 percent of the total number of jobs (CSO, 2014) and accounts for over 80.0 percent of the number of businesses registered at PACRA and account for about 40.0 percent to 60.0 percent of total GDP (ZIPAR, 2014).

Statistics on contribution of SMEs to GDP and employment especially to the worlds developing nations and more prominently in Africa proves how significant this sector is to the sustainable development of any nation. Most of the developing nations such as Zambia are in transition. Transition economies usually experience inflation, a fall in production, growing unemployment and fast unexpected changes of economic environment. Consequently, the social- productive and social-economic advantages of SMEs such as flexibility, adaptation, open entry/exit to the sector, among others can help an economy to overcome its transition problems (Small Business in Ukraine, 1997:45). Subsequently, the development of SMEs should become an important part of economic policy of every economy in transition.

For the purpose of this study, ILO (2015:2) defines small enterprises as those that have 10 to 100 employees and medium-sized enterprises as those with 100 to 250 employees. Definition by ILO clearly segment SMEs by showing the threshold of where each category of a small or medium enterprise starts and ends using the number of employees. ILO as an organisation attaches great importance to the growth of SMEs in various economies. In recent years, many developed and developing nations have had employment challenges. Therefore, ILO's advisory services on SME policies among its member countries are in high demand. For this reason, it has made key interventions in supporting the growth of SMEs because of their contribution to job creation (i.e. they account for two-third of all jobs worldwide) and income generation. For this reason, one may argue that this may be the reason why the definition attaches great importance to the number of employees when differentiating between small and medium enterprises.

In Zambia, the government under Ministry of Commerce Trade and Industry (MCTI) defines SMEs as follows:

“A small enterprise shall be any business enterprise registered with the Registrar of Companies;

i) Whose total investment, excluding land and building

- In the case of manufacturing and processing enterprises, shall be between Eighty thousand and Two Hundred Thousand Kwacha (K80, 000 - K200, 000) in plant and machinery;

- In the case of trading and service providing enterprises shall be up to One Hundred and Fifty Thousand Kwacha (K150, 000).

ii) Whose annual turnover shall be between One Hundred and Fifty One and Two Hundred Thousand Kwacha (K151, 000 - K200, 000)

iii) Employing between eleven and forty nine (11- 49) persons”, (MCTI, 2008:16).

“A medium enterprise shall be any business enterprise larger than a small enterprise registered with the Registrar of companies;

i) Whose total investment, excluding land and building;

- In the case of manufacturing and processing enterprises, shall be between Two Hundred and One thousand and Five Hundred Thousand Kwacha (K201, 000 - K500, 000) in plant and machinery,

- In the case of trading and service providing shall be between One Hundred and Fifty One Thousand and Three Hundred Thousand Kwacha (K151, 000 - K300, 000).

ii) Whose annual turnover shall be between Three Hundred Thousand and Eight Hundred Thousand Kwacha (K300, 000 - K800, 000).

iii) Employing between Fifty One and One Hundred (51 - 100) persons, (MCTI, 2008:16-17).

According to Todaro (2004), Economic growth is the steady process by which the productive capacity of the economy is increased overtime to bring about rising levels of national output and income. This is anchored on sustainable national job creation and increased production output.

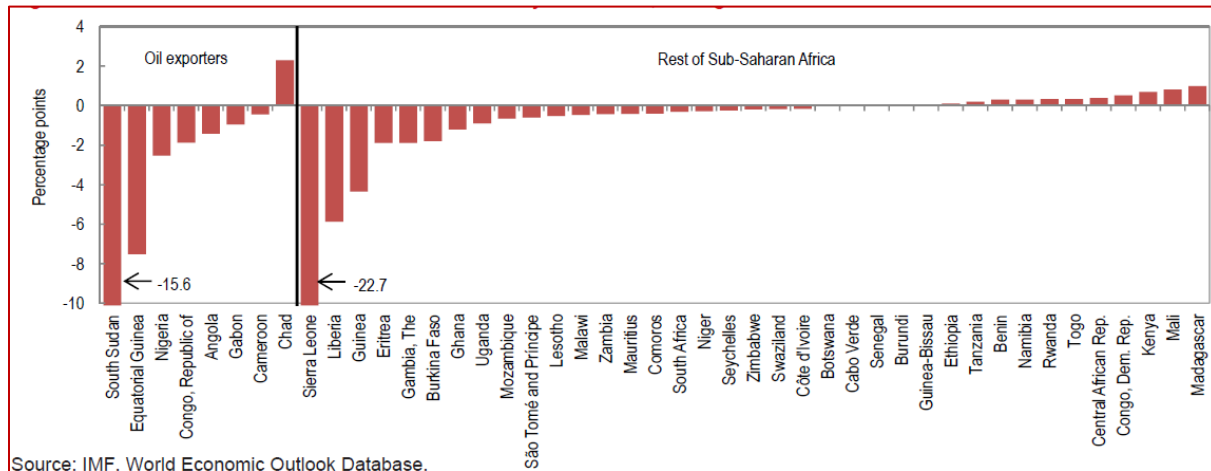
The past two decades witnessed growth and expansion of SMEs in Africa. Private sector consists mostly of informal SMEs operating alongside large firms (Ayyagari et al. 2011; Karlsson 1993). These businesses face numerous challenges which hinder their contribution to economic growth, raising the need for systematic studies – such as advanced in this research – that can identify the factors hindering SMEs from optimally contributing to economic growth. This is important in unlocking the potential of SMEs to provide greater contribution to national economic growth in sub-Saharan Africa.

Growth and expansion of the SME economy in Zambia closely relates to the economic reforms of the 1990s. Zambia's adoption Structural Adjustment Programmes (SAPs) in the 1990s led to the liberalisation of the economy and the promotion of private businesses. The liberalisation of the economy also led to the privatisation of most of the State-Owned Enterprises (SOEs) which were the major employers. However, with privatisation came the loss of jobs, which strengthened the centrality of SMEs in survival and sustenance of families. This led to the establishment of a lot of micro, small and medium businesses. This explains the reason for the existence of mostly *necessity entrepreneurs* as compared to *opportunity entrepreneurs* in Zambia today. The former category of entrepreneurs was trying to find a way to survive by creating self-employment. Most of these businesses are in the informal sector and predominately in the trading sector (MCTI, 2007). The Zambian government in 1994 established the Industrial, Commercial and Trade policy which among some of its pronouncements, was the need to devise a strategy to increase the participation of the private sector as a means to encourage SMEs growth in the country. A recent survey by the Zambia Development Agency (ZDA) revealed that SMEs accounted for more than 90 percent of the total business enterprises and that the number of SMEs had been on the rise in the recent past (ZDA 2010).

While a lot has been written on the contribution to economic growth by SMEs in both the developed world and developing world, there has not been much written on the reasons for the failure of SMEs particularly in Zambia and reasons have not been purported as to why they have not been able to effectively contribute to economic growth.

Table 2 below reveals that according to the IMF despite the region posting an almost static growth of about 5 percent, Zambia was projected to post a negative grow of about negative one

from 2014 to 2015.



**Figure 1.1: Real GDP growth projection (2014-2015) (IMF, World Economic Outlook Database).**

The SMEs sector however recorded an increase in numbers of businesses born during this period. This raises a research gap as to the reasons of the failure by the growing number of SMEs and their contribution to broad-based economic growth. Zambia as a nation witnessed a stagnation in economic growth in the recent past, unemployment has increased, per capita income declined with the gross domestic product (GDP) plummeting from 6.0 percent in 2011 to 3.8 percent in 2016. Meanwhile the labour force absorption ratio was less than 0.5 (0.38) (CSO 2017). This context provides a fertile gap in which to explore factors constraining SMEs from contributing optimally to Zambia’s economic growth.



The SMEs contribution to economic growth is determined by their number of sustained employees, production output and turnover. This is dependent on the available favourable conditions that enable SMEs to do so. The identified independent variables that can directly or indirectly drive SMEs' contribute to economic growth as shown in table 1.1 below.

**Table 1.1: Independent and Dependent Variables**

Independent Variables	Dependent Variable
Infrastructure	Economic growth (employees, output, turnover)
Taxes	
Utility Tariffs	
Financing	
Competition	
Skilled Labour	
Technology	

## 1.2 Problem Statement

This study examined factors constraining SMEs from optimally contributing to economic growth in Zambia. In so doing, it engaged in an ongoing debate about the role of SMEs in economic growth, national development and related socio environments in which they reside in. Zambia records that about 37 percent of employment is directly related to SMEs. However, despite this significance, there is very limited evidence in the literature on the optimal influence of SMEs to economic growth. This paper intends to fill the aforementioned literature gap, in order to provide the appropriate positive interventions by the SMEs, the Government and other players in this industry. Moreover, the donors can have confidence in the policies that will enhance the performance of this sector. Evidently elsewhere such as in China, SMEs have significantly contributed to economic development. The Zambian government and her development partners have in the last decade allocated capital to finance projects and loans with intent for SMEs to flourish and contribute to the economic growth. This has been done through various initiatives namely; Citizen Economic Empowerment Commission, Women and Youth Empowerment Fund under the Ministry of Youth and Sports. Despite these efforts, poverty levels are still high at

above 50 percent with stagnant production outputs and low employment absorption rate of 32 percent, (CSO).

Hence, an examination of the factors constraining SMEs from optimally affecting the economic growth becomes imperative. The need to undertake this study was timely, as there was need to identify factors that act as impediments to SMEs' in Zambia and the numerous interventions that can be set in place to ameliorate their poor performance. Further, there is need to compare results with other countries/regions in order to understand the regional nuances and identify the areas of variations, and suggest possible long lasting solutions.

### **1.3 Research Questions**

The following are the research questions of the study:

- What are the main factors affecting SMEs optimal contribution to economic growth in Zambia?
- Are the factors constraining SMEs from optimally contributing to Economic growth in Zambia similar across different business sectors?
- How effective are the existing policy and institutional frameworks in supporting SMEs?

### **1.5 Research Objectives**

#### **1.5.1 General Research Objective**

The general objective of this study is to explore factors constraining SMEs from optimally contributing to economic growth in Zambia.

#### **1.5.2 Specific Research Objectives**

The specific objectives of the study are;

- To identify factors constraining SMEs' to optimally contribute to economic growth in Zambia.
- To establish whether the factors constraining the SMEs growth in sub-Sahara Africa are similar across various sectors in Zambia.
- To determine the association between internal/external constraint factors and economic growth in Zambia.
- To explore the wider policy and institutional environment in which SMEs operate in Zambia.

## **1.6 Scope of the Study**

The scope of the study was purposively narrowed to explore the factors that hinder SMEs from contributing effectively towards economic growth in Zambia. The study mainly focused on SMEs from all sectors of the economy which was somewhat representative of the entire economy. These include the key informants such as the Ministry of Commerce, Trade and Industry (MCTI) and the Zambia Chamber of Small and Medium Business Association (ZCSMBA). This allowed for the ease and promptness with which questionnaires were distributed and answered considering the limited time allocated for data collection. This was also important in gathering general comparable data across various sectors. Great effort was put into ensuring all relevant information was collected on all specific areas of the study. This research presents useful insights into the importance of SMEs in economic growth and factors that hinders SMEs from contributing effectively towards economic growth.

## **1.7 Significance of the Study**

Despite decades of research on SMEs and their role in local economies (Ayyagari et al. 2011; Beck et al. 2005; Nuwagaba 2015; Wang 2016), systematic studies that explore critical factors constraining SMEs from contributing optimally to economic growth remain thin.

The researcher decided to undertake this study in order to explore factors that constrain SMEs contributing to economic growth in Zambia. Specifically, the following reasons brought out the impetus for undertaking this study: firstly, to identify factors. This was done in order to gain an in-depth understanding of the nature of SMEs and constraining factors. In addition, this was done in order to have evidence based information. Primarily this study is for academic purposes, but further contributes to theory and the board of knowledge.

Most studies focus on the constraints affecting the growth of SMEs in both the developed and developing countries while others focus on their contribution to economic growth. This study combines both the constraints to growth of SMEs and their contribution to economic growth in Zambia. This is because despite numerous studies being undertaken on the SME sector in sub-Saharan Africa in particular Zambia, the sector still seems to be facing a lot of challenges, hence the need for more studies to be undertaken to continue to search for new solutions. Additionally, this study provides past and recent legislative frameworks and policies that support

and guide the operations of SMEs. This information will help inform policy makers and other parties working with SMEs in designing viable policies and programmes aimed at improving their production capacity which may consequently lead to their growth, which subsequently filters into economic growth. Lastly, the findings of this study may be of use to other researchers for gaining insights on the topic and further research.

This study provides an additional reference point for governments in policymaking decision concentrated on SMEs in the local economy. Having a comprehensive understanding of the factors constraining the growth of SMEs and preventing them from effectively contributing to economic growth is crucial in advocating for appropriate policies that can enhance the SME sector and produce greater results for economic growth in Zambia and across the region of sub-Saharan Africa.

## CHAPTER 2: LITERATURE REVIEW

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### 2.1 Introduction

This section articulates the conceptual and theoretical foundations and presents factors affecting SMEs, and their contribution to economic growth. The section will review empirical literature and unpacks various case studies in similar research that help elucidate on the topic understudy and how this applies in the context of Zambia and how they influence the optimal performance of SME's.

### 2.2 Understanding Small and Medium Enterprises

According to the OECD (2009), the bulk of economic activities in developing countries such as those in Africa take place in the small to medium enterprise economy. SMEs vary in size and scope, ranging from a neighbour who has a small shop to relatively bigger firms in local shopping malls. SMEs are not limited to one specific line of business. They range from agro products and health centres to consultancy firms and capabilities vary. Variations between SMEs and bigger firms can stem from their size, production capacity, number of employees or in terms profits. The flexibility in size and scope among SMEs means that they can exist everywhere, providing avenues for employing thousands in their operating countries, and potential for contributing to economic growth. This implies that they can prove to be vital to the catapulting developing countries to economic self-dependence.

However, the real value of the SMEs in dominant business and private-sector development discourse has somewhat been downplayed; viewing them simply as small businesses and as not giving much attention to the core environment in which they operate (MCTI 2007; Nuwagaba 2015). This presents potential for research – as advanced in this dissertation – to delve into the varying factors that enable or constrain SME's contribution to economic growth.

SMEs, by number, dominate the world business stage. Although precise, up-to-date data are difficult to obtain, estimates suggest that more than 95.0 percent of enterprises across the world are SMEs, accounting for approximately 60.0 percent of private sector employment (Ayyagari et al., 2011). Japan has the highest proportion of SMEs among the industrialised countries, accounting for more than 99.0 percent of total enterprises (EIU, 2010). India, according to its

Ministry of Micro, Small and Medium Enterprises, had 13 million SMEs in 2008, equivalent to 80.0 percent of all the country's businesses (Ghatak, 2010). In South Africa, it is estimated that 91.0 percent of the formal business entities are SMEs (Abor and Quartey, 2010).

Estimated data for the 27 countries in the European Union (the EU-27) for 2012 also illustrate the importance of SMEs. They account for 99.8 percent of all enterprises, employ 67.0 percent of all workers and contribute 58.0 percent of gross value added (GVA) – defined as the value of their outputs less the value of intermediate consumption and an important factor in GDP. The contribution made by SMEs does vary widely between countries and regions. Nevertheless, although they play particularly key roles in high-income countries, SMEs are also important to low-income countries, making significant contributions to both GDP and employment (Dalberg, 2011).

They are also major contributors to innovation in economies, partly through collaboration with the larger corporate sector. SMEs that become embedded in the supply chains of larger businesses can be spurred on to improve their own human and technological capital (ACCA, 2010), thus improving their own productivity and performance.

When combining the data for those countries for which reasonably good data are available, SMEs account for 52.0 percent of private sector value added, which provides a reasonable estimate for the sector's global economic contribution (ACCA, 2010). The contribution of SMEs to economic fundamentals nonetheless varies substantially across countries: from 16.0 percent of GDP in low-income countries (where the sector is typically large but informal) to 51.0 percent of GDP in high-income countries.

According to the Australian government in 2011, SMEs contributed around 60.0 percent of Australia's industrial value added in 2009 to 2010. In OECD economies, over 95.0 percent of firms are SMEs and micro-enterprises, accounting for some 55.0 percent of GDP. In developing countries, by contrast, over 90.0 percent of all firms outside the agricultural sector are SMEs or micro-enterprises. These firms produce a considerable part of GDP. In Morocco, for example, 93.0 percent of industrial firms are SMEs, accounting for 38.0 percent of the production, 33.0 percent of investment and 30.0 percent of exports. The contribution of SMEs is considerably higher in South Africa. The estimated 90.0 percent of the formal business entities in South Africa that are SMEs contribute 52.0–57.0 percent to GDP. In Ghana, SMEs are even more prominent in the local economy, representing about 92.0 percent of Ghanaian businesses and contributing

about 70.0 percent to Ghana's GDP (Abor and Quartey, 2010).

Overall, statistics can sometimes mask the particular contribution made by individual sectors. For example, in 2006/7, the contribution made by micro and small businesses to India's GDP was only around 6.0 percent. Even so, manufacturing SMEs accounted for around 40.0 percent of industrial output, and 40.0 percent of all exports (Ghatak, 2010). Similarly, the United States International Trade Commission (2010) reports that SMEs contributed roughly 50.0 percent of US private non-agricultural GDP in 2004, a share that had remained relatively stable from 1998 to 2004. The service sectors are by far the most important contributors, accounting for 79.0 percent of SMEs' contribution to GDP.

Olawale & Garwe (2010) state that SMEs employ not less than 22 per cent of the adult population in developing countries. Additionally, the authors indicate that SMEs are better at using local resources. Thus, resources that would otherwise be wasted will be utilized by small businesses.

SMEs create dynamism by way of innovation and forming new firms. Considerable evidence has been presented over the years to show that small businesses are important in economic stabilization, and that a decline in this sector will have a negative impact on economic growth (Olawale & Garwe, 2010).

Proponents of SMEs stated that these enterprises have the ability to enrich workers' talents and capabilities. The sector not only provides jobs, but also creates "the prideful sense of being independent". These benefits are directly relevant to any effort to eradicate poverty in developing countries, especially in Africa. Experts on African SMEs have also pointed out that SMEs are a significant component of the solution to Africa's development issues. They maintain that the creation of new sustainable SMEs is vital to the economic prosperity of Africa, and without them the continent risks economic stagnation (Olawale & Garwe, 2010).

SMEs with their bias towards the service sector, have been argued to have a key role in solving unemployment problems generated by structural changes in the world economies (Olawale & Garwe, 2010). According to Aris (2006), considered Small and Medium Enterprises (SMEs) have been the backbone of economic growth of an economy in driving industrial development.

When compared with larger businesses, SMEs' contribution to output tends to be lower per firm

because they tend to be more labour intensive than larger firms and concentrated in service sectors. They therefore typically achieve lower levels of productivity, though they do contribute significantly to employment (Wymenga et al., 2011).

SMEs' greater labour intensity means that job creation entails lower capital costs than in larger firms (Liedholm and Mead 1987; Schmitz 1995), which is particularly important for developing countries and economies with high unemployment. Moreover, SMEs are generally more common in rural areas than larger businesses. Especially in developing countries, SMEs thus provide much-needed employment in rural areas.

SMEs can in fact become the engines that sustain growth for long-term development in developing countries. When growth becomes stronger, SMEs gradually assume a key role in industrial development and restructuring. They can satisfy the increasing local demand for services, which allows increasing specialisation, and furthermore support larger enterprises with services and inputs (Fjose et al., 2010).

There are various studies on the relationship between SMEs and economic growth in the literature. In 2011, Akingunola examined the relationship between SMEs financing and economic growth in Nigeria. The result shows that SMEs financing is positively related to economic growth.

Adebisi, Sunday, and Ofuani (2015) examined the financial challenges that SMEs are facing and its effects on their contribution to the economy in Lagos state. The study used primary data which was collected through administration of questionnaire to 222 respondents. The study shows that financial challenges rank as the highest among the challenges inhibiting the performance of SMEs contributing economically effectively in Lagos state of Nigeria.

Afolabi (2013) examined the growth effect of small and medium enterprises (SMEs) financing in Nigeria between 1980 and 2010. Using Ordinary Least Square (OLS), the result shows that SMEs financing was positively related to economic growth.

### **2.3 The Centrality of Small and Medium Enterprises in the Wider Context**

In examining SMEs in the wider context, this section draws on three main case study country experiences: India, Kenya and Tanzania. The selection of the three cases provided comparable experiences to illuminate perspectives on Zambia and the wider region in sub-Saharan Africa.



Existing experiences in these case studies offer a fitting foundation for this study. These studies will be able to compare the factors that are constraining SMEs in Zambia as they relate to the wider regional context in order to contribute to economic growth.

First, the SME sector in India consists of about 36 million units, providing employment to over 80 million persons. Through more than 6000 products, the sector contributes about 8 percent to GDP alongside 45.0 percent to the total manufacturing output and 40.0 percent to the exports from the country (Saleman and Jordan, 2015). The Indian case shows a clear national drive and direction for the SME sector. For instance, the government has inaugurated many industrial estates, industrial parks, special economic zones for enhancing SME's status. In addition, many associations, chambers and supporting trade unions were formed for discussing and solving SME's issues and challenges (Saleman and Jordan, 2015). According to the Ministry of SME, the units registered increased to 31.2 million by the end of 2011. This figure is estimated to grow to 40 million by the end of 2020. The government of India has inaugurated many institutions, associations, and schemes for development of small and medium sectors. Among them are the National Institute of Micro Small and Medium Enterprises, related to promotion, development and modernization of the SMEs sector. Within the national policy and institutional provisions, India promotes and develops entrepreneurs by implementing training programs, workshops, and skill development programs (Das, 2008).

Many factors influence SMEs in India. Some of these factors relate to production, marketing, finance, and external environment, infrastructure, as well as supporting framework (Saleman and Jordan, 2015). Here, the key challenges facing SMEs include difficulty accessing finance particularly through banks and other lending institutions, awareness about credit schemes, longer processes involved in obtaining bank loans, lack of knowledge about loans schemes, which links to the lack of sufficient working capital (Das, 2008). Other challenges facing the SME economy include production challenges (e.g. lack of power), lack of resources including processes of raw materials access which links to high cost of raw materials, non-availability of raw materials, lack of technical up gradation, and lack of machinery and equipment. Lack of information, lack of research and development facilities, lack of demand, lack of production capacity, lack of education all act as stressors. More widely, SMEs face marketing challenges in terms of lack of market information, promotion strategies, lack of distribution channels, lack of organized

channels, lack of returns, lack of networks, long delivery times, lack of information on marketing channels, lack of market structure, lack of awareness and experience. How the SME actors respond to these challenges within the environment in which they participate requires context specific research analysis – as advanced in this study in the case of Zambia.

The second case is Kenya. The SME economy in Kenya embodies the bulk of economic activities. Recent studies show various success trends and driving factors of the SME economy in Kenya (Stephen et al., 2011). For instance, a study by Jackson et al., (2008) found that paternalism emerged as a common theme in the way cultural dynamics and influences are combined – for in-group and out-group organizational members – and was isolated as one possible success factor for local SMEs.

However, in some areas, SMEs have been said to report high rate of failures with many enterprises dying at an infant stage. The arguments suggest that few of the SMEs grow to become big enterprises. The reason to this failure is pegged on the various factors that continue to inflict stagnation of the industry performance. These include: lack of access to credit, regulatory framework, management issues, market barriers and education and training. Recent studies such as Jackson et al., (2008) investigate factors affecting the performance of SMEs enterprises in Thika Municipality in Kenya. Findings from this study show that most SMEs in Thika Municipality finance their businesses from bank loans, personal savings, loans from family and relatives, through government institutions, and through Non-Governmental Organizations. However, the challenges that SMEs are facing from borrowing from these organizations are high interest rates and lack of collateral. SMEs thus dislike borrowing from banks, for fear of losing property in the event of defaulting on the loans and if the business fails. Such context specific evidence is important but fails to explain processes that lead to such outcomes. This raises the need for research to explore and understand the wider policy and institutional context within which SMEs operate, and elements that determine outcomes.

Additionally, the challenges encountered by SMEs include; marketing as a barrier to enterprise performance; SMEs market their products locally through media print, through dropping of leaflets, through word of mouth, and through television. Bureaucracy in registration is deemed to be another factor which hinders enterprise's growth, with corruption diverting support

programs from original beneficiaries. Cumbersome laws and regulations, political instability, high compliance costs and high cost of tax/complexity of the customs system also hinder enterprise's growth. The lack of government support programs for SMEs, illegal permits and licenses are also among the factors that hinder enterprise's growth. The Government through its policies is perceived to not have good will for the growth of SMEs (Jackson et al., 2008). In 2011, Okpara found out that the lack of financial support is a major factor that hinders the growth and survival of SMEs in Nigeria.

Meanwhile in Tanzania, SMEs have also played a critical role in developing Tanzanian economy through creation of employment opportunities, income generation, and equitable distribution of income hence contributing towards poverty alleviation (Mahemba and De Bruijn, 2003). As with elsewhere, this sector suffers several challenges particularly in domestic and global market competition. For instance, though varieties of opportunities in adapting supply chain management exist, the dominance of global supply chain systems raise adaptation challenges for small businesses (Mahemba and De Bruijn, 2003). According to Omidya network in 2012, in their paper "Accelerating Entrepreneurship in Africa" the major constraints faced by SMEs in Tanzania are insufficiency and unreliability of the infrastructure. Transport infrastructure is an additional hindrance, as the country has very poor quality and limited rail and road network, further making access to markets very difficult. The supply of electricity is equally very unreliable. These coupled with poor communication infrastructure has had a very negative impact on the growth of SMEs in Tanzania. The cost of obtaining finance and the vigorous requirement to be fulfilled to access financing magnifies these factors. This includes regulation as well as income taxes which at 46 percent are among the highest in the sub region.

Comparing the three country case studies, there exist commonalities in SME constraints. The major factors affecting SMEs in India were predominately limited access to finance and the impending difficulties to access it, the intermittent availability of electricity, the lack of technical knowledge, the lack of research and development facilities and finally the challenges in marketing of their products. The Kenya case study brought out lack of access to finance, challenges in the marketing of SME products and services and including political instability in the country. The other issues raised were high cost of compliance and the cumbersomeness of the laws and regulation. The last issue raised was the issues of corruption. The final case study of

Tanzania brought out lack of finance and vigorousness of the requirements to access funding. In addition, it highlighted difficulties in adherence to regulation with income taxes topping the list at 46 percent considered to be among the highest in the sub region. The last major factor constraining SMEs growth in Tanzania was the insufficient and unreliable infrastructure.

Meanwhile other empirical studies such as Heinonen (2011) focus on experiences of Kosovo. They illustrate that the external and internal issues affecting the growth of SMEs in Kosovo include external factors such as access to finance, competition, corruption and other barriers to trade. Internal factors – some deriving from the external ones – like management competences, lack of skilled labor, marketing strategies, innovation level and investments on technology all act as stressors (Laura Heinonen, 2011). Other factors include lack of access to finance, competition, corruption, globalization, laws and regulations, management competence, lack of skilled labor, and low investment in innovation, technology and marketing.

In the context of this dissertation, it is imperative to know the factors that affect the growth of SMEs because these have a negative impact on economic growth of a country. When the growth of SMEs is affected due to external or internal factors it ultimately distresses economic growth in a country (Dean et al., 1996; Karlsoon et al., 1993).

Similarly, other experiences such as those from Ghana also speak to wider SMEs and associated challenges. Recent studies show that SMEs in Ghana have a high failure rate despite receiving stimulus packages and copious government policy (Yeboah, 2015). The findings show that the educational qualification of the entrepreneur and size of the enterprise had the most significant influence on SME growth. This study concluded that the owners/managers of SMEs required education, even if not by formal schooling. They recommended that managers must periodically attend seminars and workshops to obtain the requisite knowledge and skills to advance their business growth. Entrepreneurs must not be driven solely by financial motives and must also avoid inertia that comes with operating a business.

The foregoing discussion has established that the current discourse on SMEs and economic growth and development serve its actors poorly: with discussions largely existing as jointed and more general. The context specific reality of SMEs as they relate to possibilities and a challenge remain less explored – and is the focus of this country-based study.

## **2.4 SMEs in the Zambian Context: Legal and Institutional Provisions**

The growth and expansion of the SME economy in Zambia can be traced back to the 1970s. It became clear by then the large-scale business sector – which continues to be predominantly mining – could not absorb the growing labor force amidst limited industrial growth and unemployment (MCTI 2007). Central to this development challenge was burgeoning rural-urban migration as the people moved to urban areas in search for employment. In response, the government created the Village Industry Service (VIS) in 1978. VIS was meant to encourage as well as provide support to rural communities to develop and utilize artisan craft skills as well as produce crafts that could be sold in exchange for money. In a move to formalize small business processes, the Small Industries Development Organization (SIDO) was formulated in 1981, which through an amendment of the Act during 1996 is now known as the Small Enterprises Development Board (SEDB). This organization was meant to provide larger volumes of support to those venturing into small businesses.

However, although government provided legislation, institutional provisions as well as a policy framework in the initial stages of the development of small businesses, the performance of these organizations have over time been constrained by the scarcity of resources. This has recently been compounded by lack of capacity to deal with increased demands of the small business sector more so in the post 1990s – the roll out period of neoliberal policies (Structural Adjustment Programs).

According to the Small Enterprises Development Act of 1996, a small business enterprise is any business enterprise whose amount of total investment, excluding land and buildings, does not exceed: 1) in the case of manufacturing and processing enterprises, fifty million Kwacha (K50 million US\$ 25,000) in plant and machinery; and 2) in the case of trading and service providing enterprises, ten million Kwacha (ZMK10 million or US\$ 5,000). The Act also considers SMEs whose annual turnover does not exceed eighty million Kwacha (K80 million) or (US\$ 40,000); and is employing up to thirty (30) persons. Legislation recognizing and supporting the development of the small business sector has been enacted through the Small Enterprises

Development Act of 1996, which is an improvement on the Small Industries Development (SIDO) Act of 1981. Table 2.1 below summarizes key elements as provided in the Act.

**Table 2.1: Smallholder industries development – key elements**

- |   |
|---|
| <ol style="list-style-type: none"><li>1.1. Incentives to micro and small enterprises in terms of tax exemption on income for up to five years;</li><li>1.2. Provision for manufacturing enterprises to operate without a manufacturing license as required under the law for up to five years;</li><li>1.3. Exemption from the payment of licensing fees required for such an enterprise under the law;</li><li>1.4. Exemption from the payment of rates on factory premises for five years;</li><li>1.5. The Trades Licensing Act shall not apply to an enterprise registered under the Small Enterprises Act, and;</li><li>1.6. Secure incentives through relevant authorities for any financial institution which undertakes to finance or develop an enterprise registered under the Act.</li></ol> |
|---|

*Source : The Small Enterprises Development Act Chapter 425 Of The Laws Of Zambia Chapter 425*

Since the 1990s, the Zambia has made efforts to improve the national institutional and policy climate in which small business operates. While previous efforts pursued the development of small businesses narrowly and single-handedly, recent efforts encouraged multi-level and multi-stakeholder approach. The involvement of donors and NGOs highlight this perspective. One outcome is that stakeholders are now actively involved in the development of the small business sector (MCTI 2007). Several organizations provide support to the small business sector, including government and quasi-government, private-sector actors and NGO actors. The support provided by most of these organizations ranges from training in business and management skills, consultancy services in business, technical assistance, marketing assistance, provision of credit, lobbying, etc.

However, despite support at national level, a lack of capacity in some of these enterprises means that only a limited set of services are being provided. For example, in the past the Small Enterprise Development Board (SEDB) and Village Industry Service (VIS) were unable to recover more than 50.0 percent of the loans they disbursed within the stipulated time periods.

Some of these challenges related to poor credit management systems. Over time, the loan funds meant for onward disbursement to the small business sector were tied up in uncollected debts. Eventually, this type of service became unavailable. Today, the SMEs sector is broadly characterized by the activities of enterprises engaged in the production of goods and services with the primary objective of generating employment and income to persons concerned. The reach and spread of SMEs has remained varied across the country, with much concentration in urban centers. Further, the SMEs are concentrated in the traditional economic sectors characterized by use of low technology, rely largely on social networks and inter-firm cooperation, and are oriented towards the local and less affluent segments of the market (Nuwagaba, 2015).

Most SMEs and especially the micro-sized have the characteristics of household enterprises. These have been operated mostly by a single person with or without the help of family members, and usually not licensed with a government agency (Nuwagaba, 2015). Their business activities are largely in trading, and simple manufacturing and only a small portion are engaged in service related businesses. The range of activities is usually in the production of consumer goods. Among their manufactured products include textile products, carpentry & other wood products, light engineering and metal fabrication, food processing, leather products, handicrafts and ceramics (Charles et al. 2017). The services sector includes restaurants and food preparation, hair salons and barbershops, passenger and goods transport, building construction, telecommunication services, business center services and cleaning services. The trading sector is largely concentrated in consumable products, industrial products, and agricultural inputs and produce. However, challenges in the formal policy and legislation as well as precarious state-business relations means many small businesses operate in the informal sector (Charles et al. 2017).

It is often argued that governments should promote SMEs because of their greater economic benefits compared to large firms-in terms of job creation, efficiency, and growth. (Elasrag 2012) In most developing countries such as Zambia, micro-enterprises and small-scale enterprises account for the majority of firms and a large share of employment. In Ecuador for instance, firms with fewer than 50 employees accounted for 99 percent of firms and 55 percent of employment in 1980; in Bangladesh, enterprises with fewer than 100 workers accounted for 99 percent of

enterprises and 58 percent of employment in 1986 (IFC,2000). A key feature to acknowledge here is that the relative importance of small producers varies significantly across countries, and within a given country, across stages of development and over time. Comparative studies around manufacturing show a common pattern in the transformation of the size distribution of firms as industrialization proceeds in low-income countries. Most firms are micro or small-scale, existing alongside a few large-scale enterprises. In some middle-income countries, medium-scale enterprises begin to account for a relatively larger share of production and employment, raising challenges for policy development.

In Taiwan, China for example, the size distribution of firms has remained relatively constant over the past thirty years, even as the structure of production changed from labor-intensive manufacturing to high-tech computer industries. On average, however, some studies argue that small scale enterprises play a declining role as countries development despite the recent shift in emphasis from large multinational firms to SMEs as witnessed in USA and Europe in the wake of the financial crises and economic own turns (IFC,2000). To poor countries such as those in sub-Saharan Africa like Zambia, recent trends and the structure of economies show that SMEs will continue to play a crucial role in local economies.

## **2.5 SMEs' Contribution to Economic Development and Growth**

Economic development is a process of economic transition involving the structural transformation of an economy through industrialization, rising Gross National Product (GNP), and income per head. Economic growth on the other hand, contributes to the prosperity of the economy and is desirable because it enables the economy to consume and contribute to more goods and services by increasing investment, increase in labor force, efficient use of inputs to expand output, and technological progressiveness. Any nation that experiences economic development and growth will benefit from improvement in the living standards especially if the Government can assist in growth by implementing complementary and growth-enhancing monetary and fiscal policies (Pass et al. 1993).

SMEs account for nearly 93.0 percent of the registered businesses in developing countries and therefore play an important role in economic development by providing employment opportunities, opening up new business opportunities, enhancing entrepreneurship, and fostering



creativity among many other things (Wang 2016). Kayanula and Quartey (2000) recognize them as the engines through which the growth objectives of developing countries can be achieved and are potential sources of employment and income in many developing countries. To Mensah (2005), SMEs act like sponges, soaking up surplus labor to provide a large share of employment and income.

Many researchers have observed that SMEs enhances competition and entrepreneurship therefore they suggest that direct government support can boost economic growth and development. SMEs boost employment more than large firms because they are labor intensive and make better use of scarce resources with very small amount of capital. Hellberg (2000) also states that developing countries should be interested in SMEs because they account for large share of firms and development in these countries. Young (1994) contended that SMEs are not only important because they are a source of employment but also because they are a source of efficiency, growth and economic decentralization.

Finally, SMEs are very important in the fight against poverty as they help in the poverty reduction strategy for most government especially those in the developing countries where poverty is most severe. Since they employ poor and low-income workers and are sometimes the only source of employment in the rural area, their contribution cannot be overlooked.

Post-colonialism, Africa has continued to face constraints that have retarded the growth of SMES. The constraints according to Fjose, Grunfed and Green (2010) include: access to electricity, civil wars, access to finance, corruption, political instability, tax rates and tax administration. Although stunted growth of SMEs has often been blamed on many of aforementioned factors, top of the challenges are tax rates and uncoordinated tax administration (Yitzhaki, 2006). Taxes confront the SME sector in various shapes and shades via: import duties, export and excise duties, sales and VAT, withholdings and income taxes, mobile advertising and billboard levies, education, levies, social responsibility charges among others (Terkper, 2007). Therefore, SMEs in Africa are faced with a number of factors that impede their growth and contribution to development of the continent.

In Zambia, although private enterprises can be traced back in the 19<sup>th</sup> century when Bantu and Ngoni people occupied the Eastern and Northern Parts of the territory (Green) and their

production was not associated with any kind of taxes (Asante, 2007), there growth was hampered by a number of factors. For instance, despite people largely depending on farming, fishing, hunting, and collecting wild edibles (Kasoma, 1986:9), they lacked technology which could have helped in producing large volumes and fight diseases that attacked crops and animals in the region. Due to this, entrepreneurship was practiced on a very small scale among themselves using barter system. The growth of private enterprises was also hampered during this time because economic powers were commonly controlled by the people in power like chiefs, kings and the political elite (Green). For example, when Europeans were attracted to precious resources such as ivory, gold and copper, chiefs assigned their trusted subordinates to conduct trade on their behalf. This is supported by Kasoma (1986:9) who posits that trading posts were opened in Feira by Portuguese and Arabs with the use of some indigenous as middlemen.

The coming of British explorers in the second half of 19<sup>th</sup> century and their acquisition of land from paramount chiefs through a number of treaties further hampered the growth of private enterprises. This is because in 1890 the whole territory came under British South African (BSA) Co. rule and in 1911; it came to be known as Northern Rhodesia (Mbikusita-Lewanika, 1990:43). Upon taking over the territory, the BSA Co. introduced poll and hut taxes to the natives. As a result of such an action, native tax receipts moved ahead steadily from 6,400 pounds in 1902 to 26,000 pounds in 1905, to 54,000 pounds in 1908 and to 72,000 pounds in 1914 (Fry, 1979:13). During this time, Africans were seen as a source of cheap labour and because of this, they were not allowed to engage in any business activities. This was achieved by putting trading licensing beyond the reach of all but a few Africans (Fry, 1979:14).

Therefore, colonial economic relations had not provided the necessary opportunities for the natives to come out of poverty but instead moulded underdevelopment. Tax together with other social-economic conditions created by colonialism undermined the subsistence economy's ability to provide for the livelihood of its population (Mbikusita-Lewanika, 1990:60). In this view, pre-independent, Zambia was characterized by a free-market system that was mostly beneficial to the Europeans resulting in unequal distribution of wealth (Mwewa, 2005).

In 1964, Zambia attained independence from British rule and the new United National Independence Party (UNIP) government under the leadership of Kaunda came up with a number of policies which were aimed at improving the livelihood of the natives. The major policies

included “Zambianisation”, Nationalisation and Humanism. Government also revised the tax system which was used by colonial masters to exploit the natives. This was achieved by enacting the Income Tax Act of 1966. The Act provided for a unitary system of income taxation, new procedures and penalties as well as the concept of Pay As You Earn (PAYE) were introduced, doing away with previous system based on arrears but rather on available disposable income (Mwandu, 2012). This move by government was cardinal to the growth of entrepreneurship among the local people because tax by nature reduces the ability to save and invest leading to less capital formation which can have a detrimental effect on the growth of SMEs. In this view, the new tax system aimed at encouraging people to save and invest so as to come out of poverty subjected to them under colonial rule.

However, it is important to note that since independence, there were no special policies aimed at growing the private sector where SMEs are concerned because the nation was enjoying high copper prices and government decided to take an active role in matters of national development. In this view, policies such as “zambianisation” which aimed at calling for local skills development, employment of Zambian nationals and transfer of skills to the local people during the tenure of foreign expatriates in the country (Molteno and Tordoff, 1974) did not succeed as anticipated because it did not advocate for direct ownership of the enterprises. Therefore, it had a negative impact on the growth of SMEs in Zambia.

Nationalization policies such as the Mulungushi reforms of 1968 and Matero reforms of 1969 also had detrimental effects on the growth of SMEs. This was because in the former, government transformed the economy from semi liberal to economic nationalization by acquiring 51,0 percent shares in enterprises that were in the key sectors of the economy such as retail, transport, and manufacturing firms through its newly created parastatal - Industrial Development Corporation (INDECO); while in the latter, it purchased 51.0 percent or more shares from the existing mining companies: Anglo American Corporation and Roan Selection Trust, leading to partial nationalisation of the copper industry. As a result, 80.0 percent of the economy was now under state control (Noyoo, 2011). For example, government established nearly 80 parastatals by 1975 and it owned controlling shares in most of them. The government further restricted the growth of private sector by clearly indicating that when a private enterprise grew to a certain level, it would take ownership (Mwewa, 2005). The implication of this move by government

meant that Zambians did not have the economic freedom which they fought for during the colonial era and this had a negative effect on the growth of SMEs.

Government further worsened the situation when Humanism became officially the country's political philosophy in 1974 when Zambia became a one party state. Humanism involved the inclusiveness of traditional African society which was characterized by the extended family in which people helped one another. Through Humanism the state took necessary measures to prevent human exploitation by putting strict measures on the development of the private sector where SMEs belong. Humanism had detrimental effect on the growth of SMEs because it restricted retail trading in various towns of the country and more industries were taken over (Kasoma, 1986:17). Therefore, the conditions created by government in the first republic coupled with high levels of poverty among the black Zambians further killed the entrepreneurship spirit which consequently, hindered the growth of the private sector and subsequently, SMEs in Zambia.

At the dawn of the second republic in 1973, Zambia was hit with a massive increase in the price of oil followed by a slump in copper prices in 1975, resulting in a diminution of export earnings. It is significant to note that in 1973 the price of copper accounted for 95.0 percent of all export earnings; this halved in value on the world market in 1975 as copper prices collapsed from 870 pounds in 1974 to 550 pounds in 1975. The GDP declined to -19.0 percent in 1975 from 32.9 percent in 1974 and 13.5 percent in 1964 respectively, while poverty levels increased drastically 70.0 percent placing Zambia among the poorest countries in the world (Chisala, 2008). Government thought that the failing of copper prices was temporary. As a result, it borrowed heavily to maintain levels of consumption in the economy. In this view, foreign debt mounted rapidly while GDP growth dropped to 0.5 percent. By 1976 Zambia had a balance-of-payments crisis and rapidly became massively indebted to the IMF. Instead of initiating a process of structural adjustment and encourage diversification (i.e. encourage the growth of the private sector), government chose to adopt regulatory policies. Subsidies and fixed consumer prices protected urban consumption, while the mining sector and state-owned manufacturing were favoured through import-licensing and foreign exchange allocation. Growth remained unresponsive to this new interventionist strategy. In this regard, government acknowledged the failure of its policies in 1978 (Thurlow and Wobst, 2000:3).

In 1981, government made an attempt to support the SMEs in the hope of recovering from the economic shocks the country was going through. Therefore, the Small Industrial Development (SID) Act of 1981 was formulated. In support of the SID Act, provisions were made in the Fourth National Development Plan of 1989 to provide infrastructure for operations of Micro Small and Medium Enterprises (MSME), promote access to credit for MSMEs with growth potential and to improve production capacities of MSMEs with the view to increase incomes and employment. The resources to the MSME sector were to be made available through Small Industries Development Organisation (SIDO), Development Bank of Zambia (DBZ) and Village Industries Services (VIS), which were the primary source of small enterprises support. However, MSME support institutions suffered from inadequate funding and poor management. This led to the inability to effectively service the private sector and subsequently, hindered the growth of SMEs (MCTI, 2008).

Due to government's failure to fund public services and revamp the economy, it turned to IMF/WB for help. Instead of IMF/WB giving money to government, they gave it a set of economic policies which involved Structural Advancement Programs (SAPs). However, Zambia's economy did not improve. This led to government abandoning the implementation of SAPs and introduced a New Economic Recovery Programme. Nevertheless, the economic policies implemented during the second republic did not contribute effectively to the growth of SMEs due to lack of political will and their partial implementation by UNIP government. By 1990, there were 280 state owned enterprises (SOEs) (ZPA, PRNo. 17) throughout the country and there are no statistics showing the number of private enterprises because the economic policies that government had put in place did not advocate for the growth of the private sector. Therefore, the first and second republic saw government not doing much in promoting SMEs' growth and proclamations that were made to develop the sector were just for political rhetoric.

In 1991, Movement for Multi-party Democracy (MMD) government came into power on a manifesto anchored on economic liberalisation and political pluralism. Therefore, in 1992, government formally embarked on an IMF/WB supported structural adjustment and economic reform programme (Hoy, 1998) which focused on policies including: removal of subsidies, economic liberalization and stabilization, privatization of State-owned enterprises, retrenchment of workers in the civil service and SOEs, promotion of private sector participation and tax policy

reforms. The basic idea was to free government from direct involvement in industrial and commercial activities, that is, divest industry into private hands. The basic strategy of the programme was to restore internal and external balances between income and spending and to re-allocate resources from less productive sectors. The private sector where SMEs belong was expected to generate productive, competitive and sustainable growth supported by an enabling environment through government policy (UN, 2001:17). This was good for the SME sector because the environment had been prepared under which it would blossom.

The liberalization of the economy came with profound reforms in Zambian taxation system and tax laws were launched in 1992. This was done to improve government revenues which had declined from the peak of around 30.0 percent of GDP in the late 1970s to just 13.0 percent of GDP from tax collections in the early 1990s. To improve revenue administration, Zambia Revenue Authority (ZRA) was established in 1994 as a semi-autonomous agency under the ZRA Act. This important development along with policy measures on income tax rates and customs tariff reform, as well as the introduction of VAT saw the contribution from tax collections rise to more than 18 percent of GDP. In 2003, presumptive taxes were introduced by government to cater for SMEs in the informal sector. The four types of presumptive taxes include: Base tax assessed on lump-sum tax of K150 per annum for traders in markets; Presumptive motor vehicle tax for public service vehicle based on sitting capacity; Turnover tax - based on turnover of below K800, 000 and taxed at 3.0 percent and; Advance Income tax levied on imports of unregistered or non-compliant taxpayers (JCTR, 2011).

As of 2015, the taxpayer population of Zambia for SMEs stood at 197,059, with majority (120,922) been small enterprises while minority (76,137) been medium enterprises. They contributed K6,735,549,814.22 in 2015 and K6,705,205,180.49 in 2016 to ZRA alone (ZRA, 2017). SMEs in Zambia are made to pay tax and other charges to central and local governments and many other institutions such as PACRA. Even institutions that have been created to oversee the development of this sector such as ZDA charge SMEs just for them to get information on how they can grow their businesses. Considering the fact that the total investment to be regarded as a small enterprise in Zambia is between K80,000 and K200,000 while for a medium enterprise is between K201,000 and K800,000 (MCTI, 2008), the contributions made by SMEs to ZRA and other government institutions can have a detrimental effect on their growth. This is attributed to the fact that SMEs have other costs to meet in their operations. Moreover, these are enterprises

that need to be nurtured because there are in transit. Perhaps this can be the reason why the number of SMEs in Lusaka has been declining (LCC Official Database, 2017)

Apart from tax reform policies, government passed a Privatisation Act in June 1992. The objectives of the Act were to: provide for the privatisation and commercialisation of State owned enterprises; provide for the establishment of the Zambia Privatisation Agency and define its functions and; provide for the sale of shares in State owned enterprises (Privatisation Act of 1992). After a slow start of the privatization process, large numbers of parastatals began to be privatized in 1995 and 1996. At the end of 1994 15 companies had been privatized; by June 1996 this had risen to 137 and the total was 257 at the end of 2001 (Situmbeko and Zulu, 2004). Privatization process was followed by the implementation of Public Sector Reform Programme (PSRP) in 1993 by government with an aim of cutting down expenditure on administration, primarily by reducing over manning in the civil service. The outcome of the privatization and PSRP was large-scale job losses. The end result of these programmes was that formal employment fell below expectation. For example, a between 1991 and 2001, 200,000 employees were retrenched from formal sector (IMF and WB, 2004:9). There were more likely to result in direct or indirect of job losses, lower productivity and closure of MSMEs. This would further retard MSMEs contribution to economic growth.

Privatization of SOEs coupled with trade liberalization killed most of the industries in Zambia because they could not compete favorably on the market with imported goods from companies that had already attained economies of scale. The removal of import tariffs made it difficult for these companies to compete with imported products. For this reason, chronological trends in company performance revealed that almost two-thirds of the companies declined within the period of 1992-2000 and majority of smaller companies experienced negative growth (Serlemitsos and Fusco, 2003). Moreover, Serlemitsos and Fusco (2003:25) alludes that just after trade liberalization, one of the most complaints from various industries was the tax structure concerning duties for finished goods and raw materials. Most of the times there was no duty on imported finished goods while duty on imported raw materials was relatively high. This made privatised industries that used to produce such as Dunlop, Colgate-Palmolive, and Lever Brothers relocate their production to neighboring countries (Situmbeko and Zulu, 2004) thereby killing the growth of the private sector where SMEs belong. Nevertheless, there are certain companies that were successfully privatized and in the long run, they have had a positive effect

on the growth of SMEs in Zambia. For example, mining companies such as KCM has been supporting SMEs in various ways. In 2003 for instant, KCM undertook a SME Supplier Development in collaboration with IFC. Under this program me, 23 SMEs underwent capacity building and were assisted in the procurement of business from KCM. In 2006, KCM awarded 70.0 percent of service contracts and commodity contracts to local suppliers mostly SMEs (Chisompola, 2009).

In view of redundancies and retrenchments that came as a result of the implementation of SAPs, government formulated remedial policies and programmes which aimed at growing SMEs. As a result, in 1994 it established the Industrial, Commercial and Trade Policy (MCTI, 2008:10). However, the MSMEs still continued facing a lot of challenges and did not blossom. This made government to revise the SID Act of 1981 and replaced it with the Small Enterprises Development (SED) Act in 1996. The objectives of the SED Act were to: provide for the establishment of the SED Board and define its functions; establish the Micro and Small Enterprise Development Fund; provide for the development of the micro and small enterprises; provide for the registration of micro and small enterprises and; repeal and replace the SID Act of 1981. The aforementioned objectives were going to be achieved through: an establishment of the Small Enterprise Development Board which was a body corporate subject to the provisions of SED Act, to do all such things as may by law do or perform; in order to facilitate the flow of financial resources to the small scale sector, the Board was going to provide financial services on its own or in cooperation with other promotional agencies; it was also going to identify small entrepreneurs, institutions and projects which required financial assistance and; it was going to provide information on sources of finance and promote local investment for micro and small enterprises among others (MCTI, 2008) .

The SED Act further stipulated incentives for micro and small enterprise. The incentives included: exemption from payment of tax on income for; the first three years of operations for an enterprise operating in an urban area; and The first five years of operations for an enterprise in a rural area; operating of a manufacturing enterprise for the first five years without a manufacturing license required for such an enterprise under any law; exemption from the payment of licensing fees required for such an enterprise under any law; and exemption from the payment of rates on factory premises for the five years (MCTI, 2008:11). However, most of



these incentives were never implemented partly because the systems for their implementation were never put in place. The SED Act had negligible impact on the development of SMEs as it was just a mere public pronouncement with little effort to implement it (MCTI, 2008). This had a negative effect on the growth of MSMEs in Zambia which further resulted in an increase in poverty levels. For example, PRSP reports that the percentage of the population living below the poverty line increased from 69.7 percent in 1991 to 73 percent by 1998 (GRZ, 2002).

Other remedial programs to grow the economy and inculcate the entrepreneurship spirit included Future Search which was established in May 1995 by Management Systems of International of Washington DC funded by WB as one of Government's Social Safety Nets under the purview of the Public Service Management Division Cabinet Office. It was designed to provide outplacement services to retired and retrenched Public Servants. It aimed at educating and equipping people who lost their jobs through redundancies with skills to adapt to the new situation and able to continue earning a living outside formal employment. For those who lost jobs, the entrepreneurial spirit was ignited as they needed to survive. Future Search believed that changing mind set was the major catalyst to the development of SMEs in the country. This led to the mushrooming of small businesses and buying some of the privatized companies by the Zambians (Mwewa, 2005). For example, when Chilanga Cement Limited was sold, 37.0 percent of the shares were leased to the general public (ZDA, 2010). Those who had resources managed to buy the shares. In this view, private sector started to grow bit by bit and by 1998, a total 236 SOEs were privatized (IMF and WB, 2004).

To further encourage the entrepreneurship spirit, the government established TEVETA an institution created under the Technical Education, Vocational and Entrepreneurship Training Act No. 13 of 1998. TEVETA was established with a view of providing training in technical education, vocation and entrepreneurship to citizens so that they can start their own businesses in that government was no longer creating jobs. So the only way to enhance citizens' survival was to look at ways of growing and developing the private sector where SMEs belong. Therefore, through TEVETA, the government together with other co-operating partners such as WB works closely to develop skills for the country and this in return enhances the growth of SMEs. For example, the World Bank had supported improvements in technical and vocational training (TEVET) through a US\$25 million credit. The project focused on developing a TEVET system

that was going to improve the skills for both formal and informal sectors of the economy through creation of a high quality, sustainable, demand-driven, and equitable training system. Progress had shown that 95 percent of employers perceived TEVET training to be relevant and of good quality (World Bank, 2010:23). Therefore, this led to the growth of the private sector where SMEs belong. This can be attributed to the fact that between 1993 and 1999, there was a decline of employment in the formal sector as earlier alluded and an increase of employment in the informal sector. CSO (1999) estimated that informal sector employment had grown substantially during 1993 to 1998 period with 35.0 percent in agricultural employment and 15.0 percent in non-agricultural employment. For this cause, by 2000, Lusaka City Council reported that there were a total of 487 small businesses in Lusaka city. However, there were no any medium enterprises (LCC, Official database).

In 2005, the government and other stakeholders realised that the cost of doing business in Zambia was too high and this was affecting both foreign and domestic investments. Despite the challenges which SMEs had, Lusaka City Council revealed that in 2005, the number of SMEs had increased and stood at 8,141 for small businesses and 2,476 for medium businesses (LCC Official Database). Therefore, government had to come up with ways of ensuring the continuous growth of the private sector. This made government to launch the Private Sector Development Reform Programme (PSDRP) with an aim of reducing the cost of doing business in the country and encouraging competitiveness in the private sector. The PSDRP was formulated primarily for laying the foundation for faster and sustained private sector led growth by improving the investment climate. In relation to SMEs, PSDRP aimed at citizens' empowerment and the specific objective under this was to "unlock the growth potential of the MSME sector through business development support and local empowerment initiatives" (Siame, 2007:5).

Some of the notable achievements of PSDRP include: establishment of Citizens Economic Empowerment Commission which has funded over 1,800 projects and has disbursed over K66,083,588,097 to entrepreneurs (CEEC database) since its inception in 2006; establishment of Zambia Development Agency in 2006 and through its MSME Division facilitates skills training packages ranging from generating business plans to pre-retirement counselling and entrepreneurship skills; It also provides Business Linkages Programme that involves fostering business linkages between large corporations and local MSMEs and; Access to appropriate operating premises and business infrastructure like Industrial Parks such as the MFEZ in Lusaka

which targeted large and hi-tech companies. This may lead to the growth of SMEs through the development of supply chain where for instant, MFEZ law encourage MFEZ companies to source a certain percentage of raw materials and intermediate goods from home grown enterprises (Chisala, 2008). Therefore, as of 2017, a total of 2,225 SMEs countrywide were registered with ZDA out of which 1,015 SMEs were from Lusaka city (ZDA, 2017).

Another notable achievement of PSDRP was an approval of the MSME policy (Siame, 2007:7) and in 2008; the policy was adopted with an aim of creating a vibrant, dynamic sector that contributes 20.0 percent of GDP and 30.0 percent annually to creation of decent employment by the year 2015. The Policy aimed at achieving the following development objectives:- To facilitate creation and development of viable Micro Small and Medium Enterprises that contributes 30.0 percent towards annual employment creation and 20 percent towards GDP by the year 2018; To facilitate an increase of 10.0 percent towards utilisation and value addition of local raw materials in identified regional areas by the year 2018; To strengthen forward linkages between MSMEs and large scale companies by facilitating an annual increase of 10.0 percent in subcontracting of MSME by large scale companies; To improve productivity in the MSME sector by 10.0 percent by the year 2018; To enhance Local Economic Development thereby stimulating broad based economic growth by establishing five (5) Business Incubators and five (5) Industrial Parks in identified locations by the year 2018. This was very effective for the sector because there was a legal framework guiding on how it can blossom and later on contribute to economic growth, creation of employment and reduction in poverty levels. With the implementation of the MSME policy, the number of enterprises in Lusaka city continued to go up and as of the year 2010, number for small businesses stood at 20,114 and medium businesses stood at 5,136 (LCC Official Database).

The private sector has also played a part in spearheading the growth of SMEs in Zambia. For example, in 2000, ZCSMBA was established as a national body to represent the interests of SMEs in the country. Other programmes aimed at growing the private sector are also run by YWCA, ILO, WB, WTO, UNIDO and many more organisations (Mwewa, 2005). World Bank for example helps to design dozens of projects that assess and address the difficulties of reaching small business owners with services, which include anything from credit and technical assistance, to exports markets, value chains, technology and more (WB, 2010). For example, the International Finance Corporation (IFC) is the World Bank's "Private sector arm", and has been

scaling up its programs in Zambia in recent years. IFC has a project aimed at expanding the Copperbelt SME Suppliers Development Program. This program provides customized technical assistance to 150 SMEs that supply the mining companies. IFC is also providing investment support and technical assistance to a variety of other SMEs in partnership with the Development Bank of Zambia (WB, 2010).

ILO on the other hand assists government to improve policy and regulatory framework for small enterprise development; it also develop innovative methods to improve competitiveness and working conditions in small enterprises and help them to enter new markets; they also train women and men in how to start a business successfully and make it grow. For example, ILO is also helping the Zambian government to implement the Zambia Green Jobs Programme (ZGJP) which a sustainable development programme that facilitates private sector development for inclusive green growth, more and better jobs particularly for young people and women (UN and GRZ, 2015). In this regard, by 2015, there were 22,338 small businesses and 5,050 medium businesses in Lusaka city. However, there was a decline in the number of medium businesses in 2015 and this had continued in both categories in that as of 2017, there were 13,529 small businesses and 2,885 medium businesses (LCC Official Database). This is sad for the sector especially after 20yrs plus of implementing SAPs and 10yrs of implementing the MSME policy Therefore, it is worth noting that although various policies and programmes have been put in place to promote entrepreneurship, there are still a lot of challenges that hinder the growth of SMEs in Zambia. Many promising entrepreneurs in Zambia are faced with so many constraints that the estimated rate of failure for start-ups is as high as 65.0 percent over a period of three years compared to an estimate of less than 50 percent in Europe over a period of five years (WB, 2013). SMEs are also faced with competitions from predators such as MNCs; Limited access to markets; Limited access to appropriate technology, machinery and equipment; Limited access to suitable business financing solutions; Inadequate business infrastructure such as roads and telecommunication facilities; Limited technical and management skills; Inadequate and unsuitable operating premises that can facilitate enterprise growth and; Lack of legal protection by the state, for example the tax policy (MCTI, 2008). All these business constraints and challenges manifest themselves in the failure by the SME sector to grow into a viable bottom up development tool and effectively contribute to national development.

## CHAPTER 3: METHODOLOGY

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### 3.1 Introduction

This chapter focuses on the methodology. It aims to highlight the research design, target populations of the study, data sources, sampling frame, techniques and sample size, data collection methods and tools, reliability and validity of study instruments, ethical consideration and data analysis.

### 3.2 Research Design

A research design can be thought of as the structure of research. It is the glue that holds all of the elements in a research project together. It is a conceptual structure within which research is conducted. A design is used to structure the research, to show how all of the major parts of the research project work together to try to address the central research question (Kombo and Tromp, 2014). This research followed an empirical and non-experimental approach because it was carried out in a natural and uncontrolled setup without a control group or treatment given to the respondents (Bless and Achola, 1990). The study adopted the mixed method approach to incorporate both the qualitative and quantitative approaches. It was exploratory because it emphasised the need to describe or explore factors that constraint SMEs contribution to economic growth of in Zambia. Mixed methods are a methodology for conducting research that involves collecting, analysing and integrating quantitative (e.g. experiments, surveys) and qualitative (e.g. focus groups, interviews). The justification of using this approach is that it gives an opportunity to collect more insights on the topic using both qualitative approaches and gives systematic information that is collected using qualitative approaches by use of structured questionnaires

The challenges and advantages of using mixed methods approach:

The major challenges are:

- Failure to understand the context and setting in which data is collected is one of the major weakness of quantitative research
- It is also more time consuming to collect both Qualitative and Quantitative data.
- Collection of both types of data requires more financial resources

The major advantages are:

- Combining both words and numbers to communicate the results and finding would appeal to a wider audience.
- Personal biases of the research is reduced by combining methodologies
- Additional evidence and support for the findings is provided by using both approaches

### **The Qualitative approach**

Primarily, face to face interviews were conducted with key informants using unstructured questionnaires. The major organisations interviewed were ZDA, ZRA, ZCSMBA and MCTI. The information that was collected is presented in narrative form. With this approach, we further reviewed published documents that include SMEs policies, ZDA, SMEs Association and similar studies reports. The objectives of the study to establish whether the factors constraining the SMEs growth in sub-Sahara Africa are similar across different sectors and explore the wider policy and institutional environment in which SMEs operate in Zambia were addressed using the qualitative methods. This was on account of the kind of data which was supposed to be collected; Most of it was qualitative in nature.

### **The Quantitative approach**

This approach involved the collection of statistical information systematically using structured questionnaires. Face to face interviews with SMEs (respondents) was preferred in order to guide the respondents to answer all the questions. The objectives of the study to identify factors constraining SMEs' to optimal contribute to economic growth in Zambia and determine the association between internal/external constraint factors and economic growth in Zambia were addressed using quantitative approaches.

### **3.3 Target Population**

The target population of the study were SMEs from selected industries and selected stakeholders namely; ZDA, MCTI, ZRA and ZCSMBA involved to providing support to SMEs.

### **3.4 Data Sources**

This study collected data from two main sources with the view to achieve the objectives and valid conclusions. The data was collected from primary and secondary sources. The primary source was the administering of questionnaires to the respondents. The secondary sources included reviewing already published documents on the topic. As stated by (Borrego et al., 2009), no single data source has complete advantage over all other sources. Hence, qualitative research should try to use as many different sources as possible.

- **Primary Data**

Self-administered questionnaires and interview guide were used as the main research instruments to gather the primary data for the study. Structured questionnaires were used to gather unbiased opinion of respondents and the interview guide to clarify unclear issues from the SMEs. Both open and closed ended questions, based on the objectives of the research, were used. The open ended-questions were used to gather the opinions and views of the respondents such as challenges being faced as well as the possible solutions for the identified challenges of the study topic.

- **Secondary Data**

Secondary data for this study was collected from various reports, the ZDA, ZIPAR, CSO reports and other business bulletins published by Ministry of Finance relating to SMEs growth and their performance. The secondary data also consisted of issues regarding SMEs reports on their operations, challenges and support they receive.

### **3.5 Sampling Frame, Technique and Sample Size**

Sampling design is a process of selecting an appropriate number of units from the population of interest to provide accurate information about the entire population (Hair et al., 2003). For an equal representation of SMEs across sector, stratified random sampling was used.

The sampling frame for the survey was the dataset from Central Statistical Office. The Statistical Business Register (SBR) contains a list of all enterprises in Zambia and it has 69,097 establishments. The SBR is routinely updated with data from administrative sources such as the Zambia Revenue Authority (ZRA) PACRA, ZDA, RDA and NCC, providing a good source of

SMEs across various sectors. A sample of 250 enterprises was randomly selected from the frame.

Participants from the key informants were deliberately selected based on their knowledge of SMEs and the local economy. Through a snowballing technique – where respondents are asked to recommend other participants – a total of 3 interviews per institution were conducted (12 interviews). The main interviewees were government actors and industry experts.

These were mainly officials from the ZDA, ZCSMBA and MCTI. In the case of ZDA the main person interviewed was the Director Enterprise Development and the Permanent Secretary at the ministry in the case of MCTI. The person interviewed for ZCSMBA was the Executive Director. These in turn recommended the key informants to interview. The institutions were selected on the premise that the ZDA was the government arm which fostering economic growth and development through promoting development and trade. The MCTI was responsible for administering national policy for the private sector on behalf of Government while the ZCSMBA is a non-governmental organisation responsible of presenting the concerns of the SMEs sector to government. The main essence of interviewing the ZCSMBA was to get a non-biased view on the factors the SMEs were facing leading them to fail to contribute effectively to economic growth in Zambia and then relate these to quantitative data from SMEs.

Enterprises were first grouped by industry and then further grouped into two (2) strata within each industry, based on the number of employees (SMEs). Probability sampling technique was employed in the research as it ensures good estimates of the population characteristics (Malhotra, 2010). Proportionate stratified sampling considered enterprises for each of the industries. The sampling unit was an enterprise. A single random sampling method was applied to select enterprises from each stratum. This method is one in which the sample is selected in such a way as to afford every individual of the population the same chance of being selected (Yin 2014).

### **3.6 Data Collection Methods and Tools**

The study adopted a self-administered questionnaire, containing closed-ended questions as well as open-ended questions, as a data collection tool. Questionnaires were given to the respondents to complete the questionnaire on their own and at their own convenience. This was important as SMEs could not always have time to sit continuously for interviews or focus group discussions.



Self-administered questionnaires also ensure that costs are minimized. They also ensure that the study is free from the bias of the interviewer as answers will be in respondents' own words. The other advantage is that respondents are given adequate time to think through responses whilst less approachable respondents can easily be targeted (Kothari, 2004). For respondents that proved that they could not understand the topic, face to face interviews were used in brief to clarify any questions, ensuring collection of precise information.

### **3.7 Reliability and Validity**

Validity and reliability are crucial in any scientific research. Validity refers to the extent to which a test measures what we wish to measure. Reliability considers the accuracy and precision of a measurement procedure (Kothari, 2004). Validity refers to the extent to which a measurement does what it is supposed to do (Kothari, 2004). Data need not only to be reliable but also true and accurate. If a measurement is valid, it is also reliable but if it is unreliable, it may or may not be valid. In this study, data were computerized and checked for its accuracy to make sure that they give valid results.

Reliability refers to the consistence, stability, or dependability of the data. The reliability of an instrument is increased by identifying the precise data needed and repeated use of the instrument in field testing (Yin, 2014). To guarantee reliability of this study, a pre-test was conducted with some enterprises. This was used to identify questions that might be unclear or ambiguous to them. This also gave the researcher an opportunity to appreciate the sort of data that was being collected and how these responded to the study questions. The questions that generated less clear responses were revised to improve reliability of responses during the final process of data collection (Yin, 2014). Reliability was also ensured and improved by designing directions for measurement with no variation from group to group, using trained and motivated persons to conduct the research and by broadening the sample of items used (ibidi.).

### **3.8 Ethical Consideration**

The researcher was solely responsible for conducting the whole research process. The researcher abided by the policies governing the enterprises in Zambia as well as the University of Cape Town. The data was not being transferable by any means between persons or enterprises. Both confidentiality and anonymity were maintained on behalf of the informants who participated or

shared their information in this study. There was no coercion or force to take advantage of the informants. Full voluntary guarantee will be sought from the informants. From the enterprises, consent was sought by delivering to the enterprises an introductory letter of me and the institution am studying from (University of Cape Town).

### **3.9 Data Analysis**

The data entry screen was developed in SPSS after the finalisation of the questionnaire and was used to capture data from the questionnaires. The answered questionnaires were checked for uniformity, accuracy and completeness. Responses were coded and entered into the code sheet to facilitate computation. This helped in establishing, analysing and interpreting the various relationships between the variables. This necessitated good presentation in graphical form for easy presentation of data. The data was captured in a way that allowed generating descriptive narratives and key themes around the objectives.

Descriptive analysis was used to analyse all the quantitative data on the factors constraining SMEs from contributing to economic growth. This involved in the production of descriptive tables and cross tabulations among variables.

In assessing the existing policy and institutional frameworks that support SMEs and constraining factors, qualitative data on the other hand were grouped in key themes. This involved coding each questions response and then allocating a unique figure to each response and question, i.e. some descriptive measures can be allocated. This involved reading through all responses to the questions and grouping them according to responses that is, picking similar ones and grouping them in one category. Responses that were not similar were also grouped in different categories and interpreted accordingly. The overall aim was to maintain the grounded insights about SME processes and factors that determine growth and outcomes in Zambia. Any conflicting responses was treated as data in themselves and analysed and interpreted accordingly (Yin 2014).

## CHAPTER 4: ANALYSIS AND RESULTS

### 4.1 Introduction

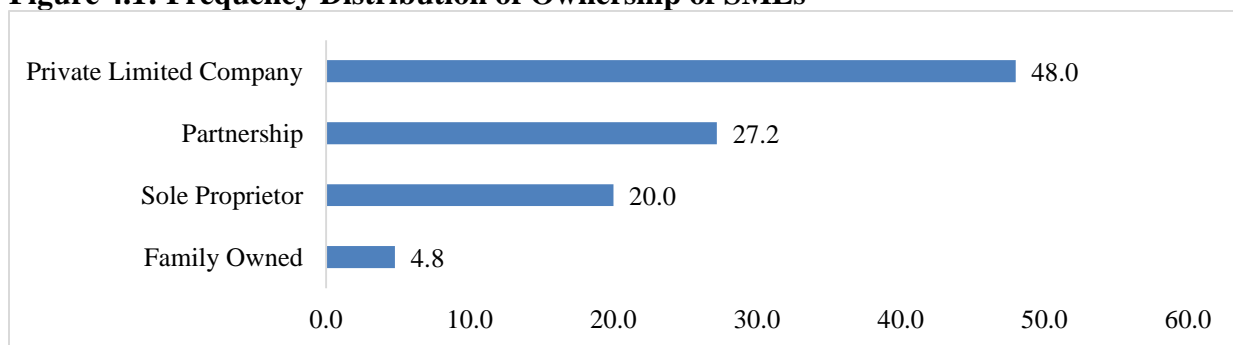
This chapter focuses on the analysis and results of the study. The chapter is organized in three main sections that draw from the Research Objectives (Section 1.5.2). The chapter explores the national context, policy and institutional context (Section 4.2), SMEs and related constraining factors (Section 4.3), and dynamics related to whether constraining factors can be viewed as generic or sector specific (Section 4.4).

### 4.2 Background Characteristics

#### 4.2.1 Ownership

Of the total 250 respondents, the majority 48.0 percent were in the private limited company. The minority of the respondent's 4.8 percent were in family owned enterprises.

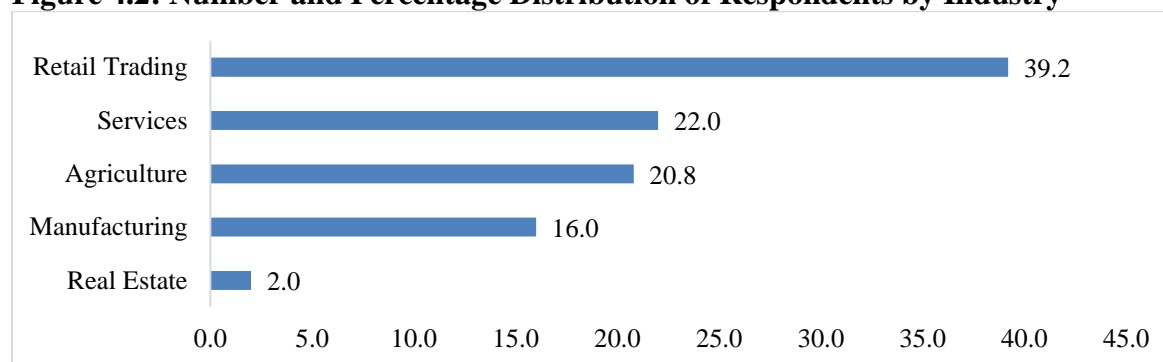
**Figure 4.1: Frequency Distribution of Ownership of SMEs**



#### 4.2.2 Industry

SMEs cut across various sectors of an economy, and as Figure 4.2 shows, responses received were fairly spread across selected industries. SMEs dominated the retail sub-sector at 39.2 percent, followed by services 22.0 percent and agriculture accounted for 20.8 percent. Manufacturing and real estate industries followed at 16.0 percent, and 2.0 percent, respectively.

**Figure 4.2: Number and Percentage Distribution of Respondents by Industry**



### 4.2.3 Employees

Of the total 531 reported employees, majority 73.6 percent were employed in the small enterprises and 26.4 percent were employed in the medium enterprises. By industry, majority of the employees were working in the retail trading industry accounting for 33.3 percent. The lowest number of employees was reported in the real estate industry at 0.9 percent.

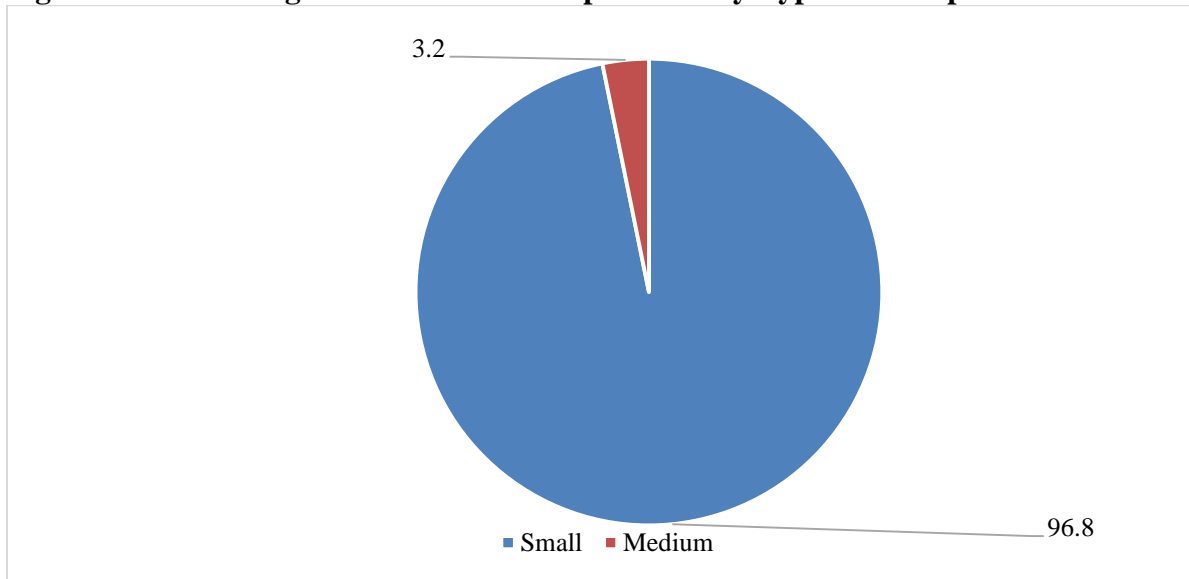
**Table 4.1: Number and Percentage Distribution of Employees by Type of enterprise and Industry**

Business activity	Type of Establishment					
	Total		Small		Medium	
	Number	Percent	Number	Percent	Number	Percent
Total	531	100	391	73.6	140	26.4
Agriculture	121	22.8	81	66.9	40	33.1
Manufacturing	74	13.9	62	83.8	12	16.2
Real Estate	5	0.9	5	100.0		0.0
Retail Trading	177	33.3	159	89.8	18	10.2
Services	154	29.0	84	54.5	70	45.5

### 4.2.4 Type of Enterprises

The findings in figure 4.3 show the percentage distribution of respondents by type enterprises. It shows that majority 96.8 percent were among the small establishments and 3.2 percent account for the medium establishments.

**Figure 4.3: Percentage Distribution of Respondents by Type of Enterprises**



SMEs are heterogeneous rather than homogenous. Their capabilities as well as market integration vary within and across different sectors. As Table 4.2 shows, the bulk of the SMEs ( $n=81$ , 32.4 percent) cluster around an average monthly turnover of over ZMK25,000 compared to 28 percent ( $n=70$ ) with a monthly turnover of between ZMK15, 000 and ZMK20,000. The rest of the SMEs were either below ZMK5,000 monthly turnover or between ZMK10,000 and ZMK15,000.

**Table 4.2: Average monthly turnover of SMEs**

Amount	Frequency	Percentage
Below ZMK10,000.00	40	16
ZMK10,000.00 to ZMK15,000.00	69	27.6
ZMK15,000.00 to ZMK25,000.00	70	28
Above ZMK25,000.00	81	32.4
<b>Total</b>	<b>n=250</b>	<b>100 percent</b>

#### **4.3 Factors that Constrain SMEs from Contributing to Economic Growth**

One of the objectives of the study was to explore the factors that constrain SMEs in contributing to economic growth. The findings show that lack of finances is the most stated constraining SMEs in contributing towards economic growth accounting for 21.5 percent. The other state factors were competition, high utility tariffs and infrastructure accounting for 20.0 percent each.

The findings further show that there are no significant differences within categories on the type of establishment in identifying or stating the constraints.

There are similarities in the constraints stated regardless on the type of establishment (table 4.4). The same pattern is observed when perceived constraints are produced by ownership of the enterprise. Within enterprise ownership categories (table 4.5); the responses are uniform; meaning the constraints are the same for all categories as shown in the tables below.

This is further observed among enterprises regardless of the number of years they have been operating/the core business they are doing (table 4.6 and table 4.7).

**Table 4.3: Factors Constraining SMEs**

<b>Factors</b>	<b>Number</b>	<b>Percent</b>
Taxes as constraint	97	18.5
Competition as constraint	105	20.0
High utility tariffs as a constraint	113	20.0
Lack of finance as a constraint	105	21.5
Infrastructure as a constraint	105	20.0
<b>Total</b>	<b>525</b>	<b>100</b>

**Table 4.4: Factors constraining SMEs by Type of Establishment**

<b>Constraints</b>	<b>Type of Establishment</b>		
	<b>Small</b>	<b>Medium</b>	<b>Total</b>
Taxes	93	4	97
Competition	101	4	105
High utility tariffs	109	4	113
Lack of finance	101	4	105
Infrastructure	101	4	105
Total	117	4	121

**Table 4.5: Factors constraining SMEs by Enterprise Ownership**

<b>Constraints</b>	<b>Enterprise ownership</b>				
	<b>Private Limited Company</b>	<b>Sole Proprietor</b>	<b>Family Owned</b>	<b>Partnership</b>	<b>Total</b>
Taxes	42	19	3	33	97
Competition	47	20	3	35	105
High utility tariffs	52	22	4	35	113
Lack of finance	48	20	4	33	105
Infrastructure	48	20	4	33	105
Total	56	22	4	39	121

**Table 4.6: Factors constraining SMEs by Number of Years Operating**

Constraints	Number of years operating					
	1	2	3	4	5	Total
Taxes	20	20	15	21	21	97
Competition	20	21	19	24	21	105
High utility tariffs	22	18	21	27	25	113
Lack of finance	21	17	18	26	23	105
Infrastructure	21	17	18	26	23	105
Total	23	22	23	28	25	121

**Table 4.7: Factors constraining SMEs by Business Activity**

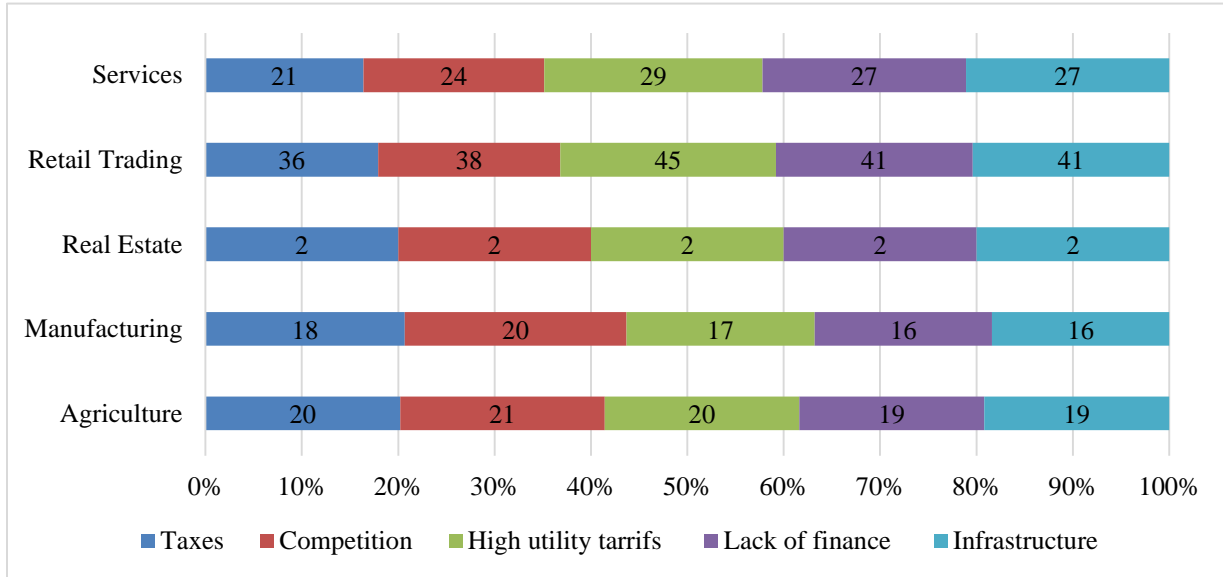
Constraints	Business activity (ISIC)					
	Agriculture	Manufacturing	Real Estate	Retail Trading	Services	Total
Taxes	20	18	2	36	21	97
Competition	21	20	2	38	24	105
High utility tariffs	20	17	2	45	29	113
Lack of finance	19	16	2	41	27	105
Infrastructure	19	16	2	41	27	105
Total	21	20	2	49	29	121

#### 4.3.1 Understanding the Generic or Sector Specific Factors

Another objective of the study was to explore whether factors constraining SMEs in contributing to economic growth are similar across different sectors of the economy. When considered in terms of how each industry contributes to the total, these translate into 50.0 percent, 28.0 percent, and 22.0 percent for lack of finance, competition and infrastructure and taxes respectively (Figure 4.4). Whilst frequency distribution is somewhat evenly spread across the different constraining factors, there appears an emphasis on access to finance as the constraining factor, but this again cuts across other sub-sectors. Similarly, all SMEs engaged in farming cited competition and infrastructure alongside access to finance as constraining factors ( $n=52$ ) but the frequency significantly drops on taxes which translate in real value contribution to the whole of only 16 percent. Key informant interviews eluded this to deliberate policy provisions in

agriculture a priority sector for the government different from other sectors.

**Figure 4.4: Relationship between sectorial focus for SMEs and constraining factors**



### 4.3.2 Policy and Institutional Environment

Further, the study aimed at assessing the existing policy and institutional environment that enable the flourishing of the SMEs.

In terms of policy and institutional effects, the centrality of policy and institutional factors in determining business outcomes cannot be overemphasized. Interestingly, there was a general positive awareness among SMEs of government policies that affect their growth, business outcomes and contribution to economic development. Policies related to the minimum wage, SME development, trade, competition and infrastructure development policy as outlined in Table 4.4.



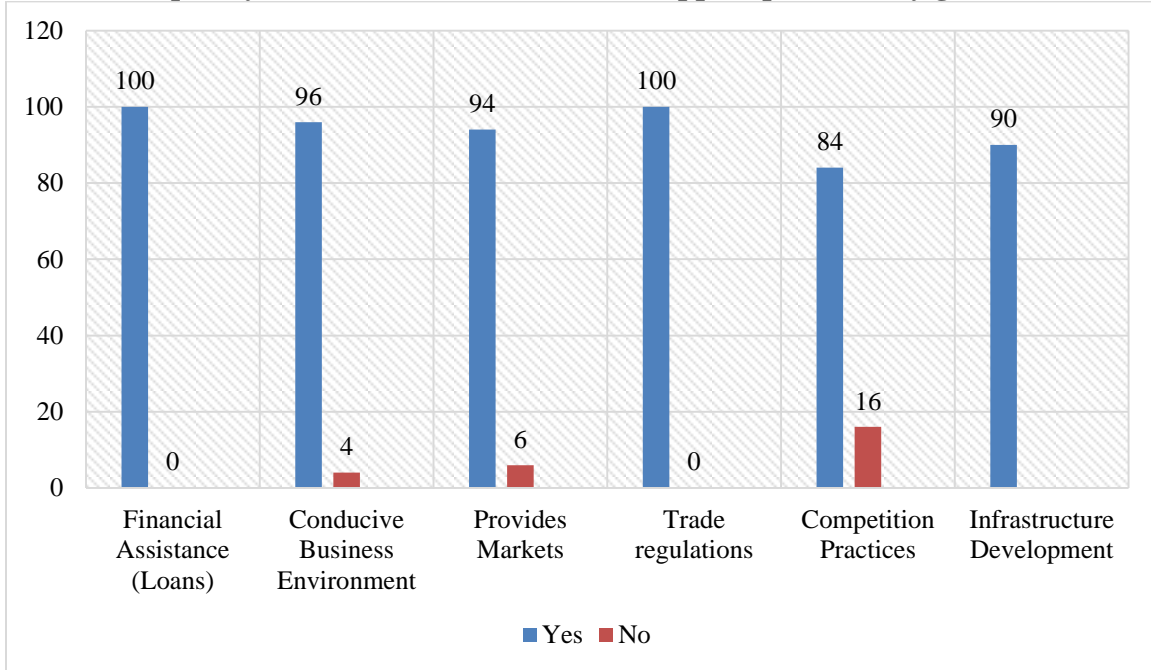
**Table 4.4: Policy Awareness among SMEs**

Policy provision	Awareness response	Frequency	Percentage
Minimum wage	Yes	250	100
	No	0	
The Micro, Small and Medium Enterprise Development Policy	Yes	220	88
	No	30	12
Trade Policy	Yes	190	76
	No	60	24
Competition Policy	Yes	210	84
	No	40	16
Infrastructure Development Policy	Yes	215	86
	No	35	14

Despite wide spread awareness of the policy and institutional processes that affect growth of SMEs, respondents were divided on the likely impacts on their businesses. Some of the SMEs highlighted difficulties in following the national policy requirements whilst other felt that the policies are less relevant in driving SME growth and their optimal contribution to the economy. However, there was also a general awareness and agreement that the government was very important to SMEs through the distribution of the services and general support (e.g. markets, infrastructure). For instance, figure 4.5 shows that 100 percent of the respondents said that government provides financial assistance (loans) and trade regulations compared to 96.0 percent of the SMEs that indicated conducive business environment. About 94.0 percent indicated that government provides markets, compared to 84.0 percent that indicated that government provides competition practices. Meanwhile about 90.0 percent of the SMEs stated infrastructure development provided by government (Figure 4.5).

Despite of all these provisions, SMEs growth has been stagnant or diminishing in the recent past. This may be attributed to lack of political will in promoting sustainable SME development and the poor performance of the macroeconomic indicators such as the; exchange rate, interest rates, GDP growth, among others.

**Figure 4.5: Frequency distribution of services and support provided by government**

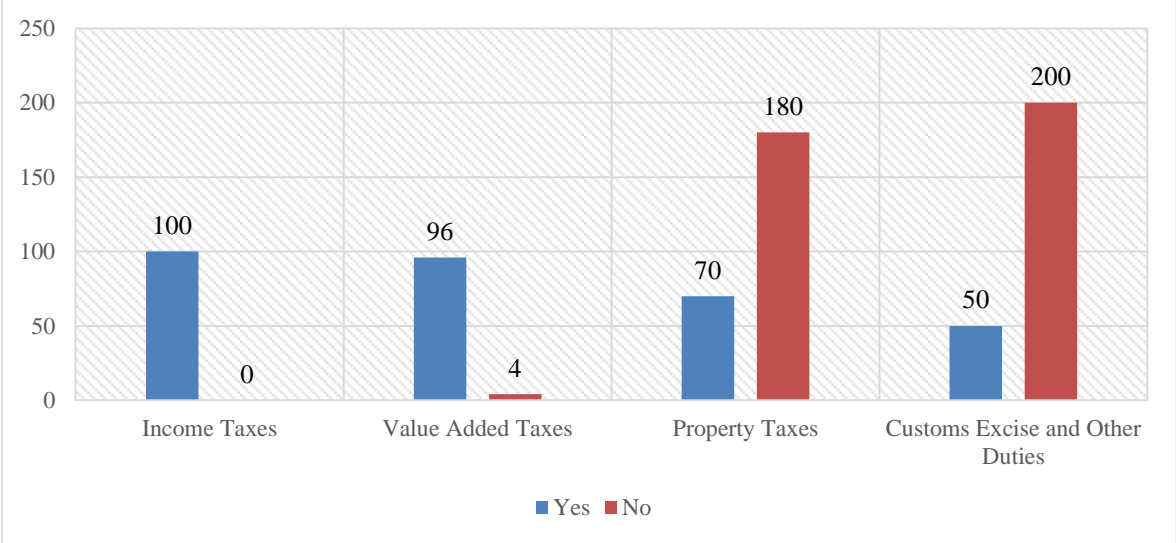


SMEs were further asked to state the government support and services that were one-off. Further probing revealed that public support services by the government are recurrent (96.0 percent) as opposed to once off (4.0 percent). This highlights the extent to which SMEs drive and shape institutional innovation. One cited one-off government service was financial assistance, which again was reportedly not accessible by many SMEs (74.0 percent of the respondents). Interestingly, 90.0 percent of the respondent SMEs revealed that their businesses were registered for tax compared to only 10.0 percent of the businesses not registered. In breaking the SMEs along tax lines, 96.0 percent of the respondents revealed they were registered for Value-Added Tax (VAT), compared to 28.0 percent registered for Property Taxes and 20.0 percent for customs excise and other duties at importation of goods and excise tax at production (Figure 4.6).

Despite SMEs receiving the stated support towards their operation, contrary, SMEs have had an insignificant influence towards economic growth in terms of job creation which should inevitably result or lead to poverty reduction, through an increase in turnover be used to recapitalize and increase production and increase government revenue.

However, SMEs complained about fluctuating policy introduction by the government. For instance, 90.0 percent of the respondents said that the recent tax changes such as those related to abolishment of VAT affected the production of goods and service and profitability, contrasting 10.0 percent of the respondents that indicated otherwise.

**Figure 4.6: SMEs and type of taxes**



**4.4 Generic and Sector Specific Factors**

The findings show that SMEs’ optimal contribution to economic growth and development corresponds to specific sectors within which SMEs operate or exist as generic. This sectorial approach analyzing SMEs stated in this dissertation is crucial in identifying and determining relevant policy interventions for SMEs in order to enhance their optimal contribution to economic growth.

Generally, analysis of questionnaire data show no significant convergence between SME sectorial focus and business line, with identified constraining factors to their optimal contribution to growth as outlined in Figure 4.5. This shows that the constricting factors to SME growth are generic as opposed to sector specific, an element which has significant implications on policy interventions. For instance, of 90 SMEs identifying themselves with relate trading, 100 percent ( $n=90$ ) reported access to finance compared to 56 percent ( $n=50$ ) and 44 percent ( $n=40$ ) for competition and infrastructure and taxes respectively.

**4.5 Association between the Internal/External Constraint Factors and Economic Growth**

Another objective of the study was to determine the association between the internal/external constraint factors and economic growth. The contribution to economic growth was determined by an enterprise’s increase in number of employees, turn over and production output. The internal and external constraining factors include; incentives/financial support, type of enterprise, ownership, business training and years of operation. The chi square measure of dependence was used to determine the dependence between the independent and dependent variables.

**4.5.1 Any form of Support and Contribution to Economic Development**

The findings show that there is a significant relationship between the enterprises with business support and their contribution to economic growth as the P value is below 0.05 (0.00) and the chi square value is 162.7. As established in the literature, enterprises that receive support (financial and other incentives) are more likely to contribute to economic growth. This can be the case as the support may trigger high capital acquisition and production which may lead to enterprise growth and contribute to economic growth.

**Table 4.5: Any form of Support and Contribution to Economic Development**

Any support for your business	Contribution to Economic Growth		
	Yes	No	Total
Yes	97	8	105
	92%	8%	100%
No	16	129	145
	11%	89%	100%
Total	113	137	250
	45%	55%	100%

Chi square Value = 162.7                      df =1                      P-value=0.00

**4.5.2 Trained in Business Operation and Contribution to Economic Development**

The findings show that there is a significant relationship between the respondents training in business operation and their contribution to economic growth as the P value is below 0.05 (0.00) and the chi square value is 162.7. Similarly, enterprises that are managed by persons that have been trained in business operations are more likely to contribute to economic growth. This can be the case as correct decisions are made in running the enterprises and may trigger high capital acquisition and production which may lead to enterprise growth and contribute to economic growth.

**Table 4.6: Trained in Business Operation and Contribution to Economic Development**

Trained on how to operate the business	Contribution to Economic Growth		
	Yes	No	Total
Yes	97	8	105
	92%	8%	100%
No	16	129	145
	11%	89%	100%
Total	113	137	250
	45%	55%	100%

Chi square Value = 162.7

df=1

P-value=0.00

**4.5.3 Enterprise Ownership and Contribution to Economic Development**

The findings show that there no significant relationship between the enterprises ownership type and their contribution to economic growth as the P value is above 0.05 (0.581) and the chi square value is 1.956. The type of enterprise ownership has no bearing on their contribution to economic growth hence the need to support SMEs growth should cut across all SMEs.

**Table 4.7: Enterprise Ownership and Contribution to Economic Development**

Enterprise ownership	Contribution to Economic Growth		
	Yes	No	Total
Private Limited Company	52	68	120
	43%	57%	100%
Sole Proprietor	22	28	50
	44%	56%	100%
Family Owned	4	8	12
	33%	67%	100%
Partnership	35	33	68
	51%	49%	100%
Total	113	137	250
	45%	55%	100%

Chi square Value 1.956

df=3

P-value=0.581

**4.5.4 Type of establishment and Contribution to Economic Development**

The findings show that there is no significant relationship between the type of establishment and their contribution to economic growth as the P value is above 0.05 (0.782) and the chi square value is 0.077. The type of enterprise/size has no bearing on the contribution to economic growth. The contribution to economic growth might be uniform across SMEs.

**Table 4.8: Type of establishment and Contribution to Economic Development**

Type of Establishment	Contribution to Economic Growth		
	Yes	No	Total
Small	109	133	242
	45%	55%	100%
Medium	4	4	8
	50%	50%	100%
Total	113	137	250
	45%	55%	100%

Chi square Value 0.077      df=1      P-value=0.782

#### 4.5.5 Number of years Operating and Contribution to Economic Development

The findings show that there is no significant relationship between the year of business operational support and their contribution to economic growth as the P value is above 0.05 (0.574) and the chi square value is 2.906. Similarly, the number of years in operations has no direct influence on the SMEs contribution to economic growth. It isn't a factor; hence SMEs should be holistically supported for their contribution to economic growth.

**Table 4.9: Number of years Operating and Contribution to Economic Development**

Number of years operating	Contribution to Economic Growth		
	Yes	No	Total
1	22	22	44
	50%	50%	100%
2	18	33	51
	35%	65%	100%
3	21	25	46
	46%	54%	100%
4	27	32	59
	46%	54%	100%
5	25	25	50
	50%	50%	100%
Total	113	137	250
	45%	55%	100%

Chi square Value 2.906      df=4      P-value=0.574

#### 4.6 Constraining Factors responses from Key Informants

The responses from the selected stakeholders that promote SMEs stated both internal and external factors that constrain SMEs in effectively contributing to economic growth. Unfair competition from the non-official sector; SMEs suffer more than large firms from many policy and institutional constraints arising from imperfect markets, and as a consequence, they benefit

disproportionately from reforms. Unfair competition arising from the low cost of doing business in the informal sector is a serious challenge for a significant section of SMEs, especially small sellers and producers. Selected stakeholders stated that majority SMEs lack access to land to sustain their productivity.

SMEs face severe complications in developing administrative and operational procedures to deal with the requirements of government regulations, such as costly and timely procedures to obtain licenses and permits, register property and move collateral.

Others stated that SMEs significantly stand out in the degree to which they identify corruption as a heavy challenge compared to large firms. High tax rates reduce firms' internal sources of financing. Majority stakeholders stated that SMEs are facing more challenges in accessing financial resources. The workers engaged in SMEs suffer from poor training and a low level of skills. The entrepreneur's characteristics such as age, gender, motivation, experience, educational background, risk-taking propensity, preference for innovation, mind-set, and personality. All of which can have a big influence on the firm's performance, success, and the growth of the SMEs can be hugely dependent on him/her.

SMEs in Zambia lack the managerial skills and connections to effectively conduct their business and to deal with the cumbersome legal and regulatory framework. Another important factor contributing to success or failure of SMEs is marketing skills. There is extensive evidence to prove that marketing plays a significant role in the success of SMEs. Marketing is also one of the biggest challenges SMEs face in their business operations. Among the major challenges facing the development of SMEs is the huge lack of technological capabilities, which is the key to developing the competency of SMEs owners and managers.

## CHAPTER 5: DISCUSSION

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### **5.1 Introduction**

The discussion chapter brings together different dimensions surrounding SMEs in Zambia as drawn from the three research objectives and expanded on the results and analysis in chapter 4. It draws on the results and analysis chapter to reflect on the theoretical and empirical implications of the study.

### **5.2 SMEs, Constraining Factors and Possibilities of Optimal Contribution to Economic Growth**

It is clear that possibilities of SME optimal contribution to growth and economic development in Zambia seem to have been stifled by the way policy and institutional processes have been implemented. The evidence is that policies remain generic rather than specific, making it difficult for SMEs to directly benefit from state provisions. For instance, Zambia policy developments have been characterized by incoherent and in some point fluctuating (Manda et al., 2017; Kalaba et al., 2013). Consequently, the SME sector has not been spared, this cuts across all the industries and sectors. This is the case as SMEs are treated the same in terms of incentive provisions. Although there is a general awareness of policies related to small and medium scale businesses, it remains unclear how business players access services such as those related to access to finance. Central to this are crucial inadequacies and mismatches between policy and reality. This reflects wider challenges facing SMEs across the region as highlighted by Quartey et al., (2017) in a study on ECOWAS. Unpacking national policy and institutional dynamics as they relate to SMEs provides policy lessons for economic growth and development and how interventions can be shaped. Institutional collaboration in supporting SMEs should be strengthened and legal frameworks enforced and ensure compliance to ensure that all stakeholders involved perform to the best of their capabilities. This study can help clarify spheres that can be exploited in order to tailor support for SMEs more broadly and across sectors.

More widely, there is a shift towards high growth trends across Sub-Saharan Africa. SMEs get to play a crucial role, supporting service demand and needs for specialization (Fjose et al., 2010). Recently, Zambia was characterized as a middle-income country experiencing robust economic



growth during the commodity boom averaging 7.4 percent (2004-2014) (World Bank, 2016). This is reflective of expanding productive capacity and most importantly the middle class. Growth and expansion of the middle drives demand for commodities which can mean expanding opportunities for SMEs as highlighted in Section 4.2 and 4.3. Liberalization of the markets in Zambia means SMEs must contend with external players and competition. However, inward migration from countries such as China taking advantage of the conducive business environment have tended to entrench new competition lines – product and technology – for SMEs. This was clear in the findings which showed decreasing or static business trends – external competition (Section 4.2). Challenges facing SMEs are diverse but cross-cutting. Three key constraints were observed across all industries in this research: taxes, lack of access to finance, competition and lack of supportive infrastructure. Recent studies such as Quartey et al., (2017) have isolated these elements with respect to ECOWAS (see also Abor and Quartey, 2010).

The lack of access to adequate finance has been at the center of policy developments across the sub-Saharan Africa. Access to finance enables SMEs to compete effectively in the now dynamic globalized market environment (e.g. developing effective production technologies), but financial exclusion on the region and countries such as Zambia means SMEs face daunting challenges of organizing capital (Quartey et al., 2017). This in part stems from inability to provide collateral that can allow SMEs to access formal sources of capital such as banks, which again faces enormous interest rates. Findings in this study reinforce previous studies such as those by Collier (2009) who points out perceptions that providing access to finance for SMEs was riskier than their counterparts' large firms. This means SMEs are unable to grow into vibrant firms that can create massive employment absorption across diverse sectors, which affects their contribution to economic development at least in the case of Zambia.

Compounding this was a second element of increased competition alongside challenges of infrastructure. Business environment are crucial in determining outcomes and contribution to the economy across various indicators. Past studies show that infrastructures for finance and more generally are crucial for more efficient growth and production (Fjoe et al., 2010). In this dissertation, infrastructure challenges include infrastructure such as water and electricity. Interviews showed how electricity and water links to wider dynamics in rainfall patterns across the sub-Saharan Africa. In its country assessment in 2016, the IMF argued that: “The Zambian

economy is under intense pressure such as electricity shortages, and poor rainfall have dampened the pace of economic activity, expenditure is running far above budget, in large part as a result of fuel subsidies and contracted emergency electricity imports that together are estimated to cost the treasury about US\$660 million a year at the current pace (equivalent to 3.2 percent of GDP) (IMF 2016). This highlights the environment within SMEs were operating limits their potential, and only now has electrification and rural infrastructure development emerged as real policy issue in Zambia (Haanyika, 2008). Slow economic performance means this policy direction cannot guarantee successful outcomes.

Taxation is also a major issue across developing countries such as those in sub-Saharan Africa which affect the ease with which to conduct business especially as they relate to cross-border trading and paying taxes. In Zambia, personal income rate increased from 35 percent in 2016 to 38 percent in 2018. The tax system comprises income taxes, consumption taxes and trade taxes. Income taxes relate to company income tax, Pay As You Earn (PAYE), including withholding tax. Consumption taxes point to import and domestic value-added tax, excise duties whilst trade taxes include customs duty and export duty. SMEs must negotiate these tax obligations which are often difficult to follow.

These constraining factors to SMEs can be considered generic as opposed to corresponding to specific sectors. This means that any policy recommendations should take a general approach as opposed to sectorial perspective.

Further, the findings show that there are no significant relationships between internal/external constraining factors and enterprises contribution to economic growth.

Overall, this dissertation has considered three core challenges facing SMEs: the question of high taxes, lack of access to finance, and challenges of competition alongside lack of support infrastructure. These have been identified as limiting the potential of SMEs to significantly contribute to economic growth and development. It has shown that these are generic rather than specific. It emphasises the need for policy intervention that can ensure access to finance, provision of infrastructure and leveling the playground for competition.

## CHAPTER 6: CONCLUSION

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This study considered factors constraining SMEs from optimally contributing to economic growth in the case of Zambia. The study highlighted a negative correlation between GDP and SME output. Results showed that a reduction in gross domestic product in the recent past has had adverse effects given the increase in the number of SMEs. Three key questions underpinned this study; 1) what are the policy and institutional related factors that shape the dynamics of the SME economy and influence outcomes in Zambia? 2) What factors constrain SME's optimal contribution to economic growth and development in Zambia? 3) Do these factors restrict SME contribution to growth and economic development?

This study drew conclusions from 250 businesses from various sectors. Increasing trends in performance were reported from 120 SMEs irrespective of GDP trends. In comparison, performance of 80 SMEs said that they had not recorded static business performance trends. Considering that there have been indications of reduction in GDP Zambia in recent years despite the supposed increase in the number of SMEs, it can be concluded that the sector was not optimally contributing to the GDP in Zambia. In summary, findings show that the major factors according to the survey were the failure to access finance as attested by 160 of the 250 respondents who put this as the biggest impediment in success of their business. The next 65 of the respondents gave high taxes as the factor affecting them the most. The rest of the respondents gave competition and the absence of appropriate infrastructure to support business growth. This can be compared with the responses gotten from the policy makers and the implementers. Key informants (KI) pointed to limited accesses to finance, the deficit of infrastructure seen as inhibiting smooth and accelerated growth and development of businesses. KI also cited limited access to markets caused by poor product development and limited access to technology. This includes the lack of finance, the lack of capacity, skills and difficulties to access and penetrate markets due to product quality, reflective of wider regional dynamics facing SMEs in sub-Saharan Africa (OECD 2009).

Lack of training, adequate skills and the bureaucracy in the disbursing of funds was also cited as the major factor constraining SMEs from contributing to economic growth. It can be argued that the factors constraining SMEs from contributing to economic growth are clustered in three main

groups. The first factor being identified as the limited access to finance. Most SMEs were seen as having problems in accessing government finance to help them expand their businesses. In the same line those who are able to access finance also have to wait for too long due to the bureaucratic processes in disbursing funds. The second factor is the lack of infrastructure, which includes poor state of roads and in some cases even the availability of roads leading to markets, electricity outages which can be attributed to the drought experienced by most sub-Saharan countries in the recent past. Most countries in sub-Saharan found themselves in a position where they had to import power at very high rates (IMF, 2016). This eventually meant they had to ration power through load shedding, which adversely affected most small business which had to operate only when the electricity is available consequently leading to loss of business revenue. Lack of alternative energy sources for SMEs strengthens this point. The last main group is the lack of skills and training by most of the entrepreneurs. This has led to the inability to access the latest technologies on the market which in turn led to poor product quality. The poor product quality has led to difficulties by most SMEs to penetrate in some overseas markets. In the local market, these SMEs have been made to compete with inward technologies from China, criticized by many businesses as displacing local entrepreneurs. However, variations in SMEs across firm sizes, technology levels, degrees of formality and degree of market integration also means experiences cannot be generalized (Fjoe et al., 2010).

More widely, findings in this study demonstrate that the factors constraining the growth of SMEs that seem to cut across all the sectors are generic and are not unique to particular sectors. This means that any possible interventions that can be applied to enhance growth and role of SMEs to the local economy must be applied in a cross-cutting fashion. Diverse state and non-state actors must be drawn in a collaborative manner to design and implement SME specific interventions in order to generate and ensure greater outcomes and contributions to economic growth and development.

And lastly but not the least, the existence of the policy and institutional environment is not effective or efficient to facilitate for the SMEs efficient contribution to the economic growth.

## CHAPTER 7: RECOMMENDATIONS AND FUTURE RESEARCH DIRECTION

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### 7.1 Recommendations

There are quite a number of interventions which have been put in place by the Zambian Government together with donor institutions to ensure maximization of SME potential. However, these interventions have not been able to address the SME nuances and specific challenges faced by them. Some of these include the Credit Guarantee Schemes which are being administered by Development Bank of Zambia (DBZ) to help SMEs to access loans and to boost their business. The other is the establishment of the asset register at PACRA to encourage SMEs with movable assets to be able to use as collateral to access loans instead of using the traditional collateral of infrastructure. The other good interventions are for the enacting into law of the requirement for 20 percent of all major contracts to be given to Zambians to encourage SMEs in the construction sector to take part in the big construction jobs. However, there remain gaps. Study makes three key recommendations that can suit SMEs globally and those in Zambia:

1. To improve the access to finance by SMEs, the Government must provide incentives to lending institutions in order to encourage them to offer credit to SMEs. This includes operationalizing the secondary market for SMEs to provide alternative sources of finance such as through the Lusaka Stock Exchange;
2. They need to prioritize business management and skills management. Currently, Zambia has only one center of Excellence in Kabwe. The establishment more of such centers could help in product development which will in turn make the products more competitive on the domestic, regional and international market. The idea of *Business Incubators* can help refine development of business ideas and accelerate SMEs to steer growth of commercialization and growth. Establishment of both business incubators and accelerators would be of great benefit to most SMEs through building competitiveness;
3. To improve effectiveness, there is need for managers, proprietors, and operators of the SMEs to be drawn into policy formulation processes. These can identify policy gaps as well as help improve implementation;
4. There is need to provide other capital incentives such as land or infrastructure to SMEs. The infrastructure can include provision of solar powered equipment in public trading areas to reduce the loss of business caused by power outages;

5. Proper enforcement and monitoring of Government policies such enforcement of the 20 percent allocation to SMEs in all public procurement activities particularly in the construction sector to ensure adherence, this will provide opportunities for SMEs in the construction sector; and
6. Government legislation on the entry requirements of some of the businesses to ensure protection of local businesses and encourage their growth.
7. Tax exemptions and incentives to SMEs to encourage their growth.
8. Easy tax filling mechanism to encourage compliance because most small and medium businesses fold up because of huge non tax compliance obligations.

## **7.2 Future Research Direction**

The focus in this dissertation was around factors constraining SMEs from optimally contributing to economic growth in Zambia. Some of the possible mechanisms through which SMEs promote economic growth are through productivity, employment and through upward trends in business growth. However, there is need for further research to investigate if:

1. SMEs are heterogeneous as opposed to homogenous. Rather than take a general perspective as advanced in this dissertation, there is need for research that can segment SMEs across firm sizes, technology levels, degree of informality, degree of market integration and examine constraining factor accordingly.
2. Research is also needed into how male-led SMEs play and the constraining challenges they face compared to their counterparts the female-led SMEs.

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## APPENDICES

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### APPENDIX 1: Questionnaire for Small and Medium Enterprises

THE UNIVERSITY OF CAPE TOWN

SCHOOL OF BUSINESS, ECONOMICS AND MANAGEMENT

**RESEARCH TOPIC: FACTORS CONSTRAINING SMEs FROM OPTIMALLY CONTRIBUTING TO ECONOMIC GROWTH IN SUB-SAHARA AFRICAN COUNTRIES: THE CASE OF ZAMBIA**

Dear respondent,

I am a student at the University of Cape Town in the Development Finance Institute, Graduate School of Business pursuing Master of Commerce in Development Finance. I am undertaking an academic research on the above topic.

You have been randomly selected to assist in this research by filling in this questionnaire. The information that will be gathered is strictly for academic purposes and will be treated with maximum confidentiality.

Therefore, your honest and truthful responses will be highly appreciated.

#### Instructions

- **Do not** indicate your name or identity number on the questionnaire.
- **Provide your response** by filling in the space provided. **Tick** the answer that best expresses your view as shown where applicable [√].

**SECTION A: Background**

1. What is your sex? \_\_\_\_\_
2. How old were you on your last birthday? \_\_\_\_\_
3. Marital Status
  - (a) Married
  - (b) Single
  - (c) Divorced
4. Type of Small and Medium Enterprise \_\_\_\_\_
5. Level of Income (per annum)
  - (a) Below K5, 000
  - (b) Between K10, 000 – K15, 000
  - (c) Above K15, 000
6. What is your level of education?
  - (a) Low/no education
  - (b) Medium (Secondary)
  - (c) High (Tertiary)
7. Number of employees \_\_\_\_\_
8. How is the establishment owned?
  - I. Private Ltd Company
  - II. Sole Proprietorship
  - III. Family owned
  - IV. Partnership
9. Years of operation \_\_\_\_\_
10. Are you trained in any business management?      A. Yes      B. No
11. Do you receive any government support?      A. Yes      B. No
12. Ever had an increased number of employees?      A. Yes      B. No
13. Have had an increase in the annual over ?      A. Yes      B. No

**SECTION B: Activities of SMEs in Zambia**

1. What is your main business activity? \_\_\_\_\_

2. Do you conduct other economic activities?

a. Yes

b. No

3. If yes, list the other economic activities that you conduct?

\_\_\_\_\_  
\_\_\_\_\_

4. Do you (as an SME) affect economic growth in Zambia during fluctuations?

a. Yes

b. No

5. How do you (as an SME) affect economic growth in Zambia during fluctuations?

\_\_\_\_\_  
\_\_\_\_\_

**SECTION C: Factors constraining SMEs contribution to economic growth in Zambia during fluctuations**

6. Do you (as an SME) contribute to economic growth in Zambia?

a. Yes

b. No

7. If yes, how do you contribute to economic growth in Zambia? *If not, please state why.*

\_\_\_\_\_  
\_\_\_\_\_

8. How effective is your contribution (as an SME) to economic growth in Zambia during fluctuations? *Are you actively involved in evaluating factors that enable you to effectively contribute to economic growth? How is this achieved? Have you implemented any new factors in your enterprise?*

\_\_\_\_\_  
\_\_\_\_\_

9. What factors enable you (as an SME) to contribute effectively to economic growth in Zambia during fluctuations?

Yes                      No

- a. Access to financial services
- b. Conducive business environment
- c. Technology
- d. Skilled labour
- e. Conducive environment

10. How do these factors do enable you (as an SME) to contribute effectively to economic growth in Zambia during fluctuations?

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11. What are the major constraints that hinder you (as an SME) from optimally contributing to economic growth in Zambia during fluctuations?

- |                                   | Yes                      | No                       |
|-----------------------------------|--------------------------|--------------------------|
| a. Access to financial services   | <input type="checkbox"/> | <input type="checkbox"/> |
| b. Conducive business environment | <input type="checkbox"/> | <input type="checkbox"/> |
| c. Technology                     | <input type="checkbox"/> | <input type="checkbox"/> |
| d. Skilled labour                 | <input type="checkbox"/> | <input type="checkbox"/> |
| e. Conducive environment          | <input type="checkbox"/> | <input type="checkbox"/> |

12. How do these constraints hinder you (as an SME) from optimally contributing to economic growth in Zambia during fluctuations?

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13. Faced/affected with any of the following in the operation of your business?

- Taxes
- Competition
- Utility tariffs
- Lack of finances
- No infrastructure

**SECTION D: Perspective & Recommendations**

14. What factors enhance your business in terms of growth and survival in Zambia? *Please list the factors*

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15. How do these factors ensure the survival and growth of your business in Zambia? *What types of development opportunities do you see emerging in your enterprise that focuses on contributing to Zambia's economic growth?*

*Are there any programs that motivate you to participate in improving Zambia's economic growth?*

*How are these programs advertised? \*how frequently do you participate in such programs?*

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16. What do you think should be done in order to improve the SMEs sector in order to have sustained economic growth in Zambia during fluctuations?

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**Thank you for Your Co-operation**

## **APPENDIX 2: Persons Interviewed**

INSTITUTION	NAME	POSITION
Zambia Development Agency	Mr Mukuka Mukula	Director Enterprise Development
Zambia Chamber of Small and Medium Business Association (ZCSMBA)	Mr Ngambi	Chief Executive officer
Ministry of Commerce ,Trade and Industry	Mrs Kayula Siame	Permanent Secretary