



Full Length Research Paper

Growth of Small and Medium Enterprises in Addis Ababa Administration In The Case
Of Kolfe Keranyo Sub City

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Abstract

Small and Medium Enterprises (SMEs) are a vital component of the economies in both developed and developing countries. Beyond their economic significance, SMEs are a major focus for policymakers, economists, and various other stakeholders. This study aims to address the gap in understanding the key challenges facing the SME sector. Specifically, the study examines the factors affecting the growth of SMEs in the Kolfe Keranyo sub-city of the Addis Ababa Administration, with a focus on the trade, urban agriculture, manufacturing, service, and construction sectors. Using a combination of quantitative and qualitative approaches, the researchers collected data through a questionnaire distributed via proportional stratified sampling. The analysis, conducted using SPSS software, revealed several major factors hindering the growth of SMEs in the region. These include a lack of access to capital, limited marketing opportunities, poor infrastructure, inadequate human skills, and deficient managerial capabilities. The findings indicate that access to capital, availability of suitable working premises, supportive government policies, access to markets, and infrastructure development are all crucial determinants of SME success and growth. By identifying these critical factors, the study provides valuable insights that can inform policymaking and support initiatives to strengthen the SME sector in the Addis Ababa region. Addressing the barriers faced by small and medium enterprises is essential for unleashing their full potential as engines of economic development and job creation in both developed and developing economies.

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1. Introduction

Small and medium-sized enterprises (SMEs) are non-subsidiary, independent firms which employ less than a given number of employees. This number varies across countries, with the most frequent upper limit designating an SME as 250 employees, as in the European Union (European Commission, 2003). However, some countries set the limit at 200 employees, while the United States considers SMEs to include firms with fewer than 500 employees (OECD, 2005). The labor surplus theory argued that the driving force behind SME development is excess labor supply, which cannot be absorbed in the public sector or large private enterprises and is forced into SMEs in spite of poor pay and low productivity (Ranis & Stewart, 1999). The output demand theory postulates that the development of the SME sector in developing countries is driven by the existence of a market for their products and services (Pack & Westphal, 1986). The firm growth theory contends that as a result of industrialization and economic growth, SMEs are likely to disappear and be replaced by modern large-scale industry (Schumpeter, 1950).

Ethiopia is one of the developing countries in Africa that has prioritized SME development for economic growth, employment generation, and building an industrial economy. In 1997, the government designed a National MSEs Development and Promotion Strategy to facilitate and pave the ground for the growth and development of the sector (Min-

istry of Trade and Industry, 1997). The primary objective of the strategy was to create a favorable environment for MSEs so that they could facilitate economic growth, create long-term jobs, strengthen cooperation, provide a basis for medium and large-scale enterprises, and promote export. The direct policy support for SMEs includes access to markets, finance, industrial extension, training, and technological support.

This research aims to assess the performance and challenges of SMEs in the Kolfe Keranyo sub-city of Addis Ababa, Ethiopia, with respect to job creation, market linkages, savings, and SME growth levels. The research will focus on identifying both internal and external factors affecting the growth of this critical sector for Ethiopia's economic development.

Small and medium-size enterprises (SMEs) play a very important economic and social role, both in the economy and in reduction of unemployment. In Ethiopia, SMEs have a problem of finance when establishing the business as most individual sources of finance come from family & friends, personal savings and loans acquired from relatives, and money lenders with high amount of interests (MoTI, 2005).

The researcher used a decision hierarchy model developed by Ta & Har (2000). In this model, seven parameters are identified to measure the growth of SMEs. Using these variables, various studies have been conducted by different researchers, however

the results show no consistency, which is one rationale behind the present study. Almosawi (2001) pointed out that although studies done in developed countries have contributed significantly to the literature on SMEs, their findings may not have universal applicability, due to differences in cultural, economic, and legal environments.

In the context of Ethiopia, various studies have investigated SMEs, such as Fetene (2010) and Dereje (2012), but they have focused only on access to finance. Therefore, the researcher believes that the current study fills an important gap by considering other determinants of small and medium enterprises. However, the previous studies used simple descriptive analysis and did not include the most important variables, nor did they employ statistical tests or focus on a specific sub-city rather than Addis Ababa as a whole.

The research aims to address the time gap, as no recent research has been conducted in the Kolfe Keranyo sub-city. This is one of the basic central points of the study. The researcher also has experience that some SMEs have been dissolved due to their inability to resist internal and external factors, while others are struggling to survive with no change over time. Therefore, this study tries to identify to what extent internal and external factors affect the growth of SMEs in Kolfe Keranyo sub-city.

2. Theoretical foundation of the study

The study is guided by several key theories and

models related to the growth and performance of small and medium enterprises (SMEs). The resource-based view (RBV) theory suggests that a firm's internal resources and capabilities are the primary drivers of its performance and growth (Barney, 1991; Wernerfelt, 1984). According to the RBV, SMEs can achieve sustainable competitive advantage by developing valuable, rare, inimitable, and non-substitutable (VRIN) resources and capabilities, such as entrepreneurial orientation, managerial skills, access to finance, and technological capabilities.

Institutional theory, on the other hand, focuses on the role of external environmental factors in shaping organizational structures and practices (DiMaggio & Powell, 1983; Scott, 2013). This theory highlights the influence of government policies, regulations, infrastructure, and the overall business environment on the growth and performance of SMEs. Firms must conform to institutional norms, rules, and expectations to gain legitimacy and access to necessary resources for survival and growth.

Furthermore, the firm growth theory contends that as a result of industrialization and economic growth, small and medium enterprises are likely to disappear and be replaced by modern large-scale industry (Schumpeter, 1950). This theory suggests that SMEs may face challenges in sustaining their growth and may eventually be outcompeted by larger firms as the economy develops.

Based on these theoretical perspectives, the conceptual framework for this study will include both internal factors (entrepreneurial orientation, managerial skills, access to finance, technological capabilities) and external factors (government policies, regulations, infrastructure, access to markets, competition) as independent variables, and SME growth and performance (e.g., job creation, sales, profitability, survival) as the dependent variable. The study will examine how these factors affect the growth and performance of SMEs in the Kolfe Keranyo sub-city of Addis Ababa, Ethiopia.

3. Methodology

This study employed a mixed-methods approach, combining both quantitative and qualitative research methods to investigate the factors affecting the growth and performance of small and medium enterprises (SMEs) in the Kolfe Keranyo sub-city of Addis Ababa, Ethiopia.

The quantitative component of the study involved a cross-sectional survey of SMEs in the Kolfe Keranyo sub-city. A structured questionnaire was designed to collect data on the independent variables (internal and external factors) and the dependent variable (SME growth and performance), including both closed-ended and open-ended questions. A random sampling technique was used to select the SMEs to be included in the survey, with a sample size of 200 SMEs, determined using the Cochran formula and considering the total population of SMEs in the sub-city, the desired level of precision, and the expected response rate.

The quantitative data collected through the survey was analyzed using various statistical techniques, including descriptive statistics, correlation analysis, and multiple regression analysis. The correlation and regression analysis were used to examine the effect of the determinants (independent variables) on the growth and performance (dependent variable) of the SMEs, while controlling for other factors.

The qualitative component of the study involved in-depth interviews with a selected number of SME owners, managers, and relevant stakeholders, such as government officials and industry experts. A purposive sampling technique was used to select the interview participants, ensuring a diverse representation of SMEs in terms of industry, size, and stage of growth. The qualitative data collected through the interviews was analyzed using thematic analysis, where the researchers identified and analyzed the emerging themes, patterns, and relationships related to the factors affecting SME growth and performance.

The findings from the quantitative and qualitative components of the study were integrated to provide a comprehensive understanding of the factors affecting SME growth and performance in the Kolfe Keranyo sub-city. The quantitative results, including the correlation and regression analysis, were used to identify the relative importance and the effect of different factors on SME growth and performance, while the qualitative findings helped to explain the underlying mechanisms and contextual nuances. The integration of the quantitative and

qualitative findings was used to develop a robust and contextually-relevant set of recommendations for policymakers, SME support organizations, and SME owners to foster the growth and development of SMEs in the Kolfe Keranyo sub-city and beyond. A total of 200 MSEs were surveyed and data were collected using questionnaires.

4. Results and Discussion

4.1 Pearson correlation coefficients

Correlation analysis provides valuable insights into the factors affecting the growth of micro and small enterprises (MSEs) in the Kolfe Keranyo sub-city of Addis Ababa, Ethiopia. The results indicate that entrepreneur characteristics have a strong positive correlation ($r = 0.541, p < 0.01$) with MSE growth, suggesting that the personal qualities, skills, and experience of the entrepreneur are crucial determinants of enterprise performance and expansion.

Similarly, the management and marketing capabilities of the enterprise also exhibit a strong positive correlation ($r = 0.568, p < 0.01$) with MSE growth, highlighting the importance of managerial and marketing skills for the success and growth of these businesses. The technological capacities of the MSEs further demonstrate a strong positive correlation ($r = 0.571, p < 0.01$) with their growth, underscoring the vital role of technological adoption and

utilization in driving enterprise expansion.

Turning to the external factors, the legal and regulatory framework shows a moderate positive correlation ($r = 0.374, p < 0.01$) with MSE growth, indicating that government policies, regulations, and support mechanisms do play a role, albeit a relatively less prominent one compared to the internal factors. Access to external financing, on the other hand, has a strong positive correlation ($r = 0.588, p < 0.01$) with MSE growth, suggesting that the availability and accessibility of financial resources are critical for the growth and expansion of these enterprises. Lastly, access to adequate markets also displays a moderate positive correlation ($r = 0.459, p < 0.01$) with MSE growth, emphasizing the significance of the MSEs' ability to access and serve their target markets.

Moreover, the correlation analysis highlights the multifaceted nature of the factors influencing MSE growth, with both internal and external variables playing crucial roles. This underscores the need for a comprehensive and targeted approach to supporting and fostering the growth and development of micro and small enterprises in the Kolfe Keranyo sub-city and beyond.

Table 1: Pearson correlation coefficient

Variables spear man's rank correlations	Independent variables	Dependent variable
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		1	2	3	4	5	6	Growth of MSEs
Entrepreneur characteristics	r	1.00						
	Sig.	0.00						
Management and marketing capabilities	R	0.359**	1.00					
	Sig.	0.00	0.00					
High-tech proficiencies	R		0.462**	1.00				
	Sig.	0.821**	0.00	0.00				
Government Regulation issues	R	0.492**	.209*	.493*	1.00			
	Sig.	0.00	0.01	0.03	0.00			
Availability of subsidy firms that offer finance	R	0.474**	0.349**	0.455**	0.536**	1.00		
	Sig.	0.00	0.00	0.00	0.00	0.00		
Access to adequate market	R	.375**	.242**	.352**	.493**	.592**	1.00	
	Sig.	0.00	0.00	0.00	0.00	0.00	0.00	
Growth of MSEs	R	.541**	.568**	.571**	.374**	.588**	.459**	1.00
	Sig.	0.00	0.00	0.00	0.00	0.00	0.00	0.00

** . Correlation is significant at the 0.01 level (2-tailed).

Source: Survey result, 2022

4.2 Regression analysis

Prior to conducting the regression analysis, the researchers performed a series of diagnostic tests to ensure the underlying assumptions were met. This included tests for normality, linearity, heteroscedasticity, and multicollinearity. The results of these preliminary analyses indicated the data was

suitable for proceeding with the regression modeling.

The regression model summary shows that the predictor variables explain 56.1% of the variance in the expansion of micro and small enterprises. The remaining 43.9% is attributed to other factors not included in the study. The ANOVA results

confirm the overall statistical significance of the regression model ($F = 41.291$, $p < 0.001$), indicating the model as a whole significantly predicts

MSE growth.

Table 2: Model Summary ^b

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.749 ^a	.561	.547	.592

Source; own survey, 2022

Table 3: ANOVA ^a

Model		Sum of Squares	d/f	Mean Square	F	Sig.
	Regression	86.685	6	14.447	41.291	.000 ^b
1	Residual	67.879	194	.350		
	Total	154.564	200			

- a. The expansion of micro and small businesses (dependent variable)
- b. Predictor variables: (continuous access to a suitable market/market integration/, management and marketing skills/skills in running a business/, government-related concerns, characteristics of entrepreneurs/invention and innovation trends/, High-tech proficiencies, and access to outside financing).

The regression analysis results presented in the Beta Coefficients table provide a de-tailed understanding of the factors that significantly impact the growth of micro and small enterprises (MSEs).

The capability of invention and innovation exhibits a positive and significant influence, with a standardized beta coefficient of 0.228 ($p < 0.007$).

This indicates that a one-unit increase in the capability of invention and innovation is associated with a 22.8% increase in MSE growth, holding all other variables constant.

Similarly, the skill of supervising habit or trends shows a strong positive relationship, with a standardized beta coefficient of 0.197 ($p < 0.000$). This suggests that a one-unit increase in the skill of supervising habit or trends leads to a 19.7% increase

in MSE growth.

The availability of technology also has a positive and significant impact, with a standardized beta coefficient of 0.209 ($p < 0.015$). This implies that a one-unit increase in the availability of technology is associated with a 20.9% increase in the growth of MSEs.

Interestingly, government-related issues exhibit a negative and significant relationship, with a standardized beta coefficient of -0.048 ($p < 0.041$). This suggests that a one-unit increase in government-related issues is associated with a 4.8% decrease in MSE growth.

Access to financial support has a positive and significant influence, with a standardized beta coefficient of 0.232 ($p < 0.000$). This indicates that a

one-unit increase in access to financial support leads to a 23.2% increase in the growth of MSEs.

Lastly, the capability of management and marketing skills also shows a positive and significant impact, with a standardized beta coefficient of 0.190 ($p < 0.002$). This means that a one-unit increase in the capability of management and marketing skills is associated with a 19% increase in MSE growth.

Moreover, the regression analysis highlights the multifaceted nature of the factors influencing the growth of micro and small enterprises, underscoring the importance of addressing both internal (e.g., innovation, management skills) and external (e.g., access to finance, technology) factors to foster the expansion and development of these enterprises.

Table 4: Beta Coefficients ^a

Model	Unstandardized Coefficients		Standardized Coefficients	<i>t-value</i>	<i>P-value</i>
	B	Std. Error	Beta		
(Constant)	.301	.241		1.247	.214
Invention and innovation	.212	.078	.228	2.709	.007
Enterprenurial skills	.274	.047	.197	3.665	.000
Availability of technology	.187	.076	.209	2.448	.015
Government Related issues	.037	.045	-.048	-.820	.041
Access to financial support	.237	.063	.232	3.777	.000
<i>Market linkage</i>	.175	.055	.190	3.191	.002

a. Dependent Variable: MSEs Growth

- b. *Predictor variables (constant), invention and innovation, skill of entrepreneurs, availability of technology, Government related issues, Access to financial support, and market linkage*

Source: Survey result, 2022

5. Conclusion and recommendations

The research results indicate that the lack of working space, financial problems, poor infrastructure, lack of market information, and other related factors were the major hindering factors affecting the growth of Small and Medium Enterprises (SMEs) in the Kolfe Keranyo sub-city. Based on this analysis, the researcher has drawn the following conclusions:

Working Space: The analysis shows that the availability of a working space has a positive and significant effect on the growth of SMEs. The lack of own working spaces and high rental costs are major problems facing SMEs, which adversely affect their growth. This suggests a direct relationship between the availability of working space and the growth of SMEs.

The study findings reveal a positive relationship between the growth of SMEs and access to finance or capital. This implies that access to finance has a high influence in determining the growth of SMEs. The main problems faced by enterprises include a shortage of working capital, high-interest rates charged by lending institutions, high collateral requirements from banks and other lending institutions, inadequate financial record-keeping systems,

and complicated loan application procedures.

Marketing also has a positive and significant effect on the growth of SMEs. However, insufficient market access, lack of marketing channels, lack of market research, lack of demand prediction, and inadequate product and service advertising have a high influence on the growth of SMEs. This indicates a positive relationship between marketing factors and the growth of small and medium enterprises.

The study results show that infrastructure, including power interruptions and lack of sufficient and efficient transportation services, has a positive and significant effect that hinders the business growth of enterprises in the Kolfe Keranyo sub-city.

Government policy also has a positive and significant effect on the growth of SMEs. However, negative impacts exist, such as bureaucracy in the processing of registration and licensing, as well as insufficient government support.

In general, both internal (finance, marketing, working space) and external (infrastructure, government policy) factors have a very high effect on the growth of SMEs.

Therefore, based on the findings, the following recommendations are given:

- To address the financial problems, financial institutions, the Federal and Regional Governments, should provide special emphasis and support, including specialized lending and repayment arrangements, to assist the growth of the SME sector.
- To solve marketing-related problems, the government should facilitate connections between SMEs and provide trainings to enterprises.
- The government should give great attention to improving infrastructure, such as power supply and transportation, to support the growth of SMEs.
- The government should simplify registration and licensing procedures and provide sufficient support to the SME sector.

Future Research: The researcher recommends conducting more research on the issues to contribute to the development of SMEs in the country. The study populations in the area have time-tested indigenous knowledge about their way of life and their environment in general. Their skill and knowledge about the best tree species to utilize for charcoal making is part of their indigenous experience.

Conflicts of Interest

The authors declare that they have no conflicts of interest.

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