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# **Entrepreneurship in the Developing World: Implications for Business Development in Tanzania**

**WP # 04/2019**

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**Series Editor 2019: Luca Righetti, Research Director (UK), CDI  
Publisher: Cambridge Development Initiative, Cambridge, UK**

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# **Entrepreneurship in the Developing World: Implications for Business Development in Tanzania**

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## **I. Introduction**

Entrepreneurship is an inherent part of growth and development strategies in emerging economies across the globe. National governments, often with the aid of international organizations such as the World Bank and United Nations Industrial Development Organization (UNIDO), have been formulating policies conducive to entrepreneurship and private sector development (Ács & Virgill, 2009). Entrepreneurs have been perceived as social agents for structural changes that lead to industrial and economic growth (Brinkman, 1995). In developing countries entrepreneurship can serve as an alternative response to market imperfections by engaging in the informal sector, thereby filling in critical gaps left by underdeveloped markets (Leff, 1979). For example, large groups developed by entrepreneurs in India play an important role in correcting deficiencies in the information and capital markets (Ghemawat & Khanna, 1998).

The Global Entrepreneurship Monitor (GEM) (2018), the largest and most comprehensive study of entrepreneurship worldwide, shows that developing countries have amongst the highest rates of total entrepreneurship. Specifically, early-stage entrepreneurial activity, defined as the proportion of 18-64-year olds who are in the process of starting a business or have started a business in the past 42 months before the survey, is particularly high in the developing world. Entrepreneurial attitudes appear to match the prevalence of entrepreneurship. Developing countries possess the highest proportion of people who perceive entrepreneurship as a "good career choice" according to the study's survey data. Moreover, they tend to possess a heightened intention to conduct entrepreneurial activities, higher perceived capabilities, and a notably reduced fear of failure.

Although developing economies tend to have higher entrepreneurial activities, entrepreneurs in the developing world find it hard to survive and grow their businesses. This essay explores several reasons for these difficulties and discusses their implications. By examining case studies across the world offers we can gain breadth of insights, however note that CDI must take care in drawing concrete lessons from this as generalised trends may not apply to the specific Tanzanian context.

## **II. Defining Entrepreneurship**

Entrepreneurship in much of the developing world is contextually dissimilar from that in the developed world and its academic definitions, such as the early classical economists view (e.g.

Cantillon, 1734; Turgot, 1766), the Schumpeterian theorisation (1947) and the contemporary perspective of entrepreneurship (Schults, 1975; Baumol & Strom, 2007). For example, Schumpeter (1947) associated the role of the entrepreneur with the process of creative destruction – a disruptive force that sustains economic growth through technological progress. The Schumpeterian conception of an entrepreneur is sustained around an individual (or a group of individuals) who exploits market opportunities through technical or organisational innovation. This hypothesis, which highlighted the importance of entrepreneurship for economic growth through technological advancement, was formalised by Aghion & Howitt (1992), who constructed a framework in which the prospect of future research threatened rents from current research, thereby generating disincentive effects on present entrepreneurship. This has moulded the conventional view of modern-day entrepreneurship in much of the developed world.

By contrast, the conventional view of the literature on developing context is a dichotomy between necessity-driven entrepreneurs and opportunity-driven entrepreneurs. The former encompasses those driven to rudimentary forms of self-employment due to a deficiency in formal employment opportunities caused by labour market rigidities and/or human capital deficiencies. The latter constitutes those whose motivations are similar to those outlined by Schumpeter.

Although necessity-driven entrepreneurs can become opportunity-driven entrepreneurs, the former category appears to have remained sizeable in Africa. The GEM report shows that, despite overwhelmingly positive attitudes towards entrepreneurship as a career choice in Africa, the continent ranks the lowest of all regions in terms of perceived opportunities, with only 37.2% of respondents believing that there were good business opportunities. This suggests that the high prevalence of entrepreneurship in Africa is substantially driven by necessity.

However, this by no means that all entrepreneurship in Africa, let alone the developing world, is necessity driven. Williams and Youssef (2014) conducted a study of informal sector entrepreneurs in urban slums in Brazil by taking samples of entrepreneurs with under five employees and found that the prevalence of opportunity-driven entrepreneurs is noticeably higher than that of necessity-driven entrepreneurs.

### **III. Standard of Living**

Understanding the differences between these two categories of entrepreneurs is critical for any programme attempting to boost the potential of entrepreneurship in emerging economies. Perhaps the most pertinent difference concerns the standards of living.

Block et al. (2015) find that necessity-driven entrepreneurs are more likely to pursue cost minimisation strategies rather than product differentiation. Necessity-driven entrepreneurs in the developing world frequently do not possess any employees or fixed assets and instead reductions in costs may arise from discretionary reductions in their disposable incomes. Hence,

those in necessity-driven self-employment are predicted to have lower average incomes than those in formal employment.

Ellis & Mdoe (2003) reinforce this result with specific relevance to the Tanzanian context. They investigate research conducted in 10 different villages in the rural Morogoro region and differentiate between "non-farm self-employment", which is used as a measurement for opportunity-driven entrepreneurship, and "farm self-employment" which is used to measure necessity-driven entrepreneurship. They suggest that rural poverty is strongly linked to a deficiency in land and livestock and an inability to seek alternatives to diminishing farm opportunities. As such, cost minimisation strategies would constitute reductions in disposable income or the disposal of minimal existing assets. By contrast, the highest quartile of income earners experienced "non-farm self-employed" income encompassing 44% of total income (versus 11% for the lowest quartile). Hence, the authors make two conclusions: firstly, becoming better-off within rural Tanzania involves reducing dependency on agriculture; and secondly, even amongst opportunity-driven entrepreneurs, vast inequalities of income exist.

#### **IV. Institutional and Financial Development**

Another key factor to consider when examining entrepreneurship in the developing world is the institutional context. The GEM report suggests clear linkages between the prospects of entrepreneurs and the level of institutional and financial development. The political and institutional climate in the four sampled African countries (Egypt, Madagascar, Morocco and South Africa) have been identified as hindering rising entrepreneurship. Africa, despite being the region in which perceptions of entrepreneurship are the most positive (74.5% of surveyed respondents believing that entrepreneurs are admired in their societies), is plagued by the highest prevalence of political instability, corruption and the poorest financial infrastructure of all surveyed regions.

Hence, in such developing countries, there is a tendency for most of the entrepreneurial activity to be concentrated in the wholesale and retail sectors; these areas require minimal financial resources and technology and rely least on institutional stability compared to manufacturing, healthcare, education, administrative services or other industries. It has been argued by Beck et al., (2008) that financial development, which is associated with small business prevalence and entrepreneurial ambition, is linked to strong economic growth. Implicitly, deficient financial development and inefficient financial institutions in developing countries may be a hindrance to entrepreneurship, and therefore to business development. The study also identifies lower support for entrepreneurs on average, particularly from the institutional and cultural climate.

McGrath and MacMillan (1992) suggest that there are a basic set of beliefs that entrepreneurs hold about themselves and others in society that is a differentiating factor from the beliefs of non-entrepreneurs. This was computed from a cross-cultural study of 700 entrepreneurs in 9 countries. The researchers advance their original idea by implying that social interventions

aimed at encouraging entrepreneurship need to be tailored to their target populations. The authors' study includes a comparison of values between American, Mainland Chinese and Taiwanese entrepreneurs, and they conduct discriminant analysis to determine whether statistically significant patterns of group membership would emerge from the aggregated responses. They determine that culture is malleable when ideology predominates, and therefore entrepreneurship becomes sensitive to institutional matters more than cultural ones. However, this essay cautions generalising this result to the Tanzanian context due to the small sample size, relatively old data and highly qualitative nature of the conclusion.

## **V. Entrepreneurship education programmes**

The evidence from entrepreneurship education programmes (EEPs) provides some indication of the elasticity of entrepreneurial activity in response to education. In theory, if necessity-driven individuals dominate entrepreneurship, education will have a proportionately smaller impact on entrepreneurial activity. Fayolle and Gailly (2013) measure the impact of a short, compulsory 6-month entrepreneurship education programme on the prevalence of entrepreneurial outcomes. They find that the effects of such programmes are only noticeably positive when prior exposure to entrepreneurship is weak. Conversely, for students who had previously been exposed to business education or EEP education, there are significant counter-effects which in some cases were detrimental to their career prospects. As such, the authors suggest that there is an intrinsic need to target those with very little exposure to entrepreneurship. This result implies that individuals with more educational awareness and knowledge may be more inclined to pursue formal employment, and therefore are less likely to pursue entrepreneurial activity, explaining the deleterious effects of extensive EEP training. On the other hand, individuals with minimal experience and training benefited substantially from EEPs, indicating that they were most beneficial to those who were inclined to pursue entrepreneurship with a degree of opportunism.

An indirect channel through which entrepreneurship education may influence the prevalence of entrepreneurship is perceptions. The GEM survey identified that entrepreneurial attitudes and activity tend to move in tandem with one another. Karimi, et al., (2014) developed an ex-ante and ex-post survey to assess the impacts of both elective and compulsory entrepreneurship education programmes on educational institutions in Iran. The authors find that elective EEP programmes significantly increased entrepreneurial intention; however, the increase was statistically insignificant from compulsory EEPs. This extends upon the study conducted by Fayolle and Gailly (2013) by identifying how the voluntary and compulsory elements differed. The study implies that only opportunity-driven entrepreneurs, who would be more inclined to take up elective entrepreneurship and business education, are likely to benefit from such undertakings. As such, entrepreneurship education can be viewed as most effective when targeted at opportunity-driven entrepreneurs, as opposed to their necessity-driven. In addition, given that compulsory programmes, which are more likely to target necessity-based entrepreneurs who suffer from asymmetries of information regarding the benefits of such

programmes, are shown to have limited impacts, it is possible that such programmes undertaken at places of higher education are limited in their effectiveness, and may worsen inequalities of opportunity.

## **VI. Conclusion**

In conclusion, entrepreneurs in Tanzania likely constitutes a majority of necessity-driven entrepreneurs, but also a non-trivial proportion of opportunity-driven entrepreneurs. Individuals who pursue opportunity-driven entrepreneurial activity tend to be concentrated in the wholesale and retail sectors; those who are necessity-driven tend to be concentrated almost exclusively in small-scale agricultural production. Entrepreneurs tend to be limited by a very poor institutional climate, which curtails their ability to expand beyond sectors which require minimal financial and technological commitment, both in terms of financial constraints and political risk. Generally, perceptions of entrepreneurship tend to move in line with entrepreneurial activity, particularly opportunity-driven entrepreneurship. As such, the prevalence of entrepreneurship is determined by factors which affect perceptions, including social and cultural norms, and the political and institutional climate. The standards of living are very different between opportunity-driven entrepreneurs and necessity-driven entrepreneurs; even within the category of opportunity-driven entrepreneurs, significant inequalities of income and wealth exist. Going forward, the evidence highlights that voluntary entrepreneurship education programmes, which are mainly lacking in Tanzania, may have a strong positive impact on the wealthiest opportunity-driven entrepreneurs who have had minimal exposure to business and entrepreneurial education. However, poorer opportunity-driven and necessity-driven entrepreneurs neither experience nor are aware of the benefits of such programmes. As such, it is probable that such programmes may even worsen income and wealth inequalities in Tanzania unless they are targeted at rural populations reliant on agriculture.

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**Citation:** Chen, M.L. (2019). Entrepreneurship in the Developing World: Implications for Business Development in Tanzania. CDI Working Paper Series WP 04/2019, Cambridge: Cambridge Development Initiative.

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