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Poverty Reduction through Strengthening Small and Medium Enterprises

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Abstract

Although Botswana is clearly one of the richest countries with one of the most vibrant economies in Africa, available statistical evidence suggests that the problem of poverty has recently caused a lot of concern in the country. Numerous attempts already made to deal with the problem have not yielded encouraging results, as the incidence of poverty continues to persist. Drawing from the experiences of three other African countries, this paper recommends a strategy based on strengthening small and medium enterprises (SMEs) for poverty reduction in Botswana. After discussing the constraints facing the SMEs in the country, the paper presents a set of six recommendations designed to ameliorate, if not eliminate, these constraints, thereby strengthening the employment and income generating capacities of the SMEs and consequently reducing poverty in the country.

1. Introduction

Available statistical evidence suggests that there is significant amount of poverty in Botswana. Although several attempts have been made to deal with this problem, one would hesitate to claim that a breakthrough has been made, especially when one can clearly see that the incidence of poverty appears to persist.

Our view in this paper is that, amongst the menu of available poverty reduction strategies, a strategy with far reaching potential is that of strengthening Small and Medium Scale Enterprises (SMEs). By undertaking deliberate, and appropriately planned strengthening of SMEs, one will most certainly end up by achieving the following results: enhancing their productivity; raising their employment generating capacities; and consequently placing higher incomes in the hands of the poor entrepreneurs. A direct way of strengthening these enterprises will require that we focus our attention on two main factors: first, addressing the constraints facing those enterprises and second, taking appropriate technology to the enterprises and making sure that such technologies are adopted by the enterprises. We do not need to over-emphasize the fact that such technologies must be appropriate. The appropriateness of a technology can be viewed from four main characteristics which must be incorporated into the design of the technology: the technology must be entrepreneur capability friendly to the extent that its design must take into account the capability of the entrepreneur; it must be productivity enhancing; it must have a high employment generating capacity; and it must equally have a high income generating capacity. By generating larger volumes of employment as well as higher levels of income, the SMEs will not only have contributed towards poverty reduction, but they will also have enhanced the welfare and standard of living of the many in the society.

This paper is divided into seven parts. The first part is an introduction. The second part attempts to define the terms "poverty" and "small and medium enterprises".

Part three highlights the poverty situation in Botswana, and part four explains the rationale for the choice of strengthening SMEs as a strategy for poverty reduction. Part five presents the numbers and some characteristics of SMEs in Botswana. In some cases, comparisons are made with the situation in Kenya. Part six outlines the various constraints faced by the SMEs, and part seven discusses a set of recommendations designed to strengthen SMEs, raise their employment and income generating capacities and consequently have a positive impact on poverty reduction. Part eight presents concluding remarks.

2. Definitions: Poverty and SMEs

2.1 Poverty The definition of the term “poverty” has become more elusive today than what it was a few years back. The boundary of the definition has broadened significantly and, as a result, it has acquired several dimensions encompassing several factors, which hitherto were not explicitly part of the definition. Moreover, apart from the challenge posed by the breadth of the concept in so far as its definition is concerned, its measurement is equally challenging. In the circumstances, the definition we shall present here will certainly not be an exhaustive one for, in any case, that was not our aim in the first instance. The reason for refraining from any attempt to provide an elaborate or exhaustive definition rests on the fact that our principal aim is simply to highlight some of the dimensions of the concept that are relevant to this paper.

The most common approach to the definition of poverty is an income or consumption centred approach. According to this approach, the poor are identified as those who command levels of income that are insufficient to provide a minimum standard of living (Rahmato, 1987; Warnock, 1988; Dreze and Sen, 1989; World Bank, 1990). The main focus of this approach is the quantitative definition of the standard of poverty. The approach has been used for making broad comparisons between standards of living in different regions of the world. To operationalize this definition, two quantitative measures have been applied: the income poverty line which specifies an income level defining the minimum standard of living; and consumption poverty line, which specifies the level of expenditure that is necessary for the purchase of a minimum standard of nutrition and other basic necessities.

What needs to be noted about these definitions are the difficulties and the cautions that we need to exercise when we choose to make inter-country comparisons based on the definitions. For instance, poverty may need to be looked at as relative to prevailing standards in a society, rather than an absolute definition which is applicable globally. By comparing an industrialized country where the standards of living are higher with an underdeveloped country where the standards of living are relatively much lower, one will immediately appreciate the fact that poverty is recognized at a higher standard of living and income in the former country than in the latter country .

A second approach to the definition of poverty places emphasis on the basic capabilities of people, rather than their command of goods and services. According to the definition, one is regarded to be free from poverty if one has the capabilities of securing enough food, adequate health care and is capable of being an active participant in the society. .

Although these two approaches are by no means mutually exclusive, this paper relies more on the first approach than the second one. It is our position that in an economy like Botswana where, so far, social amenities (health, water, education etc.) are efficiently supplied by the government, giving the poor a command over goods is certainly more appropriate and will go a long way in poverty reduction. This paper

believes that by strengthening the SMEs, higher employment and incomes will be generated among the poor, and the objective of poverty reduction will, to some significant extent, have been achieved.

2.2 Small And Medium Enterprise So far, there has been no standard, clear-cut and globally accepted definition of the phrase “small enterprises” or “medium enterprises” or “small and medium enterprises”. Within the same country, the definition may vary from one institution to the next. In addition, whereas one particular government may define the SMEs in one way, another government elsewhere may define the same enterprise differently. Notwithstanding those seemingly different definitions, a close look at the different groupings of these enterprises does suggest the existence of broad characteristics common to any one grouping that permits us to distinguish one grouping from the next. On the basis of these broad characteristics, it has been possible to coin widely acceptable definitions based on a set of criteria such as the value of paid up capital, the value of operating capital, the employment capacity of the enterprise, the value of production equipment and the volume of sales. For example, in Mauritius, the Mauritian Central Statistical Office (CSO) classifies firms with an employment capacity of 10 persons or more as large firms, while those firms with 9 or fewer employees are referred to as small enterprises (Dabee, 2001). In their study of manufacturing enterprises in 1999 in Mauritius, Wignaraja and O’Neal, cited by Dobee (ibid), presented their own definitions on the basis of which their study was conducted. The two researchers classified firms with fewer than 10 employees as micro enterprises; while those with employment capacity of 10 to 49 were grouped under SMEs and firms with 50 or more employees were placed under the category of large firms.

Unlike the case of Mauritius, in Zimbabwe, the definitions of these enterprises are more elaborate. The government of Zimbabwe applies the following definitions for the different classes of enterprises: micro-enterprises are defined as those enterprises that make use of family as well as hired labour of up to five workers; small scale enterprises are defined as those enterprises which employ between five and twenty hired workers; and medium scale enterprises have an employment capacity of 20 or more, have a capital value of Z\$ 2 million, fixed assets valued below Z\$ 2 and Z\$3 million and an annual turnover of up to Z\$2 and Z\$15 million.

3. Highlights of Poverty in Botswana

In spite of its glamorous and alluring performance in terms of economic growth which has been sustained over considerable length of time, available statistical evidence clearly suggests that Botswana has a significant amount of poverty among its population (Ministry of Finance and Development Planning, MFDP, 1997). Although the overall national poverty headcount rates for the poor and the very poor showed some percentage decline between 1985/86 and 1993/94, the documented rate of 50 per cent registered as of 1993/94 remains too high. Table 1 summarizes the estimated national poverty headcount rates extracted from the 1997 MFDP report on poverty and poverty alleviation in Botswana. In 1985/86 a total of 59 per cent of Botswana were living in poverty, both poor and very poor. A total of 60 percent of females and 58 per cent of males fell under this category of the poor.

**Table 1: Estimated National Poverty Head Count
Rates in Botswana by Poverty Group 1985/86 and 1993/94(%)**

Individuals	Urban	Urban Village	Rural	Total
1985/1986				
<u>Male Headed HH</u>				
Non Poor	70	44	33	42
Poor + Very Poor	30	56	67	58
Total	100	100	100	100
<u>Female Headed HH</u>				
Non Poor	69	40	32	40
Poor + Very Poor	31	60	68	60
Total	100	100	100	100
<u>All Households</u>				
Non Poor	70	42	32	41
Poor + Very Poor	30	58	68	59
Total	100	100	100	100
1993/1994				
<u>Male Headed HH</u>				
Non Poor	75	57	46	56
Poor + Very Poor	25	43	54	44
Total	100	100	100	100
<u>Female Headed HH</u>				
Non Poor	66	52	43	50
Poor + Very Poor	34	48	57	50
Total	100	100	100	100
<u>All Households</u>				
Non Poor	71	54	45	53
Poor + Very Poor	29	46	55	47
Total	100	100	100	100

By 1993/94, there was a slight improvement, since the total percentage of Batswana who were then living in poverty was 47. At that time, the percentages of females and males who were poor or very poor were, respectively, 50 and 44.

The same data source suggests that the highest incidence of spatial poverty occurred in the rural areas for both 1985/86 and 1993/94 as well as for males and females. In 1985/86, whereas 68 per cent of the rural population fell under the category of the poor or the very poor, only 58 per cent of the urban villagers and 30 per cent of the urban dwellers were poor or very poor. In 1993/94, 57 per cent of female rural dwellers and 34 per cent of urban females were either poor or very poor. Those percentages translate to 189,611 rural females and 38,708 urban females leading poor or very poor lives.

4. The Choice of SMEs as a Strategy for Poverty Reduction

Although the choice of SMEs as a strategy for poverty reduction would not run into any significant difficulty in meeting the approval of policy makers and development economists today, such a proposition would have raised eyebrows among the officials and academics during the second part of the 1960s and most of the 1970s. At that time, development economists had almost no regard whatsoever for these enterprises as generators of employment or income. According to the development economists at the time, the surest way for a developing country to enjoy accelerated growth and sustained development was through large scale capital intensive enterprises (Loveman and Sengenberger, 1991; Gray et.al.,1997).

It was believed that SMEs were seriously disadvantaged by their very rudimentary nature and characteristics. Characteristics such as simple management and organizational structures, rudimentary technologies, low skill requirements (characteristics which have made the SMEs the centre of attraction today) were then looked at as factors that would spell their doom in a world characterized by stiff and brutal competition. However, and on the contrary, the experience of the late 1980s and the 1990s clearly suggests that this attitude has taken a complete turn-around. Available statistical evidence suggests that there has been a sharp acceleration of the SMEs in the 1990s and a corresponding pronounced interest in the enterprises from local and international donors. This renewed interest can partly be explained in terms of the decline in the trend of global economic performance, which started after the second half of the 1970s. Several factors were responsible for this decline, chief among them being: the first and the second oil shocks which took place in 1973/74 and 1978/79, respectively; the emergence of the external debt crisis and the structural changes that took place in the international capital markets; and the domestic macroeconomic policies adopted by various countries. The consequence of this decline had a devastating effect on the labour market: the employment capacity of the labour market declined drastically. This, coupled with rapid population growth rates and the pool of semi-skilled and skilled labour released from the civil service and parastatals as a result of reforms, had the effect of multiplying the numbers of unemployed who were candidates for the SMEs in the formal and the informal sectors.

The attraction of the SMEs as an alternative employment generator derives from very nature and characteristics which have made the enterprises relatively more accessible to the poor, the less skilled and the less sophisticated. First of all, whereas the severe economic stress has resulted in larger firms losing steam and consequently collapsing, the SMEs have often survived and maintained their competitiveness (Birch, 1979, McPherson, 1996; and Loveman and Sengenberger, 1991). Second, their labour absorptive capacity is higher than the larger formal sector enterprises, and, in addition, their average capital costs per job created is considerably smaller (Mlambo, 2001). Third, and probably the most important set of factors that determine the attraction and accessibility of the SMEs to the poor, derive from the fact that the enterprises are characterised by high labour intensity, ease of entry and exit, small start-up and operating capital, low labour skill requirements, and they give impetus for entrepreneurial and indigenous technological development (Mlambo, 2001; and Ikiara, 2001). In a recent study he conducted in Zimbabwe, Mlambo found that while the formal sector employment has experienced significant declines, the SMEs have become the leading employment creator (Mlambo, 2001). In the same study, Mlambo notes that as economic hardships escalate, and as unemployment, skewed income distribution and poverty worsen, the SMEs have come to attract the attention of entrepreneurs, governments, non-

governmental organizations, donors and other institutions (Ibid). Table 2 provides data on the rapid increase of SMEs in Zimbabwe between 1991 and 1998 and the numbers of employees in the SMEs service sector in Mauritius between 1985 and 1998.

Table 2: The Numbers and Growth of SMEs and Employees in the Enterprises in Zimbabwe and Mauritius

	1985	1991	1992	1993	1997	1998
1. Zimbabwe						
i. No. of SMEs		254,667		255,241		331,251
ii. % Growth 1991-1998						30.1
2. Mauritius						
i. Employees in SMEs Service Sector	38,471		50,767		58,519	
ii. % Increase 1985-1997					52.16	

Source: Mlambo (2001) and Dabee (2001)

The table suggests that between 1991 and 1998, the numbers of SMEs in Zimbabwe grew at an average annual rate of 30.1 percent. In the case of Mauritius, employment in the SMEs service sector increased by 52% over the period 1985 and 1993.

5. The SMEs in Botswana

Findings from a recent study on employment creation in Botswana suggest that the trade and services sector commands the largest percentage share of SMEs in the country (Mukras, 2000; Siphambe, Mukras and Oucho, 2001). A total of 82 percent of the SMEs fall under the trade and service sector, while manufacturing and construction have 15 percent and 3 percent of the total respectively.

Table 3: Sectoral Distribution of SMEs in Botswana

Sector	Trade & Service	Manufacturing	Construction	Total
Percentage	82	15	3	100

Source: Mukras, 2001

In terms of education, the data suggest that the majority of the entrepreneurs manning these enterprises have primary or secondary school education, as can be seen in Table 4. A total of 31 percent of the entrepreneurs in the manufacturing sector have primary education; 30.6 in the trade and service sector have Junior secondary education and 25.6 percent in the construction sector have junior secondary education. Another 25.6 percent have senior secondary school (SSS) education, and a further 25.6 percent have higher than SSS education. These statistics do suggest that the construction sector is the most demanding sector in terms of its education requirements.

Table 4: Education of Entrepreneurs in Botswana

	Manufacturing	Trade and Service	Construction
No Schooling	6.2	1.2	2.3
Primary School	31.1	23.8	20.9
Junior Sec. School	29.1	30.6	25.6
Senior Sec. School	28.6	28.7	25.6
Above SSS	5.0	15.6	25.6
Total	100	100	100

Source: Siphambe, Mukras and Oucho, 2001

One important determinant of success of any enterprise is the attitude of the entrepreneur. The study on employment generation in Botswana cited above made an attempt to determine the attitude of entrepreneurs towards the success of their enterprises. In particular, an attempt was made to find out from the entrepreneur whether in his opinion the responsibility for the success or failure and the problems encountered by the enterprise should be ascribed to the government, the entrepreneur or both. Most entrepreneurs responded that such a responsibility rests with them and not the government. Table 5 summarises these results. The results, overall, do suggest that the attitudes are positive.

Table 5: Attitude/Responsibility for Success/Failure and Problems Encountered (%) by Entrepreneurs in Botswana

	Self	Government	Both	Total
Manufacturing	75	15	10	100
Trade and Service	84	8	8	100
Construction	65	14	21	100

Source: Siphambe, Mukras, Oucho, 2001

6. Constraints Facing SMEs in Botswana

The SME's in Botswana face a large number of constraints that have varying degrees of adverse effects on their performance. We shall look at these constraints on a sectoral basis.

6.1 The Manufacturing Sector There are three main constraints facing enterprises in the manufacturing sector. Listed in order of their importance, the constraints are: delayed and non-payment by clients, inadequate finance and shortage of markets. In Kenya, the shortage of markets is the leading constraint. These data are summarised in Table 6.

**Table 6: Constraints Facing SMEs in Manufacturing Sector
in Botswana and Kenya (%)**

Problem	Botswana	Kenya
1. Delayed and/or non-payment by clients	23.0	-
2. Inadequate finance	20.0	12.3
3. Shortage of market	16	19.8
4. Power and water rationing		13.3
5. High cost of raw materials		7.5
6. Stiff competition		6.1
7. Others	41.0	41.0
Total	100	100

Sources: Ikiara, 2001; Siphambe, Mukras and Oucho, 2001

To resolve these problems, the entrepreneurs made a number of proposals: provision of loans/ credits at low rates of interest (62% in Botswana and 37.2% in Kenya); facilitation of access to markets by restricting manufacturing licences to avoid over-crowding (8.3% in Botswana); providing ready markets for finished goods (8.1% in Kenya); and provision of reliable alternative sources of water and electricity (6.2% in Kenya).

6.2 Trades and Service Sector Like the manufacturing sector, the first two most common constraints facing the trade and service sector in Botswana are delayed and/or non-payment by clients and the shortage of markets. In Kenya, the shortage of markets, lack of reliable utilities and shortage of finance feature once again as the top most severe constraints. Table 7 provides comparative data on constraints faced by the sector in Botswana and Kenya.

**Table 7: Constraints Faced by SMEs in Trade and Service Sector
in Botswana and Kenya**

Problem	Botswana	Kenya
1. Delayed and/or non-payment by clients	29	-
2. Shortage of market	17	18.9
3. Theft/unreliable workers	16	4.8
4. Shortage of finance	9	10.3
5. Lack of unreliable utilities	9	11.4
6. High taxation		9.3
7. Harassment by authorities		4.9
8. Stiff competition		8.3
9. Others	20	31.7
Total	100	100

Sources: Ikiara, 2001; Siphambe, Mukras and Oucho, 2001

Entrepreneurs interviewed proposed the following measures for dealing with their constraints: training of their employees; facilitating enterprises in their efforts to secure markets; provision of credits at low rates of interest; and lowering of taxes.

6.3 The Construction Sector Among the three sectors included here, the construction sector is the least popular sector. Entrepreneurs claimed that the sector is difficult as well as being fraught with severe competition. The three most important constraints cited in Botswana are delayed and/or non-payment by clients, lack of adequate finance and stiff competition, especially from foreign construction firms. Table 8 contains data from Botswana and Kenya on constraints cited by entrepreneurs in the construction sector.

Table 8: Constraints faced by SMEs in the Construction Sector in Botswana and Kenya

Problem	Botswana	Kenya
1. Delayed and/or non-payment by clients	32	11
2. Lack of adequate finance	20	8
3. Stiff competition	12	11
4. Theft	12	-
5. Scarcity of contracts (markets)	-	13
6. Scarcity of raw materials	-	13
7. High cost of raw materials, labour and transport	-	12
8. Insecurity/high risks	-	10
9. Others	24	22
Total	100	100

Sources: Ikiara, 2001; Siphambe, Mukras and Oucho, 2001

Once again we can clearly see from these data that the same constraints feature at the top of the list in both countries: shortage of finance, shortage of markets, stiff competition and delayed and/or non-payment by clients. The entrepreneurs feel that these constraints can be resolved by undertaking the following measures, among others: provision of credit facilities or subsidies (both Botswana and Kenya); giving entrepreneurs relevant training and technical assistance (both Botswana and Kenya); assisting entrepreneurs to secure a larger share of the market by awarding them more contracts (Botswana); and restricting licensing to reduce overcrowding of contractors in the sector and consequently reducing competition.

7. Recommendations for Strengthening SMEs

The principal objective of this piece of work is to provide a set of policy recommendations designed to reduce poverty by strengthening SMEs. The issue of strengthening an enterprise has, in essence, numerous dimensions. A strong enterprise is one which is well managed, a requirement which calls for an efficient and effective entrepreneur and as work-force; the enterprise must have adequate start-up and operational capital; it must have at its disposal, as well as be able to apply, an effective and appropriate technology; it must have the capability of penetrating the market; and it must be capable (sometimes with and other times without assistance from outside) of resolving constraints

it is facing. With this type of strength, the employment and income generating capacities of the SMEs will be highly enhanced.

The recommendations listed below have been principally derived from the constraints facing entrepreneurs.

Recommendation 1: Provision of Soft Loans Among the constraints that kept on surfacing from sector to sector was inadequate capital, both start-up and operating capital. Entrepreneurs repeatedly emphasised the scarcity of capital as a serious problem hampering the performance of their enterprise. We therefore wish to recommend that SMEs be provided with capital at low and affordable rates of interest.

Recommendation 2: Application of Appropriate Technology The important role of technology in the improvement of the efficiency and effectiveness of production is no longer in dispute. What needs to be looked at and considered with caution is that any technology that is to be applied must be appropriate and carefully targeted to achieve desired objectives. Cognisant of the benefits of technology, we are here recommending that SMEs should be equipped with appropriate and targeted technology with the following four properties: technology which is friendly in terms of entrepreneur capabilities; technology which is cost-effective and will therefore not raise the start-up and operational costs disproportionately; technology with soft administrative demands; and technology which will significantly raise the employment and income generating capacity of the enterprise while still remaining profitable.

Recommendation 3: Research for the Promotion of the Appropriate Technology Although we have recommended the application of appropriate technology by the SMEs, such technology may not be readily available in the shelves for immediate purchase and application. Moreover a second best technology that may be available may be far from satisfying the suitability criteria that we might have set aside for choosing technologies appropriate for our SMEs. In the circumstances, it may be more efficient and cost effective to challenge the appropriate engineering department to conduct research so as to evolve these type of technology as well as similar and closely related technological products. We therefore recommend that research be encouraged into areas of generating appropriate technology and similar production concerns.

Recommendation 4: Training of Entrepreneurs and Workforce In any credible enterprise, both the management as well as the work force must be trained in their respective areas of operation. In other words, for an enterprise to carry out production efficiently, in addition to enjoying a smooth and efficient management environment, relevant training in technical, managerial and financial areas is indispensable. Further testimony to the importance of training is given by entrepreneurs in the construction and trade and service sectors. These entrepreneurs strongly emphasised the dire need for the right type of training for both the work force and the entrepreneurs. We therefore recommend that both the entrepreneurs and the work force should receive relevant and appropriate training so as to ensure the efficient operation and management of the enterprises. Among the areas where training can be conducted are: general management, sales and marketing management, accounting, motor mechanics and electricians, welding and metal works, and carpentry and upholstery.

Recommendation 5: Gender Dimension Comparative data presented in Table 4.1 on the rates of national poverty headcount suggest that female headed households are poorer than their male headed household in urban, urban village as well as rural areas. Although the numbers of females who participate in the SMEs as entrepreneurs are slightly larger than their male counterparts, they have much greater difficulties in securing start-up as well as operating capital than their male counterparts (Mlambo, 2001). Moreover, even where they have clearly demonstrated credible expertise such as in bricklaying, carpentry, electricity installation, welding, and printing as documented by Mlambo in Zimbabwe, they are not afforded equal opportunities and resources to promote their efforts. We therefore recommend that a deliberate effort is necessary to promote the advancement of women in the SMEs so as not only to correct the imbalance in the opportunities made available to reduce poverty among women, but to also facilitate greater female participation in the SMEs sector.

Recommendation 6: Fiscal and Financial Incentives The incentive structure facing an economic unit, whether such a unit be in the educational sector, manufacturing sector or service sector, is an important determinant, other things being equal, of the physical and mental energy that the unit is prepared to harness in order to take advantage of the available incentives and consequently make success out of the operation it is undertaking. Put differently, given that the right attitude towards the success of an enterprise does exist, incentives, when correctly chosen and targeted, will certainly have the effect of not only motivating the entrepreneur, but also have the potential of spurring greater urge to work relentlessly for the success of the enterprise.

Mauritius has a good measure of success incentives in the promotion of SMEs. Among the incentives the country has offered the SMEs are income tax relief; development incentives; exemptions from customs duty; and exemptions from VAT. In light of the above argument and the experience of Mauritius, we wish to recommend that suitable financial and fiscal incentives be established for the promotion and strengthening of SMEs.

8. Conclusions

Available statistical evidence suggests that poverty is an issue of national concern in Botswana. Although attempts have been made to ameliorate, if not eliminate the problem, the measure of success so far achieved has, however, not been promising as the problem continues to persist.

A strategy recommended in this paper for poverty reduction in Botswana takes the route of strengthening the SMEs. Although these enterprises face a number of constraints, chief among them being non-payment or delayed payments by clients, inadequate finance and the narrowness of product markets, it is argued here that these constraints are not binding and the implementation of appropriate well designed policy measures will go a long way in strengthening the employment and income generating capacities of these enterprises, thereby reducing the problem of poverty. A total of six recommendations are made, the following being among them: provision of soft loans; fiscal and financial incentives; research for the promotion of appropriate technology; promotion of advancement of women in the SME sector; and training of entrepreneurs as well as the work force in the sector.

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