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The State of Entrepreneurship in Pakistan: Engaging Youth in Economic Growth

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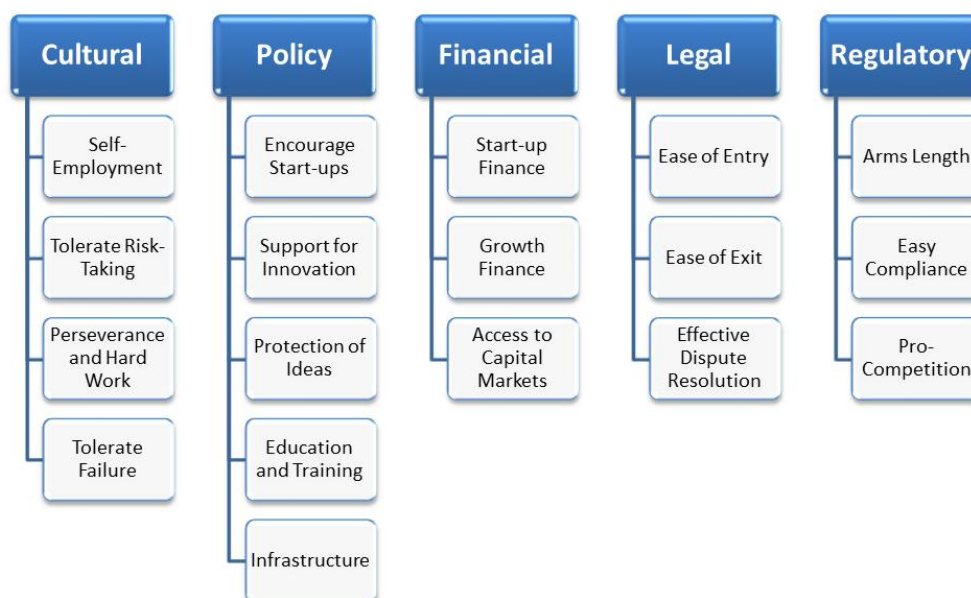
Research and Development Department

State of Entrepreneurship in Pakistan: Engaging Youth in Economic Growth

1. Entrepreneurs and Economic Growth

Entrepreneurship has gained a unique standing in traditional and new economic growth perspectives that amply highlight the role of labor, capital, natural resources, technology and innovation as well as the process involving the creation of firms in helping economies expand and create jobs on sustainable basis. The ability of firms to harness these factors of growth effectively determines the true dynamism of a given economy. Entrepreneurs are critical for the creation of firms and unleashing countless new sources of economic growth, employment and improving living standards.¹ Entrepreneurs are risk-takers when trying to commercialize novel product and service ideas generated as a result of new knowledge and diffusion of science and technology. The success of entrepreneurship greatly depends on enabling cultural, policy, financial, legal and regulatory environment conducive to risk-taking.

Entrepreneurship Development Framework



Source: From the Authors, 2012

¹ The International Labor Organization notes that “enterprises and the entrepreneurs who run them play a crucial role in creating jobs and reducing poverty.” <http://www.ilo.org/empent/lang--en/index.htm>

High growth economies around the world have consistently ensured aspiring entrepreneurs are encouraged with the help of an efficient business start-up and growth support system that provides low cost loans and risk-finance, technology leads, networking and marketing opportunities, predictable and transparent legal and regulatory environment, provision of training and development, and infrastructure necessary to innovate, operate and grow. Education is increasingly becoming a focal point for encouraging entrepreneurship among youth.² Education and training prepares entrepreneurs to better understand commercial opportunities and growth is vital for promoting young entrepreneurship.³ In this regard, young female entrepreneurs should equally be supported as equally capable of developing commercial acumen.⁴ This in the presence of cultural appreciation for self-employment can churn out new enterprises at a much faster pace.

Cultural acceptance for entrepreneurs is often low in developing countries for a variety of reasons including state presence in the economy and family ownerships. Public sector jobs are preferred for security, stability, influence and honor considerations. On the contrary, in societies where state is greatly absent from economic opportunities, business start-up rates and prospects for success are much better. The presence of state in economic activities suffocates the birth of new enterprises. Many sectors of the economy are closed to competition. Pakistan is no different. The state is heavily engaged in economic activities. Public sector enterprises (PSE) are not only inefficient and a burden on government finances but are also constraining the process of firm creation. With regards to family-owned businesses especially involving extended family members, conservatism takes deep roots often suffocating the birth of new ideas. On the other hand, publically listed companies are more entrepreneurial vis-à-vis market pressures for innovation and competitiveness.

Entrepreneurship in family businesses has its own unique dimensions and challenges. This is an important issue given the fact that around 80 percent of businesses in Pakistan and elsewhere in the world are family-owned and operated. Most family businesses are risk-averse. Many focus survival rather than growth. Excessive risk-

² According to Organization for Economic Co-operation and Development (2007) "education can contribute greatly to creating a more entrepreneurial culture, starting with young people at school. Education can also provide entrepreneurs with tools to develop and expand their business, for example through management training and business advisory services. Access to skills is also affected by factors such as labor market regulation" (2007: 25).

http://www.ioes.hi.is/events/DEGIT_IX/Papers/Antonietti_vanZon.pdf

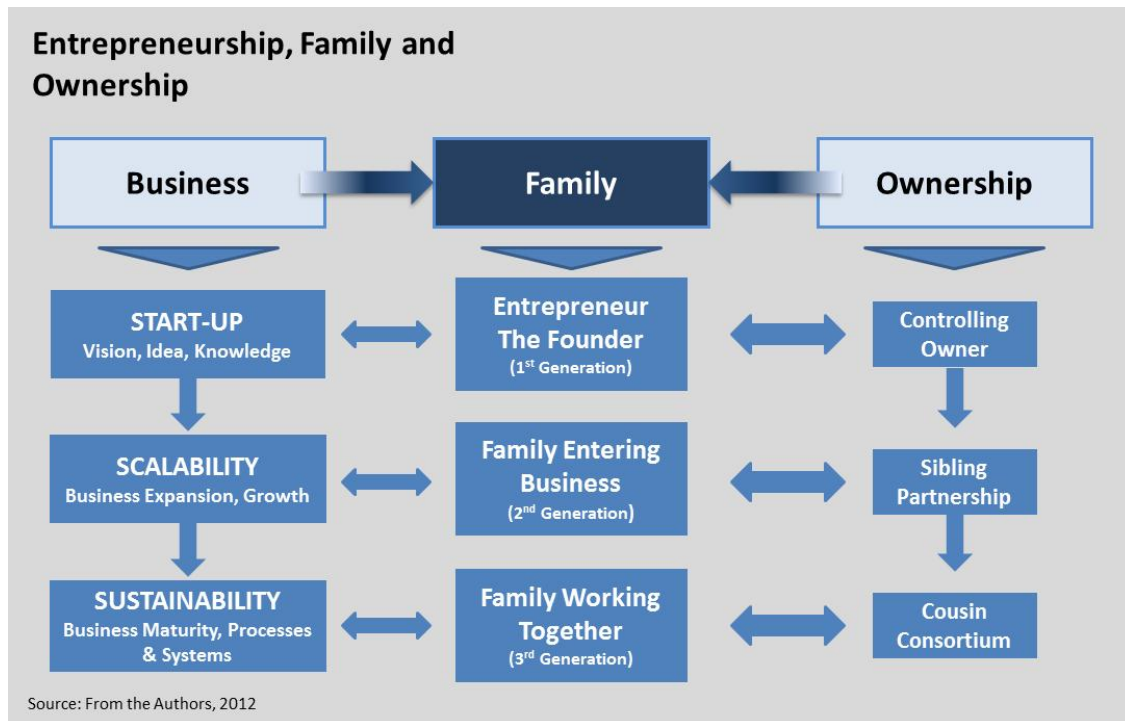
³ According to Global Entrepreneurship Monitor (2010), "entrepreneurship education is the building of knowledge and skills either "about" or "for the purpose of" entrepreneurship generally, as part of recognized education programs at primary, secondary or tertiary-level educational institutions," and "entrepreneurship training is the building of knowledge and skills in preparation for starting a business" (2010: 8).

<http://www.gemconsortium.org/download/1268382743599/GEM%20Special%20Report%20on%20Ed%20and%20Training.pdf>

⁴ One of the key reasons hindering female entrepreneurship in Pakistan is that they ... "are not given the opportunity to start a venture and nurture it into a successful business. Women are looked as the "food-makers" rather than the "food-earners." However, research does show that those women who have been given the chance and the proper resources have worked to become strong entrepreneurs." For details see International Entrepreneurship:

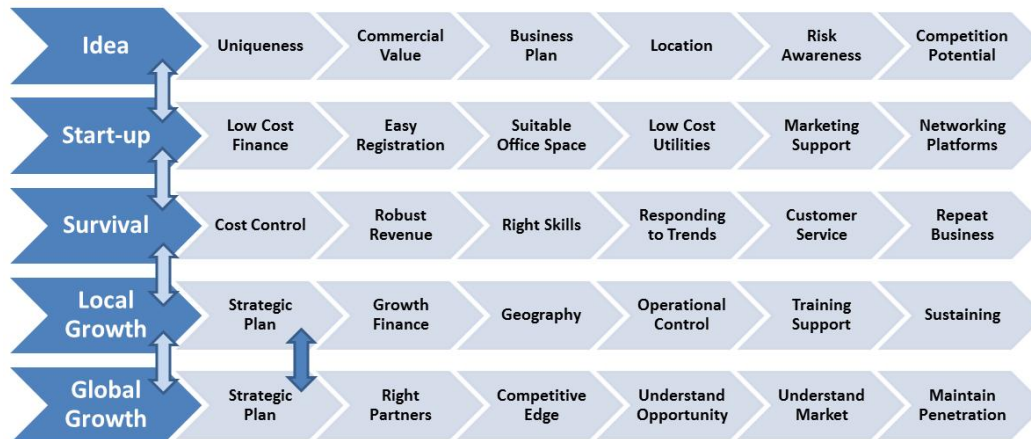
http://www.internationalentrepreneurship.com/asia_entrepreneur/pakistan_entrepreneur.asp

aversion compromises entrepreneurship that is essential for survival and growth. Resultantly, only 15 percent of family-owned-managed businesses survive till the 2nd generation and less than 3 percent family businesses survive till the 3rd generation stage. This is due to a variety of reasons. First, owners are not necessarily good managers. Second, owners do not necessarily share all information with employees which leads to less than optimum decisions. Third, incentives structure of managers in family businesses is often weak that effects performance. Fourth, outsourcing critical advisory is not easily forthcoming in family businesses. Fifth, family businesses are not very good in timely responding to new trends. Sixth, family is family. The interplay of family relations and demand of running business complicates decision making. This also discourages the introduction and adherence to formal corporate practices in running firms. The result is that family businesses experience uncertainties throughout various phases of growth and as controls pass from the founders to siblings and to cousin consortiums.



Entrepreneurship is a behaviour and a step-by-step process. It is stage-and scale-neutral and required at every phase of economic development and firms' growth irrespective of size. It is by no means limited to starting a business. **We define entrepreneurship as commercialization of an idea and its growth.** High long-term growth flows from unhindered flow and growth of ideas. This is an agenda for job creation and economic development. Key pillars of the entrepreneurship development framework as elaborated above need to support the entrepreneurial process undertaken by individuals and firms. Developing countries can learn a lot by ensuring a comprehensive and strategic approach to supporting entrepreneurial behavior and process step-by-step. Lack of support at any stage can stunt the development of entrepreneurial initiatives.

Entrepreneurship Step-by-Step

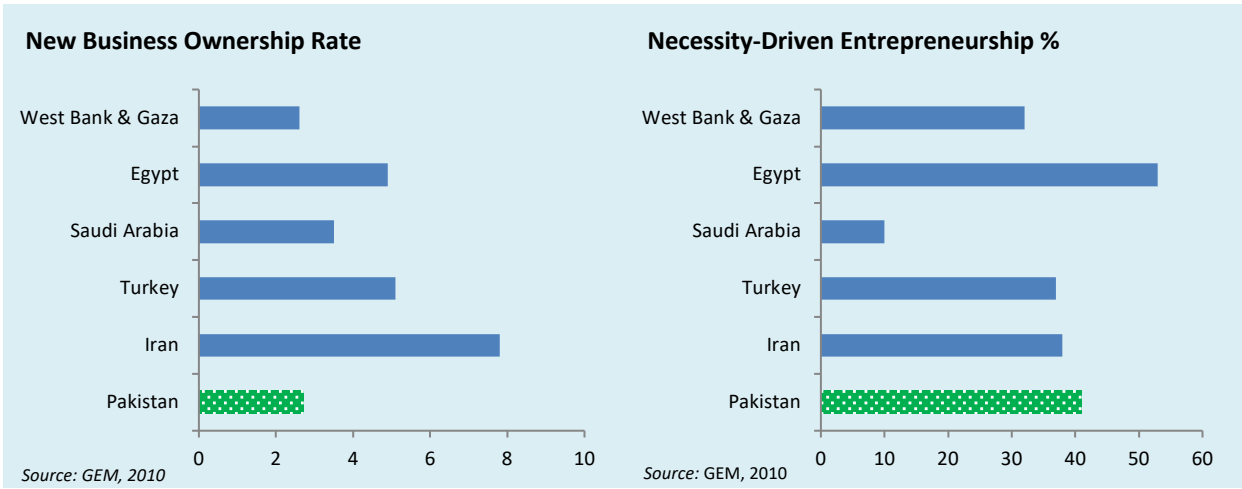
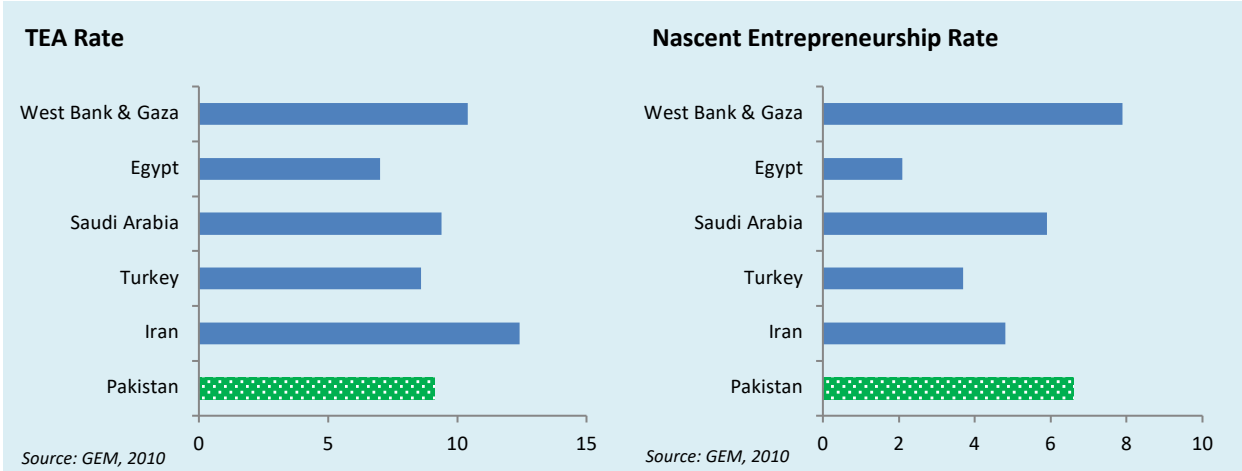


Source: From the Authors, 2012

2. Entrepreneurship in Pakistan

The Global Entrepreneurship Monitor (GEM) report on Pakistan (2010) provides interesting insights into the state of entrepreneurship in Pakistan.⁵ The report compared factors having significant influence on entrepreneurship in 59 countries classified as factor-driven economies like Pakistan as well as efficiency- and innovation-driven economies. The report also looks at entrepreneurship in Pakistan against a peer group countries comprising of Iran, Turkey, Saudi Arabia, Egypt and West Bank and Gaza. It shows that Total Early Stage Entrepreneurial Activity (TEA) rate in Pakistan standing at 9.1 percent is well below the average of 22.8 percent and 11.7 percent in factor driven- and efficiency-driven economies respectively. But TEA performance in Pakistan is better and almost comparable to countries like Egypt, Saudi Arabia and Turkey. TEA rate in Pakistan is much better than 5.6 percent average in many innovation-driven economies. TEA rate comprises of 6.6 percent nascent entrepreneurs and 2.7 percent new business owner-managers, Pakistan is doing much better in the case of former when compared with countries like Iran, Turkey, Saudi Arabia and Egypt but with reference to the latter the country is faring poorly in the same group.

⁵ For details see http://www.gemconsortium.org/docs/search?doc_cat_id=4&team_id=89&q=



New business ownership rate, 3 to 42 months old owner managers business, in Pakistan standing at 2.7 percent is much lower than 11.8 percent and 5.2 percent average of in factor- and efficiency-driven countries respectively but as good as the level in innovation-driven economies. Pakistan is mostly lagging behind in its peer group on account of new business ownership rate. The rate of established business ownership at 4.7 percent is also far below the average rate of 12.6 percent in other factor-driven economies. The report also identifies opportunity-based TEA and necessity-based TEA. The opportunity-based TEA rate in Pakistan standing at 5 percent is lower than 8 percent and 7.26 percent average in factor- and efficiency-driven economies respectively. But in necessity-based TEA, Pakistan is doing better than its peer group. The fear of failure in working age population in Pakistan standing at 27.73 percent is much lower as compared to other factor-driven economies as well across the peer group.



Entrepreneurial activities among males are also higher as compared to female population. Male established business ownership (EBO) rate is almost 9 times higher than female EBO rate. Provincial entrepreneurial scorecard is also of great interest. Baluchistan tops in startup effort and business closure rates. EBO rate is highest in Punjab. Aspirations to grow among early stage entrepreneurs and business managers are also low in Pakistan when compared with other reporting countries. This is due to combination of difficult global economic conditions and weaknesses in the local investment climate. Most experts on entrepreneurship in Pakistan interviewed were less confident about the impact of existing government programs. Culture and social factors for entrepreneurship development are also less favorable in Pakistan when compared with many factor- and efficiency-driven countries.

3. Promoting Entrepreneurship in Pakistan

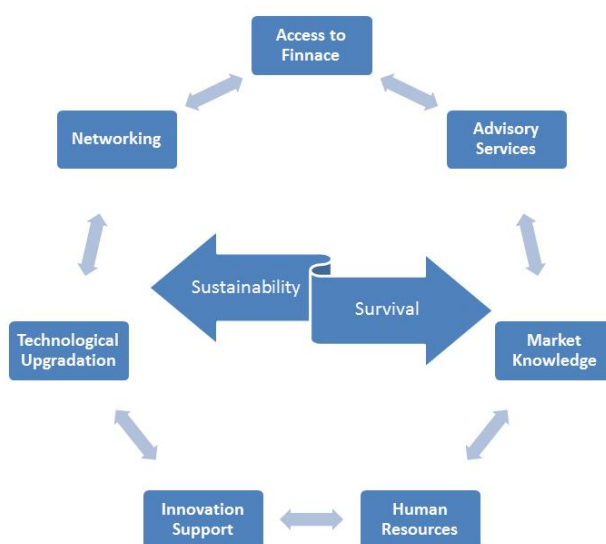
Entrepreneurs are already driving growth in Pakistan but largely in the informal sector. This is because red-tape and weak investment climate continues to discourage starting a business in the formal sector. The country has a large informal economy buzzing with small businesses providing a lot of jobs. But these businesses are not growing. Small businesses operating mostly in the informal sector routinely fail. They rarely graduate to medium sized enterprises (SMEs) and these entities in turn find it challenging and risky to grow large and globalize. This is evident from the fact that almost 98 percent of registered entities in Pakistan are SMEs operating in retail and manufacturing sector. SMEs provide 78 percent of non-agricultural jobs while contribute over 25 percent to GDP and over 30 percent to exports and represent over one third of entire value addition in the country. Increasing cost of production and weaknesses in the investment climate continue to discourage the growth of firms and many choose to operate informally. Large businesses are few and far between. Large-scale manufacturing employs only 1 million out of 50 million workers in the country. Pakistani multinational are extremely rare.

An enabling investment and business climate helps entrepreneurs to flourish. This essentially means pro-growth, pro-competitiveness and pro-poor investment and business climate. This requires action on strengthening macroeconomic foundations. Currently, this is greatly missing in Pakistan. The persistence of double digit interest

rates constraining SME credit take-off. Doing business in Pakistan remains tough.⁶ Pakistan's Doing Business ranking has declined from 96th place in 2011 to 105th place in 2012. Meaningful reforms are needed policy, legal and regulatory framework to improve business climate. This will encourage entrepreneurship in the county. Similarly, Pakistan needs to make large-scale investment into cross-cutting drivers of competitiveness ranging from health services, education, infrastructure, financial services and innovation. This will help to improve Pakistan's competitiveness ranking currently stagnating at 118th place out of 142 countries for the last two years.⁷

Pakistan also needs to develop an entrepreneurship support system as part of an enabling business and investment climate. This would require both institutional and organizational developments. **We propose a national level entrepreneurship policy.** This should be backed by appropriate legal and regulatory framework. The implementation of the policy should be entrusted with a purpose-built one-stop organizational structure having a nationwide presence. Currently, the support system for entrepreneurial activities in Pakistan is highly fragmented comprising of largely dysfunctional provincial- and national-level bodies. Small Industries Corporations and Small and Medium Enterprise Authority need redesigning especially involving reorganization and refinancing.

One-Stop Entrepreneurship Support System



Source: From the Authors, 2012

⁶ Nadeem Ul-Haque, Deputy Chairman Planning Commission and former Vice-Chancellor Pakistan Institute of Development Economics, argued: "in Pakistan innovation and risk taking is severely inhibited by the intrusive role of government in the marketplace. From the early days of planning when protection and subsidy policies determined winners in the market place, entrepreneurship has been diverted to seeking government favors." It is further argued that in order "to develop an entrepreneurship culture in the country, the system of incentives (laws and policies) that promote rent seeking will have to be dismantled." <http://ideas.repec.org/p/pid/wpaper/200729.html>

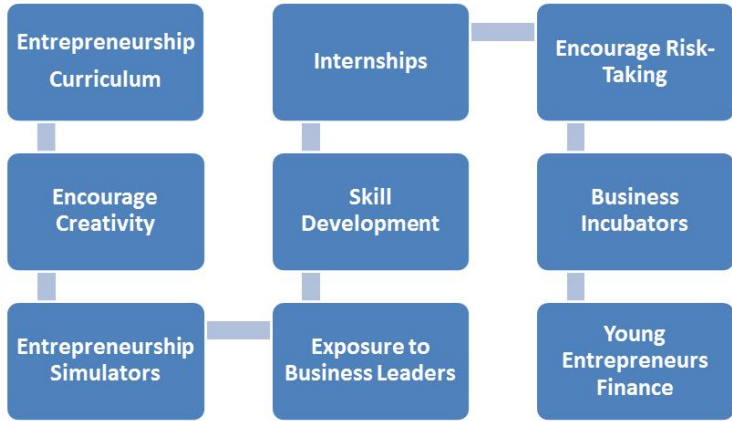
⁷ World Bank, *Doing Business 2012 Country Profile for Pakistan*, World Bank: Washington DC, August 2009.

4. Promoting Young Entrepreneurship in Pakistan

Young entrepreneurship has a special significance for economic growth in Pakistan. The country is enjoying a rare demographic dividend as around 70 percent of its population is under the age of 29 years. Around 65 percent of the youth lives in rural areas. Turning this large demographic dividend into a social and economic asset is the most important development imperative of the present time. The particularly so since public sector jobs are hard to come by. The rise of market-driven economies around the world and the accompanied rolling back of the state from economic activities in the last three decade has led to substantial retrenchment in the public sector. Private sector jobs and self-employment is increasingly replacing government jobs often preferred for security and influence considerations.

Youth employment and engagement in economic activities has immense social and economic ramifications. A number of approaches are adopted to promote youth entrepreneurship. **We propose the development of a functioning strategy to promote youth entrepreneurship in Pakistan and encourage eligible young people to start their own full-time businesses and pursue self-employment as a career choice.** This needs to involve class-room training for students to undertake business, financial and marketing planning exercises. Encouraging entrepreneurial flair at an early stage engenders a mindset change among students to undertake self-employment. Education will also equip youth with essential management and leadership skills. Making youth aware of their potential to think creatively to start their own businesses can prevent psychological problems that come from unemployment once they leave school. Such programs need to be implemented through partnerships with private sector, academia, civil society organizations and provincial authorities as well as with the help of the existing finance and business support entities.

Young Entrepreneurship Development Strategy



Source: From the Authors, 2012

Classroom entrepreneurship training links academic learning with potential business opportunities. It motivates students to adopt an innovative mindset and channel their talents towards creativity and self-reliance. Class-room training will help the youth to: 1) learn how to think innovative business ideas; 2) learn the qualities of successful

entrepreneurs; 3) learn essential business management skills; 4) learn how to become an effective business negotiator; 5) learn how to prepare and implement a business and marketing plan; and 6) learn how to become financially independent. Classroom business simulation needs to be taken to business incubation stage in a systematic manner. Business incubators will provide a wide ranging pre-incubation and incubation services to aspiring entrepreneurs. Exposing youth to learning the niceties of running a business can help them better prepare them both as entrepreneurs and good managers.

Starting-up and developing a business is fraught with many challenges. New and young entrepreneurs in particular need mentoring and coaching to deal with various start-up issues. Business incubators can be critical in providing these services. A number of business incubators are already operating in various universities across Pakistan. But their numbers are not sufficient. The business incubator model needs to be replicated nation-wide in partnership with other relevant partners. Business incubators are useful in providing pre-incubation and incubation services; the former includes marketing, product research as well as essential business planning support while latter ensures the provision of shared office space, access to information and communication technologies and advice on business management, marketing, legal/regulatory and financial issues.

Access to low cost as well as risk finance critical for promoting entrepreneurship is seriously constrained in Pakistan. This is more so for young entrepreneurs as they often lack both business history and collateral for obtaining loans. Existing finance providers need to develop special financial products for young entrepreneurs. However, it is important that public money is also made available for providing Seed Grants and venture capital, the government allocated Rs.10 billion for the latter in the Budget FY2009 but failed to disburse the amount due to budgetary constraints. Special grants of up to Rs.100,000 be provided to socially, geographically and physically disadvantaged youth for small business startup with an aim to kick start entrepreneurial activities in poorer and excluded segments of the society. This, however, would require a partnership between the government and financial sector institutions to help youth entrepreneurs get access to adequate start-up financing and growth loans.

Concluding Remarks

Large-scale efforts to engender young entrepreneurship require various partnerships for creating large-scale impact. Partnerships can align support for providing financial access for business start-ups as well as extensive mentoring for sustainability and growth. This should actively encourage the involvement of academic, financial sector and business support entities as well community-based organization, donors and volunteers. It can help initiate a series of activities ranging from helping youth to prepare their own business plans to facilitate them to access finance and all other essential business support. An effective youth entrepreneurship program should have a wider geographical and social coverage with special focus on disadvantaged young people belonging to deprived areas. Promoting youth entrepreneurship will lead to

revitalization of disadvantaged communities. Such programs are already being practiced in many countries around the world. This is based on a belief that long-term economic growth is driven by entrepreneurship and innovation. Helping youth to adopt an entrepreneurial mindset while ensuring needed support system is widely available which can lead high long-term growth in Pakistan. Engaging youth in economic activities by helping them to effectively capitalize on ideas is the only way to tackle growing joblessness and poverty in the country.