

***TAX INCENTIVE AND THE GROWTH OF SMALL AND MEDIUM
ENTRPRISES IN CASE OF AMBO TOWN.***

***A thesis submitted to the School of Graduate Studies of Jimma University in
Partial Fulfillment of the Requirements for the Award of Degree of Masters of
Science in Accounting and Finance (MSc)***

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Statement of Declaration

I Kebede Atomsa, declare that research entitled "Tax incentive and the growth of SMEs in case of Ambo town." in partial fulfillment of the requirement of the M.Sc. program in Accounting and Finance with the guidance and support of the research advisor. I do hereby declare that this thesis is submitted to Research and postgraduate studies office of Business and Economics College is original and it has not been submitted previously in part or full to any university.

Submitted by:

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This Thesis has been submitted for examination with my approval as advisor.

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CERTIFICATE

We certify that the research report entitled “tax incentive and the growth of SMEs in case of Ambo town” was done by Mr. Kebede Atomsa for the partial fulfillment of the requirements for the award of a Master’s Degree in Accounting and Finance under our supervision.

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ABSTRACT

The study analyzes the benefits of tax incentive on the growth of small and medium-sized enterprises (SMEs) in Ethiopia, taking SMEs in Ambo town as a case study. In this SMEs growth is hindered by the challenges of lack of financial resources to expand, the entrepreneur managerial skills/attitudes, inadequate infrastructural facilities and above all unpleasant taxation policy of the government. In the light of all these, this study reviews the role being played by various governmental tax incentives on the growth of SMEs. The study employed descriptive research design and inferential statistic thus; primary data was collected on variables contributing to tax influence and their benefits on the growth of SMEs. The purpose of this study has been to analysis tax incentive and the growth of SMEs at Ambo town. A sample of 230 was collected from owners and organization on the growth of SMEs at Ambo town during Descriptive statistical measures, chi square and binary logistic regression model were used for the analysis in the study. The result of the study disclose that majority of SMEs (79.1%) them did benefits from tax incentive but only around (20.9%) of SMEs were not benefits from tax incentive, Out of the SMEs who have benefits from tax incentives, 50 % and 29.13 % were male and female respectively. The log odd that who benefits using tax incentive for the growth of SMEs in the Diploma increased by 33% as compared to primary school controlling variables. Therefore, it is more advisable if Government and tax authorities should carefully consider and revisit the benefits of tax incentive policy to determine effective types of tax incentive and its implementation. It is better in encouraging SMEs should be educated on the importance and benefits for them to apply for the tax incentive.

Keywords: *Business, Catalysts, tax incentive, SMEs, growth.*

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List of Acronyms and Abbreviations

DBA	District of Business Administration
EIA	Ethiopia Investment Agency
EPZ	Export Processing Zones
ERCA	Ethiopia Revenue and Custom Authority
FDI	Foreign Direct Investment
FIRS	Federal Inland Revenue Service
IFC	International Finance Corporation
MFIs	microfinance and institutions
MIGA	Multilateral Investment Guarantee Agency
MSMEs	Micro small and medium enterprises
NBE	National Bank of Ethiopia
SMMIDA	Small and Medium Manufacturing Industry Development Agency
SPSS	Statistical Package for Social Sciences
TGE	Transitional Government of Ethiopia
TREO	Tax Remissions and Exemption Office
UNCTAD	United Nations Conference on Trade and Development
UNIDO	United Nations Industrial Development Organization
VAT	Value added tax
WEBS	World Business Environment Survey

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CHAPTER ONE

INTRODUCTION

1.1. Background of the study

The role of government and community and private enterprise in developing the Small and Medium Enterprise sector are found in a number of advanced, promising as well as developing economies (Ntiamoah, 2016). As the SME sector fails to grow, in particular where clear potential exists, this would be measured as a market failure for which effective government intervention could improve the market outcome (Labonte, 2010). Governments could play the significant role by taking actions to mitigate market failure and eliminate policy biases (Authority, 2006). Governments can also develop policy and environment for the SMEs sector to grow and play the role as catalysts towards its sustainability (Al Barwani et al., 2014).

SMEs are frequently in an unfavorable position in market competition, have difficulties in competing with large enterprises and remain compromising to market risks, which result from their nature of business, i.e. small size and weak capacity (Neneh, 2011). The vitality and competitiveness of SMEs and the comprehensive and coordinating social and economic development can be enhanced, only if the government adopts appropriate economic policies that are in line with the character of SMEs, properly handle its relationships with enterprises, exercise macro controls of appropriate incentive and timing, and create a fair, open and enabling external environment for enterprises of varied ownership (Ong'olo, & Awino, 2013).

In addition to adopting appropriate economic policies most governments in the world provide necessary promotional business sustain for their Small enterprises. Government incentives are broadly divided into two sections; financial and non-financial. Financial incentives are property loan, working capital, grant and tax. On other hand, non-financial incentive come in forms of advisory, technical, marketing, management, networking, distribution and research and development. The application of the support is based on the SMEs theory which means they are compromising and possesses limitations (Yusoff & Yaacob, 2010). Additionally, Government

supports in developed countries also follow entrepreneurship concept on new start up business which SMEs highly need to be innovative, creative and flexible (ibid).

In reality, policies to promote the development of SMEs are common in both developed and developing countries. Policies designed to assist SMEs, especially in developing economies, have been an important aspect of industrial policy to alleviate poverty and qualify industrial enterprise of a country (Gebremichael, 2020). The main argument for favoring SMEs in developing countries is that they are increasingly playing a role in economic growth and development through their contribution in the creation of wealth, employment, and income generation (Abor & Quartey, 2010).

Most of the developed countries are characterized by the growth of small and medium enterprises. For example, Poland adopted the policy of encouraging investment in the share of SMEs by removing taxes applied on profit made when selling a security. In India and South Korea investor, benefit from reduced capital gain taxes on SME's equity investments. By cutting of short term capital gains in half from 30 to 15% for share listed of small and medium enterprises. The UK and Spain governments also adopted a tax incentive policy where retail investors may deduct asset percentage of the value they invest in SMEs equity. This is happening through offering tax offsets only for acquiring new SME's equity offerings. In France, the investors can get a tax credit of 18% of the value invested in innovation mutual funds. Latter at least 60% of their portfolios in SMEs equity via these policies have been adopted; the possible outcome may not significantly affect entrepreneurs as their interest rather lies with the capital influence from equity offerings in SMEs (Broersma and Gautier, 2017).

Belgium also offers several investment allowances. The investment deduction for small and medium enterprises amounts to 10.5% of depreciation taken on assets. The rate varied between 10.5 and 12.5% since 2009. In addition, an allowance of 20.5% is grand to SMEs for investments in protection measures in either the year of the investment or the following year. Concerning carry forwards, the same rules apply as for the person previous mention deductions. on the other hand SMEs are allowed to deduct an additional 0.5 %, since 2012; carry forwards are no longer possible (De Wit and De-Kok, 2014).

The tax incentive is also common in developing countries especially in Africa, for instance, Zimbabwe provides investment incentives with six objectives in those are employee creation, small business development, industrial development, export promotion, spatial development and upliftment of low standard life. Most of the incentives taken in form of financing arrangements, which operate through the minister of industry and international trade the industrial development corporation and the Zimbabwe investment center. The most widespread tax incentive grows to exporters under the export processing, zone (EPZ) (Kaplan, 2001).

The Tanzania's tax incentive programs aim to attract productive investment, create employment and enhance exports. In Tanzania investment Act of 1997 provides the fundamental framework for investment promotion, through associated tax measure was incorporated into respective tax legislation. The main change in 1997 was to end income tax holidays outside of export processing zones, in favor of expensing of capital assets and remission from customs duty on capital goods for holds of certificated of investment from Tanzania (Zee et al., 2002).

The Ethiopian government has been also provided that investment incentives to support private investment and to promote the inflows of foreign capital. Custom Duty, loss carried forward, tax holiday, Duty Drawback Scheme and Voucher Scheme are some among the investment incentives given by Ethiopian government (Semiret, 2013).

The policy rational for tax incentives are aimed at creating conducive environment for both domestic and foreign private investors. The overall policy of the government is designed to improve the living standards of the people, enhancing economic growth and thereby increase the productivity of revenue (ERCA, 2011). To achieve the desired Economic growth and development there needs to be structural changes from low to high productive economic activities; like regional investment, sectoral investment, performance enhancement and transferring technology (UNCTAD, 2012).

The growth SMEs was attributed to 12.6 percent growth in industrial output, 11 percent increase in service sector and 3.3 percent expansion in agriculture. Consequently, the share of industry in GDP has increased to 28.1 percent in 2018/19 from 27 percent in 2017/18 while that of service sector rose slightly to 39.8 percent from 39.2 percent.

However sectoral investment or small and medium enterprises sector face different constraints including finance, corruption, policy uncertainty, instability, tax and regulation, governance, skill

to mention but few. Tax is mentioned to be one of the constraints that face small and medium enterprises due to this tax incentive are introduced to reduce the tax burden and in the encourage of small and medium enterprises growth. Therefore, these studies analyze the benefits of tax incentives and the growth of small and medium enterprises in Ambo town.

1.2. Statement of the problem

The concept of growth SMEs development goes beyond the establishment of formal incentive granting institutions and provision of incentive packages for small-scale entrepreneurs (Chen, 2006). This incentive package is also vital role to give emphasis on the nature of institutions, which can help or harm SMEs development in a given society (Yamoah et al., 2013).

Empirically studies have shown diverse views on tax incentives as a means for economic growth and industrial development. According to the aimed of the international journal of humanities and social sciences poverty alleviation program , to reduce the rate of poverty among the masses and this program covered the provision of jobs for able and unemployed youths, provision of loans for small and medium scale enterprises at a minimum lending rate and provide tax incentive. Several governments suggest that a tax incentive to attract investment, yet policies often fail to fully assess their likely costs and potential benefits. Incentive policy should balance the higher revenue and social benefits jobs, positive externalities, action effects from a possibly increased investment with the indirect costs of incentives such as administrative cost and the revenue losses from incentive given to investments that would have been made even without them (Sebastian,2010).

Kymabalesa (1994), states that among the important roles governments are expected to play is to facilitate the operation of small businesses in the provision of equitable direct tax including attractive tax concessions and less costly bureaucratic procedures about imports and exports. It is evident that with the help of the government it is most likely that the private sector of the country would find it conducive to operate and hence make enough profits to stimulate reinvestment.

The investment climate is also especially critical for determining the benefits of incentives in attracting investment. Every step that the investor takes to start his /her business helps to assess the investment climate. The time is taken in getting licenses and legal documents; the access to land, corruption, social and political abilities of the country allows understanding its investment

climate. These significant factors affect the alternative of the investor to invest in a particular region or sector. The investment climate influences the benefits of fiscal incentives in attract investment through the responsibility that public goods play in improving investment returns. At this point the public goods are the components of the investment climate such as infrastructure, rule of law, enforcement of contracts, and so on. However, when public goods and investment are highly balancing as with the investment climate then in countries with large gifts of such goods a go down in taxes is greatly added benefits at encouraging investment than in countries with smaller gifts (Sebastian and Parys, 2009).

As per best knowledge of the researcher, small and medium enterprises have been essential to economic development. Yet it is observed that the government is inability to effectively implement its tax policies, government grants little tax incentives to attaining the effective use of tax incentives in Ethiopia, particularly in Ambo town. Among the following are some of the genuine causes of these under achievements. Government inability to effectively implement its tax policies, government grants little or no tax incentives, problems related to finance, access to market and low competitiveness, business information, working premises, poor acquisition of technical skills and management expertise appropriate technology and access to quality infrastructure.

From what has stated above it is clear that SMEs need a favorable environment, goods, and favorable tax system would be a big incentive. As per researcher, best knowledge I couldn't got paper on this title in our country particularly in Ambo town. Given this gap, this study seeks to analyze the benefits of tax incentives that deserve to companies and the interaction that exists between the incentives and the growth of small and medium enterprises.

1.3. The objective of the study

The main objective of the study is to analyze benefits of tax incentive and the growth of small and medium scale enterprises Ambo town.

1.3.1. Specific objectives

- To identify the types of an incentive currently exists for SMEs and its implementations.
- To investigate whether tax incentive package in Ambo Town have benefited SMEs owners
- To analyze the major challenges of small and medium enterprises growth in Ambo town.

- To assess what measure was undertaken to reduce the major challenges of SME's growth about tax incentives.

1.5. Significance of the study

The analysis of the quantitative data helps to observe the tax incentive and the growth of SMEs. Analysis of the qualitative data helps to identify the major constraints, which affects the successful implementation of tax incentive. Generally, the results of this study could be useful to various stakeholders including:

i. Academics/Researchers

Findings from this study can assist academicians in increase of the prospectus with respect to this study by providing a deeper understanding of the major constraints that affect the implementation of government tax incentive on SMEs.

ii. Micro and Small Enterprises

The findings of this study help MSME operators in Ambo town, to have a better understanding about government tax incentive and to identify their weaknesses which make tax incentive difficult to get to them. Identifying their weaknesses related to government incentive package programs, may facilitate corrective actions to be taken by the operators.

iii. Governmental Policy Makers

The government can use the findings of this study to assist in policy reformulation, to ensure effective and efficient implementation process and to take appropriate corrective actions.

1.6. Scope of the study

The study was geographical, content and methodological scope. The geographical study was focus on Ambo town small and medium enterprises, Oromia regional state, Ethiopia. The Contents of the study focus on the tax incentive and the growth of small and medium enterprises, try to asses, and identify vital points related to incentives. Methodologically, the study was employee the socio - economic method of data collection and analysis, and it is the implication to the society and the economic growth as a whole.

1.7. Organization of the study

This study is divided into five chapters. The first chapter includes introductory parts of the study (background of the study, statement of the problem, research objective, research questions, and significance of the study, scope of the study and organization of the paper). The second chapter deals with review of related literature, theoretical background and empirical studies of the issue under study. The third chapter deals with research methodology. The fourth chapter deals with data presentation, interpretation and analysis of major findings of the study. The fifth chapter contains conclusion and recommendations based on the finding of the study. Lastly, list of reference materials and papers are annexed in the appendices.

CHAPTER TWO

LITERATURE REVIEW

2.1. INTRODUCTION

Small and medium enterprises (SMEs) have been defined along an abroad continuous sequence of size and type. In provisions of size, measures used to classify SMEs include employment, assets, and revenue. Definitions of SMEs vary from one organization/ associated with another, from country to country, industry and from one financial institution to another. The multilateral investment guarantees Agency (MIGA) and the international finance corporation (IFC) define small emprises as those that assets and less than \$3 million total annual sales. Meanwhile, medium enterprises are those that meet two of the following three conditions: less than 300 3employees, less than \$15 million total assets and less than \$ 15 million total annual sales, (Dabebneh and Tukan, 2007).

According to Bolton (1971), the committee defined small and medium scale enterprises are firm that meets the following three criteria. Firstly, it has relatively small and shares of the market place. Next, owners manage it in a personalized way, finally, it is not through the medium of a formalized management structure and it is independent, in the sense of not forming a part of a large enterprise. There are various criteria of the size that might be used to define a small (turnover, number of employees, capital base, profits, the extent of imports and exports), and different definitions have indeed been developed for application in a range of countries.

2.2. Conceptual Issues

2.2.1. Definition of taxation

Kohler (1961) defines tax as a charge levied by a government unit against the income or wealth of a person or corporation for the common benefit of all. The importance of taxation as an avertable tool of economic growth and development depends on the proper tax system that can generate revenue through tax. Tax incentives have the potential of attracting both local and foreign investment if properly harnessed. however undesirable that most developing countries have not been able to expand the effective of tax incentive because of the need, perhaps, to meet the desires of the electorates and the poor management of the tax system. As per Soyode and

Kajola (2006), tax incentives can be described as incentives considered to encourage investments in certain favorite sectors of the economy and which are occasionally geared towards attracting inflow of foreign exchange to match domestic supplies for rapid economic growth. Generally, these incentives are in the sectors of manufacturing, agriculture, export, soil mineral, and other areas".

Lent (1986), tax exemption, tax incentive is a simple and effective way of increasing the productivity of investments by making available to companies and businesses within the period of exemption, tax-free income. He states that it is a simple and direct way to support financially the cost of groundbreaking. Thus, it increases the profit prospects of a new venture and enables the company to recover its capital cost quaky such that the risk of investment is considerably reduced. In the same Vein and Andic (1970) argues that tax exemption leads to the buildup of the firm's fixed assets and working capital, enables affirm to reinvest quickly the tax-free earnings or part of it and to expand its business.

Modern economists have suggested that industrial development (investment) can enhance economic growth and that there is a great potential for tax incentives to promote such investments as would lead to the development of the industrial sector, and therefore, economic growth and development of SMEs. The basic premise is that without some form of government intervention or finical incentive, the private sector will not invest the socially optimal amount in the industry. Many economists argue that tax incentives can be a very useful device to attract foreign capital, especially where the most investor may be reluctant to invest due to poor investment climate.

2.2.2 Tax incentive in Ethiopia

The Transitional Government of Ethiopia (TGE) issued the first investment code (Proclamation No. 15/1992) on May, 25 1992 with the look for encourage private investment under this code areas eligible for investment incentives were limited to manufacturing and Agriculture sectors. The incentives provided were 100% exemption from custom duty on importation of capital goods and income tax exemption (tax holiday) ranging from 1-8 years depending on type and location of the investment. This proclamation had been in use for four years and substitute by Proclamation No. 37 of 1996 in June 1996. The changed Investment Code of 1996 complete areas eligible to incentives to Education, health, tourism and construction sectors.

Capital entry requirements for joint ventures reduced from US\$500,000 to US\$300,000 and for technical consultancy services reduced to US\$100,000. This code was opened the real estate sector and Electricity and water supply to foreign investors, extended the losses carried forward provision, and cut the capital gains tax from 40% to 10%.

Additionally to Proclamation No. 37/1996 enhanced and replaced by proclamation No.116 / 1998 in June 1998. The major changes bring in this proclamation were Defense and telecommunication sectors allowed to private sectors to invest jointly with government which was reserved for government only in the earlier codes. The investment code was also modified in July 2002 (Proclamation No. 280/2002), in July 2002 (Proclamation No. 286/2002 and in September 2012 (Proclamation No. 769/2012) and additional liberalized the investment regime and removed most of the remaining restrictions. In general all areas of investments are open for foreign investors except Banking, insurance and micro credit and saving services; forwarding and shipping agency services; broadcasting services; and air transport services using aircraft with a seating capacity of up to 20 passengers which are reserved for government, domestic investors and Ethiopian nationals (EIA,2014).

The main change conducted in the establishment of Industrial Zone and Investment boards were made on August 13, 2014 and July 2014 respectively. Investment incentives provided in the investment codes are free repatriation of capitals; Duty free importation of goods and vehicles related to the investment; Tax holidays up to eight years; Opening and operating foreign currency accounts; owning fixed property for the reason of the investment, Loss carry forward, duty drawback scheme and voucher scheme. Among the fiscal incentives given the most popularly used are custom duty exemption and income tax exemption (tax holiday).

2.3. Theoretical framework

2.3.1. Theories of entrepreneurship

Private enterprise theories and research remain significant to the expansion of the entrepreneurship field. Scholars to explain the field of entrepreneurship have put several theories forward. The recent study examines three private enterprise theories with a bias on the growth of SMEs. Like Economic entrepreneurship theory, psychological entrepreneurship theory and sociological entrepreneurship theory.

2.3.2. Economic entrepreneurship theory

The economics private enterprise theory has profound heredity in the classical and neoclassical theories of economics, and the Austrian market process. However, criticisms leveled against the classical and neo-classical conjectures led to the Austrian market process which was a model influenced by Joseph Alois Schumpeter (1934). Schumpeter (1934) describe entrepreneurship are a driver of market-based systems to important function of the nation of the market economy. Odeyemi (2003) argue that the theory existing a judgment active certainty in explaining this and pointed to the fact that knowledge is communicated throughout a market system. If an entrepreneur knows how to produce new goods or services or knows an enhanced way to do so, profit can be gathering from first to last this knowledge. Entrepreneurs promote knowledge when they believe it will result in some industrially defined benefits.

Nweze (2009) holds that entrepreneurs are sensitized to use cyclic facts that have possibly never seen before and never to be seen again, to produce value. Thus, the Australian market process was based on three main conceptualization (Kirzner, 1973). The previous was the arbitraging market in which opportunity grow to be known for given market player as others overlook certain opportunities or take on the suboptimal activity. The second was attentiveness to profit-making opportunities, which entrepreneurs determine, and entrepreneurial benefit the third conceptualization subsequent Say (1803) and Schumpeter (1934), was that ownership is separate from entrepreneurship.

To uncertainty and risk (Gartner, 2004). These conceptualizations show that each opportunity is unique and for that reason previous activity cannot be used to predict outcome reliably. (Casson, 2005) Contends and that an entrepreneur is the prime mover in economic development and function is to innovative or to carry out a new combination. Somebody who carries out this occupation is an entrepreneur, whether they are independent or dependent employees of a business. However, while the cause generating opportunities are unexpected in entrepreneurship literature, a generation of scholars led by Shane and Ulrich (2004) examined the relationship among the entrepreneur, product development and technological innovation. The studies noted that the technology opportunity set is endogenously created by investments in new knowledge (Udunchukwu, 2003). However, not only does new knowledge contribute to technological change, but it also creates opportunities for use by third-party firms (Jaffe, 1989), often a new

venture (Shane, 2001). The development of new knowledge gives increase to new opportunities through awareness spillovers; therefore, entrepreneurial activity does not involve simply the arbitrage of opportunities (Kirzner, 1973). In addition, the exploitation of new opportunities created but not appropriated by the current organization. In the current study, just like suggested in the economic entrepreneurship theory by Schumpeter (1934) who described entrepreneurship as driver of market-based systems, mitigating the adverse effect of market-based systems, mitigating the adverse effect of taxation requires innovation which is dependent on entrepreneurship, creating of new knowledge, risk-taking and management, adaptability and leveraging technology.

2.3.3. Psychological Entrepreneurship Theory

The stage of investigation in psychological theories is the individual (Olokoyo, 1999). The theories give emphasis to personal characteristics that define entrepreneurship. Personality character require for achievement and locus of manage are associated with entrepreneurial leaning, which involves risk-taking, innovativeness, and tolerance for uncertainty. The essence of the psychological or personal theory is the difference in individuals' attitudes. According to this theory there was the difference in attitude. That means the internal attitude and ability to judge and forecast the situation leads a man to become a successful entrepreneur define personality traits as stable qualitative that person shows in most situations. Onuba argues that there are permanent natural qualities or potentials of the individual that naturally make him an entrepreneur. Various characteristics or behaviors related with entrepreneurs are that they be likely to be more opportunity-driven (they nose around), display a high level of creativity and innovation, and show a high intensity of administration skills and business knowledge (Oluyombo, 2010).

Olorunisola, (2003) says that entrepreneurs are optimistic. (They saw the cup as half full than as half empty). Emotionally resilient and have the mental energy, they are hard workers, show intensive commitment and perseverance, thrive on the competitive desire to excel and win tend to be dissatisfied with the condition quo and need development, entrepreneurs are also transformational who are permanent learners and use failure as a tool and catalyst. They also believe that they can personally make a difference, are individual of integrity and above all visionary.

David McClelland's theory (1961) on need for achievement explained that human beings have needed to succeed, accomplish, excel or achieve. McClelland emphasized the relationship of accomplishment motivation or the need for achievement (Olaitan, 2006). According to McClelland, one would expect a relatively high. Because having a high achieve the goals and uses the skills and abilities needed to accomplish them (Nweze, 2009). Moreover, it is the inner drive of industrials that propels them to work more and to achieve something for their interest by taking a personal risk (Olokoyo, 1999).

Need for accomplishment then reflects a strong purpose point of reference, an obsession with job or task to be done consequently, McClelland advocates increasing level of need achievement in society to stimulate entrepreneurship and economic growth (Olaitan, 2006). Lastly, according to McClelland, entrepreneur is activated by the high amount of accomplishment incentive and he stated a desire to do well, not so much for the sake of community thanks or status, but for an internal sensitivity of personal achievement, encourage people to be an entrepreneur (Onuba, 2010).

An entrepreneur's need for achievement drives him to become innovative by devising tax coping mechanisms to survive in the business engagements and excel. This is what motivated the author to adopt David McClelland's theory (1961).

2.3.4. Sociological entrepreneurship theory

These are theories based on the sociological aspect. This is because socio-culture factor has a substantial influence in creating entrepreneur as well as entrepreneurship (Fred, 2010). Moreover, social and cultural factor places a high value on innovation, carefree and independence is more likely to create entrepreneurial measures than a arrangement with contrasting values (Abugu, 2007).

Among these types of theories, max Weber is protesting a value is an ancient one. These values included, first, an emphasis on the inherent goodness of work itself. A person's work was regarded as a calling in the very literal rendered as a manifestation that one that God, several, blessed one elect few predestined to share this grace. Protestant values called for self-restraint and deferred of gratification. By investing one's earning in the form of capital, one could practice such self-denial. Over many years, repeated investment of earnings created the capital base for

the takeoff of western societies into the economic breakthrough of the industrial revolution (Chibundu, 2006).

2.3.5. Schumpeter's innovation model

Schumpeter's model is a dynamic system that continually generates change and technological progress. Schumpeter's model is a dynamic one, which describes an equilibrium path the economy follows over time, not the equilibrium described by the familiar supply and demand models that were in fashion when Schumpeter first described his perception of creative damage early in the twentieth century. Schumpeter described the entrepreneur wealth as a recurrent strong wind of creative damage in which each firm seeks to gain an advantage in the market place through innovation. He criticize that the problem that is usually being think about how capitalism administers existing structures, where the relevant problem is how it creates and destroys than (Schumpeter's, 1934). Each innovation, such as a more attractive design, a lowering of production costs, a new product, and the new source of supply of inputs or raw materials, or improved management methods was pursued because it helps the possibility of generating higher profit for the innovating firm. Such creative activity also destroyed the monopoly power that its competitors had gained using their earlier innovations. Each innovator's gain is, therefore, only temporary because the creative innovation of its competitors will, eventually, destroy its hard-earned market power. This repeated formation and damage prevent permanent monopolies from developing and in the development, society enjoys continuous technological progress. Creative destruction was according to Schumpeter, the source of economic growth and the enormous increases in living standards that the world was experiencing in the early 1900s (Uduchuwu,2003).

2.3.6. A Systems theory of creativity

Mihaly Csikszentmihalyi (1988) sophisticated this theory by relating creative effort by individuals to the state of the area they are working in and the characteristics of those who evaluate the importance of the creative undertaking in the field concerned, (Ekpenyoung, et al, 1992). According to unduchkwu (2003), the environment has two salient aspects, a culture, or symbolic, aspect, which here is called the domain, and social aspect called the field. Innovation

is a procedure that can be observed only at the joint where individuals, domains, and fields interact.

2.3.7. Government Policies and Programs for SMEs in Ethiopia

In Ethiopia, the arrangement of enterprises into small, medium and large scale depends on a number of variables such as level of employment, turnover, capital investment, and production capacity, level of technology and sub sector. In Ethiopia, enterprise can be defined as Micro Enterprise as the numbers of its employees (together with the owner or family) are not greater than 5 & total asset is $\leq 100,000$ ETB for business sector and $\leq 50,000$ ETB for service sector. Enterprise with 5-30 employees and total asset 100,001-1,500,000 ETB for industry sector and 50, 0001-500,000 ETB for service sector is defined as Small Enterprise. Medium enterprise is an enterprise which has more 30 employees & total assets more than 1,500,000 ETB for industrial sector and more than 500,000 ETB for service sector (MSMEs, 2011).

2.3.8. Why Small and Medium Scale Enterprises?

Several reasons explain the focus of special policies and programs on SMEs, over and above the simple fact that they account for a large share of total employment. In addition to employment there are various reasons; Small and Medium Scale Enterprises (i) Mobilize funds which otherwise would have been idle; (ii) Have been recognized as a seed-bed for local growth entrepreneurship; (iii) Promote local growth technological know-how; (iv) are able to compete (but behind protective barriers); (v) Use mainly local resources, thus have less foreign exchange requirements; (vi) provide for the needs of the poor and; (vii) get used to easily to customer requirements (flexible specialization).(viii)SMEs can be just as, or even more productive than larger firms, credit constraints and various institutional failures that impose on them especially severely hold them back. Given that improve credit restraint and institutional failures takes time, particular support can be a useful second-best approach, according to this argument (Dalitso & Peter, 2000).

2.3.9. Characteristics of Small and Medium Enterprises

A key attribute attributed to SMEs is elasticity, and their continued existence is often attributed to their flexibility and rapidity of response to environmental change (Levy & Powell, 2006).

According to Storey (1996), state those SMEs are more flexible than large firms hence they bring about innovation in terms of their goods and service. On the other hand, MacGregor et al. (1998) suggest that the characteristics of SMEs based on the organizational 15 environment in which most SMEs operate include a small management team; centralized power and control; informal and control systems; lack of control over the business environment; lack of resources; and product technology; limited market share; heavy reliance on few customers and a chaotic organizational structure. Raymond et al. (1998) put forward that SMEs are describe by low levels of governmental youth hence planning and control processes are less formalized. The management is often the sole responsibility of the owner-manager (Abdullahi et al., 2015).

2.3.10. The role of Small and Medium Enterprises in the economy Growth

Proponents of policies and plan to support small firms have long argue that they are more labor intensive, equitable in allocate the income that they generate, widely dispersed geographically, and nurturing of entrepreneurs (Daniel Agyapong, 2010). SMEs speeds up the spirited strength of a national economy by generating employment opportunities for a lot of the people, flexibility and industrial diversification, and making use of resources that might or else not be used in the growth process (Abeka & Evance, 2011).

SMEs enjoy a ready for action benefit over large enterprises in servicing dispersed local markets (Sanusi, 2003). SMEs plays a significant role in countries economy through employment creation, income generation, productivity, proper utilization of resources, technology transfer, revenue generation, internal and international trade linkages, and equal distribution of wealth (Abdullahi et al., 2015).

Inside Ethiopia, subsequently to the agriculture sector, the SME is the next main employment-generating sector (Fiona Meehan, 2004). The Ethiopia Government was give due awareness to the expansion of SMEs, mostly for women, as a means to shrink poverty and employment creation (Rahel & Issac, 2010). In a variety of growing countries, which have great economic success, SMEs by virtue of their size, location, capital investment and their capacity to generate greater employment, have established their effect for fast economic growth (ILO, 2003). Small and Medium Enterprises contribution towards encouragement of employment for young entrepreneurs and economic development of the country is widely recognized. In contrast, there

are strong arguments that supporting and support financially SMEs will result in inadequacy, discourage competitiveness and become a bottleneck factor for development of SMEs (Biru, 2014).

The SME sector in Ethiopia is tied up with a number of problems that alleviate its growth and development, thus minimize its vital role in countrywide economic growth and improve the women's economic empowerment (ILO, 2003). The private sector in Ethiopia was residue small, which accounts for less than 50 percent of total employment in the formal urban sector. But at this time the state of affairs seems to be changing and the SMEs sector is playing a vital role in the business development of Ethiopia. It is documented that this sector provides not only employment chance, but it is also an effective means of improve poverty and reducing income inequality (Biru Ashenafi, 2014).

2.3.11. Challenge facing SMEs

Small businesses compared to large business worldwide, faces a broad scope of restriction and problems, even in effective process economic system. The limitation relate to legal and regulatory environment and business premises (at affordable rentals) and managerial expertise, access to appropriate technology, quality of the business infrastructure in poverty stricken region and, in some suitcases, the tax burden (Diale, 2009). The restriction might vary from region to region, between rural and urban, between sectors, or between individual enterprises within a sector. The common restriction include lack of capital, difficulties in procuring raw materials, lack of access to relevant business information, low technological capabilities, high transportation costs, communication problems, problems reason by burdensome and practical procedures and policies and regulations that generate market distortions (Tambunan, 2008).

2.3. 12. Government Policies and Small Scale enterprises

Government in business with other stakeholders can play a vital role in influential the situation in which growing SMEs can grow, provided that suitable business information, supporting networks and skills expansion, and ensuring the accessibility of suitable business finance. Creating an enabling environment and effective support programs for sustainable growth is not easy, however, and as policy has developed rapidly in recent years, the evaluation evidence from existing policy programs remains relatively limited (Roper & Hart, 2013). Network contacts and

relationships with larger firms both nationally and internationally are also often seen as 19 important as SMEs grow and develop. Further than the start-up phase, managerial and marketing skills allied with adequate financing and effective protection for property rights is also vital to sustain innovation and growth (Roper & Hart, 2013).

The Government can occur up with policies that can incentive package and granting the growth of novel technologies, products, and solutions (Ntiamoah, 2016). Government can likewise seem to hinder SME introduces policy which can restrict the independence, as well as the entrepreneurial freedom of some variety. To make your mind up the failure rate of SMEs, the Government decided to create the previous institution sector sound, stable, honest, dependable, globally competitive, and to strengthen its ability to provide recognition to the SMEs (Eniola & Entebang, 2015).

2.4. Empirical Evidence

Relative broad empirical findings have been developing to show that tax incentives encourage investment by the industrial sector (firms) and thus industrial development and growth of SMEs.

In study poses by Meron, (2016) a general question of whether or not investment have increased in Ethiopia because of the tax incentives existing; and thus whether or not offering such incentives has been beneficial to the country. Descriptive statistics is used to analyze the development of domestic manufacturing investment, tax income and expenditure rate of Ethiopia. Inferential statistics is also used by utilize time series OLS model. The regression result give you an idea about that tax incentives and market openness have significant positive long run effect on private domestic manufacturing investment, inflation on the other hand has significant negative long run effect

According to study by Daniel (2019) was to analyze the effect of tax incentive on the growth of small and medium-sized enterprises (SMEs) in Rwanda taking SMEs in Nyarugenge as a case study. Qualitative and quantitative research approach was adopted. Simple random and purposive sampling practice was used to choose the sample. The data set was analyzed using descriptive statistics. A multiple regression study was used to give details the relation between variables.

In the field research conducted by Aharoni (1966) on the way foreign the United States manufacturing firm made investment decisions, it was ascertained that the concession given by the host country brings about the decision to invest. It was observed that small investors are generally responsive to tax incentives than large ones. This implies that tax incentives play an important role in small business and industries because it enables them to generate enough capital for their investment/expansion. It was concluded that tax incentive is a core stimulant for investment.

Rolfe (1993), in a study on the determinants of foreign direct investment (FDI) incentives, preference differentiated between the performances of incentive schemes as it applies to new and existing firms. Using a survey of managers of our firms, it was observed that start-up firms would prefer incentives that reduce their initial expenses that target profit and manufacturing industries will prefer tax incentives related to depreciable assets because they utilize more assets than service industries.

Mayende (2013) in a study on the effect of a tax incentive on firm performance attempted to analyze the effects of tax incentives on performance of Uganda and manufacturing firms. The study finding shows those firms with tax incentives perform better in conditions of gross and value-added than their complement. The key strategy suggestion of the study finding indicates that the government needs to make more efficient the condition of tax incentives for better firm presentation. The recommendation was that the provision of tax incentives needs to be transparent, non-discrimination or of ownership of firms and criteria of accessibility is clear. Furthermore, comprehensive information on procedures and criteria for obtaining tax incentives under each existing programs need to be frequently, available to the public. This will lead to increased output of different firms, ensure accountability and guard against miss-use of the incentive.

In other to examine the relationship between tax incentives and economic growth, Ogbonna and Ebimobowei (2012) examined the impact of tax reforms and the economic growth of Nigeria from 1994 to 2009. To achieve the objective of the study, relevant secondary data was Statistical Office of the Accountant General for Federation, and other relevant government agencies. The result showed that tax incentives are positively and significantly related to economic growth and

that tax incentive stimulates economic growth. Base on the result of study accomplished that tax incentives and reform get better the revenue-generating of the government to take on socially attractive expenditure that will translate to economic growth. On the other hand, it was recommended that sustainable economic growth cannot be accomplished with tax improvement processes except out of date tax laws and rates are review in sequence with objectives, corrupt-free and efficient tax administrative machinery with personnel's accountability and transparency of government officials in the management of tax revenue.

Another researcher, Njeru (2012) was against the use of tax incentives on FDI development. Njeru (2012) sought to establish the effect of tax incentives in Export Processing Zone firm on business investment in Kenya. The study was to determine the relationship between tax incentives amid foreign direct investment in Kenya. The population for the study integrated all 104 export-processing zones firms in Kenya where the examiner select all firms located in Nairobi city using purposively generous 65 firms. The study reliability with the numerical data shows that Investments in EPZ firms increase with the increase in sales, profit as well as tax incentive. The results showed no significance when correlated with foreign direct investment. The investment incentives, trade-related incentive, and import duty exemption showed a significance level of above 0.05. From the above results, the research concludes that there was no significant improvement in foreign direct investment because of implementing tax incentives in Kenya. The findings of this study, the researcher recommends that the government of Kenya should judge another incentive separately from the tax chiefly on persons that will improve more sales, being the most significant factor attracts investment in EPZ arranged to attract foreign direct investment, especially those provided to EPZ firms.

Meanwhile, Gabe and Gray bill (2002) were mixed on their view on the impact tax incentives have on economic development. Gabe and Gray bill (2002) in research on the effect of state economic development incentive on employment growth of establishment surveyed 366 Ohio manufacturing establishments that launched major expansions between 1993 and 1995 based on the effects of tax incentives. Empirical findings point out that incentive has a very little or negative effect on actual growth and they have a considerable positive effect on make known growth. Findings also suggests that establishment that received incentive overestimated their announced employment targets more than establishments that did not receive incentives. They

concluded that incentives substantially widen the difference between announced and actual change. The recommendation was that for the government to know whether the firm has other attractive location opportunities, it must refrain from providing an incentive and the firm subsequently move to another location. This means that the government does not know whether an incentive is crucial for a proposed expansion to occur unless it denies the establishment's incentive request.

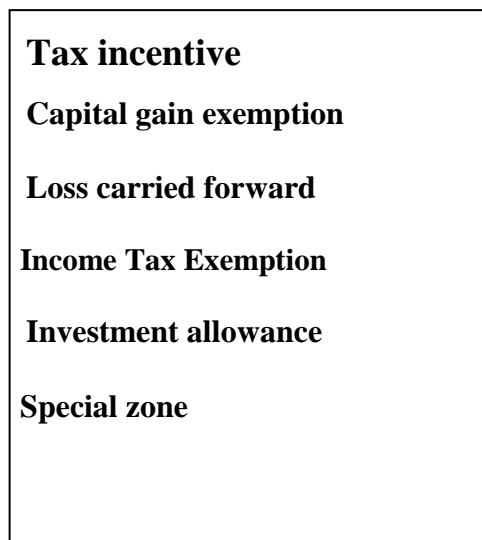
In contrast, some researchers and analysts argued that tax incentive is limited to other factors and policies to achieve economic development objectives. Munyanyi (2015) research on tax incentive and investment expansion: evidence from Zimbabwe's tourism industry. The study was encouraged by the understanding that less industrial countries use tax incentives as a means for attract incentives to have any shock on social and capital growth. In another area of the economy that improve investment in the tourism sector. Other factors like corruption, transparency in government policies, length and cost starting a business in the country, for instance, are another important factor that needs to be taken into consideration. The advice was that there is a need for political stability, consistent and supportive policy limited 33 government interference in the industrial, delegation and opening up of more local and foreign tourism encouragement inside, request of low tax rate cross industries and the general creation of a positive situation for the effectiveness of tax incentives.

2.5. Conceptual Framework

Based on the objectives of the research and review of literature exist regarding the tax incentive and the growth of SMEs clearly define independent variables and dependent variable. The dependent variable is the variable of primary interest to the researcher. Independent variables were factors that would affect the dependent variable in either a positive or negative way. The research model which shows the relationship between dependent and independent variables is presented as follows.

Conceptual frame work

Independent variable



Dependent variable

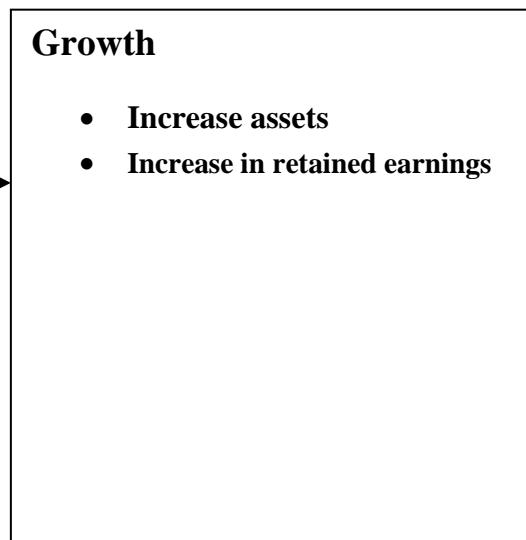


Figure 1.Conceptual framework of the study. Source: Researcher's Own Impression (2020)

CHAPTER THREE

RESEARCH METHODOLOGY

3.0. Introduction

The research methodology adopted in the study was discussed here. It shows the description of the research methods and instruments that were employed in the study. It covers the research design, population, sample size, sampling procedures, sources of data, data collection instruments, measure of research variables, and measurement of research instrument. It also shows how the research was processed, analysed and presented.

3.1. Description of the Study Area

Ethiopia is the Federal Democratic Republic composed of ten national regional states and two sub self-administered distinct towns. The study town, Ambo Town is located in West Shoa Zone in the regional state of Oromia, Ethiopia. West Shoa Zone is one of the 22 zones of Oromia National Regional State in Ethiopia. Ambo is one of the well-known 360 woreda's in Oromia regions, part of west shoa zone. It is located at 112 km west of Addis Ababa on the main road of Nekemte. In West Shoa Zone there are currently 34 rural and 6 urban kebeles. Ambo town consists of six kebeles these are Hora Ayetu, Ya'i Gadaa, Torban Kutaye, Awaro Kora, Kisose Ido Liben and Sanqalee which is administered by Ambo administrative town.

3.2. Research Design

The study was adopted descriptive survey design. According to Arvind and Vijay (2014), a descriptive survey is associated with the description of facts of a study. The design was considered appropriate for this study, as it was assist in depth investigation to analysis tax incentives and their effective on the growth of small and medium enterprises in Ambo town. This research design allows a detailed description and analysis of the variables under study, descriptive design allows the detailed description and presentation of their accurate and explaining their relationship without manipulation as supported by (Saunders et al). Further explanatory research designs were produces results that are holistic, contextual and rich in detail on the subject of the study. The study employs both qualitative and quantitative approaches to capture data for the purpose

of deep analysis and understanding the benefits of tax incentive and the growth of Small and Medium Enterprises. Document review also employed to analyze the secondary data obtained from related documents.

3.3. Study population

Sekaran (2006) define a population as the total collection of elements about which inferences was made. It refers to all possible cases, which were of interest for a study. It is the large collection of all subjects from where the needed sample is drawn. The study populations of this study were 1040. These numbers was obtained from district of business administration and that registers and exists of SMEs in Ambo town (Ambo town centre of MSMEs, 2019). These towns were selected on basis of greatly inhabited enterprises.

3.4. Sample Size and Sampling Procedure

In selecting sample, an optimum sample size was considered. According to Kothari (2000) an optimal sample was fulfill the requirement of efficiency, representative, reliability and flexibility. To determine the sample size, the researchers used solve in Yemen’s formula

$$n = N / (1 + N(e)^2) \dots\dots\dots (1)$$

= 288 SMEs were determined.

Where, N= Population size, n = sample size and e= expected error (level of precision)

Accordingly, the total population from the SMEs owners’ and the organization works of study, the confidence level is 95% with 5% of precession or expected error since the respondents had homogeneous characteristics.

3.5. Data collection procedure

This research work were involved visiting the small and medium enterprises development agency, distributing questionnaires to respondents was involved, and conducted interview with the manager coupled with discussion held with official of the government agency in charge of handling small and medium enterprise growth. The questionnaires were hand over from the respondents personally.

3.6. The Study Variables

3.6.1. Dependent Variable

The response variable in this study is the status of tax incentive on small and medium enterprises at Ambo town. The activity of government are identified either benefit of SMEs or no benefit of SMEs growth. The response variable is a dichotomous category and my interest of the study was benefit to the growth of SMEs. Thus, coded as the value 0 for 'benefit of Tax incentive for the growth of SMEs growth' and 1 for 'no benefit of tax incentive for the growth of SMEs growth'.

3.6.2. Independent Variables

The independent variables in this study are classified as Capital gain exemption; Loss carried forward, Income Tax Exemption, Investment allowance and Special zone.

The major change conducted in the establishment of Industrial Zone and Investment boards were made on August 13, 2014 and July 2014 respectively. Investment incentives provided in the investment codes are free repatriation of capitals; Duty free importation of goods and vehicles related to the investment; Tax holidays up to eight years; Opening and operating foreign currency accounts; owning immovable property for the purpose of the investment, Loss carry forward, duty drawback scheme and voucher scheme. Among the fiscal incentives given the most popularly used are custom duty exemption and income tax exemption (tax holiday).

The Council of Ministers Regulations No.84/2003, as amended in 2008, specifies the areas of investment eligible for investment incentives.

Capital gain exemption

Reduced tax rates/Preferential tax rates: are the reductions in a tax rate, specifically the corporate income tax rate.

H01: Capital gain exemption has no a significant and positive relationship with the growth of SMEs

Income Tax Exemption (tax holiday)

Any investors who invest to establish a new enterprise in manufacturing, agro-processing, production of agricultural products and information and communication technology development

are entitled to income tax exemptions. Any income tax derived from approved new investment shall be exempted for periods of 1 to 8 years, depending upon the priority area of investment activities and the geographical location of the investment. The maximum tax-exempt allowance is currently set at 2,200 Birr (US\$81) per month, but the allowance cannot exceed 25% of an employee's salary. It will also not cover expenses paid to an employee who possesses a company vehicle or uses a transportation service provided by their employer.

H02: Tax holiday has no a significant and positive relationship with the growth of SMEs

Loss carry forward

Loss carry forward refers to an accounting technique that applies the current year's net operating loss (NOL) to future years' net income to reduce tax liability. Net capital losses (the amount that total capital losses exceed total capital gains) can only be deducted up to a maximum of \$3,000 in a tax year. Net capital losses exceeding the \$3,000 threshold may be carried forward to future tax years until exhausted. There is no limit to the number of years there might be a capital loss carryover. Business enterprises that suffer losses during the income tax exemption period can carry forward such losses, following the expiry of the exemption period, for half of the tax exemption period.

H03: Loss carry forward has no a significant and positive relationship with the growth of SMEs

Investments allowance/Accelerated depreciation: is the deduction of some fraction of an investment from taxable profits (in addition to depreciation).

H04: Investments allowance has no a significant and positive relationship with the growth of SMEs

Special zones

Special zones are placed in geographically limited areas where qualified companies can locate and hence benefit from the exemption of various scopes of taxes or administrative requirements.

H05: Special zones has no a significant and positive relationship with the growth of SMEs

3.7. Logistic Regression Model

Logistic regression analysis extends the techniques of multiple regression analysis to research situations in which the outcome variable is categorical. Generally, the response variable is binary, such as (benefits or not benefits, save or no save, presence or absence, success or failure etc) in logistic regression. Further, Logistic regression analysis is statistical technique examines the analysis of various factors on a dichotomous outcome by estimating the probability of the event's occurrence. It describes the relationship between a dichotomous response variable and a set of explanatory variables. The logistic model is special case of generalized linear model where the assumptions of normality and constant variance of residuals are not satisfied. Binary (binomial) logistic regression is the form of regression which is benefits when the dependant variable is a dichotomous and the predictor variables are of any type.

Since logistic regression assumes that's $P(y = 1)$ is the probability of the event occurring, it is necessary that the dependent variables is coded accordingly. That is for the factor level I the dependent variables should represent the desired outcome. Logistic regression assumes linearity of independent variables and log odds. Otherwise, the logistic regression underestimates the strength of the relationship and reject the relationship easily, that is being not significant (not rejecting the null hypothesis) where it should be significant. Logistic regression requires quite large sample sizes.

3.7.2. Odds ratio

The odds of an event happenings (e.g. the event that $Y = 1$) is defined as the ratio of the probability that the event will occur divided by the probability that the event will not occur. That is, the odd of event A is given by:

$$\text{Odds (E)} = \frac{P(A)}{P(A')} = \frac{P(A)}{1-P(A)} \dots \dots \dots (2)$$

Where A is an event defined related to the Benefits of tax incentives

3.7.3. The Model of Binary Logistic Regression Model

The dependent variable in logistic regression is usually binary that is the dependent variable can take the value 0 with a probability of success π , or the value 1 with probability of failure $1 - \pi$.

This type of variables is called a Bernoulli (binary) variable. The relationship between the predictor and response variables is not a linear function in logistic regression instead log it transformation of π is used. Consider a collection of P explanatory that the outcome is present to denote by:

$$P\left(\frac{\pi}{1-\pi}\right) = \frac{\exp(\beta_0 + \beta_1 x_1 + \dots + \beta_p x_p)}{1 + \exp(\beta_0 + \beta_1 x_1 + \dots + \beta_p x_p)} \quad (3)$$

Then log odds of having $y=1$ is modeled as a linear function of the explanatory variables as:

$$\ln\left(\frac{\pi}{1-\pi}\right) = \beta_0 + \beta_1 x_1 + \dots + \beta_p x_p: 0 \leq \pi \leq 1 \quad (4)$$

Where β_0 is intercept and β_1, \dots, β_p is regression coefficients of the explanatory variables.

3.7.4. Methods of Estimation of Logistic Regression

The most commonly used method of estimating the parameters of a logistics regression model is the method of maximum like hood (ML). In generally, the sample likelihood function is defined as the joint probability function of systematic variables specifically, suppose (x_1, x_2, \dots, x_p) are p independent systematic observations Since y_i is the binomial systematic variable the probability function of y_i is:

$$(Y = y_i) = \pi^{y_i} (1 - \pi)^{1-y_i} \quad y_i = 0 \text{ or } 1 \quad i = 1, 2, 3, \dots, n \quad (5)$$

Since y 's are assumed to be independent, the joint probability function or likelihood function is given by $\log(y_1, y_2, \dots, y_n) =$ The log likelihood functions as:

$$L(\beta_0, \beta_1, \dots, \beta_p) = \sum_{i=1}^n y_i (\beta_0 + \beta_1 x_{i1} + \beta_2 x_{i2} + \dots + \beta_p x_{ip}) - \sum_{i=1}^n \ln\{1 + \exp(\beta_0 + \beta_1 x_{i1} + \beta_2 x_{i2} + \dots + \beta_p x_{ip})\} \quad (6)$$

The most effective and well known Newton Raph SOL iterative method can solve the equations.

3.7.5. Model Selection

In model selection, there are two competing goals: on one hand the model should be complex enough to fit the data well. On the other hand, it should be simple to interpret, smoothing rather than over fitting the data (Agresti, 2002).

3.8. Goodness of Fit of the Model

Analysis goodness of fit involves investigating how close values predicted by the model with that of observed values (Bewick and Jonathan, 2005). The comparison of observed to predicted values using the likelihood function is based on the statistic called deviance. The goodness-of-fit process evaluates predictors that are eliminated from the full model, or predictors (and their interactions) that are added to a smaller model.

3.8.1. Likelihood-Ratio Test

The likelihood ratio test statistic (G_2) is the test statistic commonly used for assessing the overall fit of the logistic regression model. The likelihood-ratio test uses the ratio of the maximized value of the likelihood function for the full model (L_1) over the maximized value of the likelihood function for the simpler model (L_0). The likelihood-ratio test statistic is given:

$$G^2 = -2 \log \left(\frac{L_0}{L_1} \right) = -2 [\log(l_0) - \log(l_1)] = -2 \log \left(\frac{l_0}{l_1} \right) \dots \dots \dots (7)$$

It is compared χ^2 with a distribution with 1 degree of freedom. This log transformation of the likelihood functions yields a chi-squared statistic.

3.8.2. The Hosmer and Lemeshow Test Statistic

In order to find the overall goodness of fit, Hosmer and Lemeshaw proposed grouping the values of the estimated probabilities. Hosmer Lemeshaw goodness of fit test divides subjects into deciles based on predicted probabilities and computes a chi square from observed and expected frequencies using these grouping strategies, the Hosmer Lemeshaw goodness of fit statistic, C, is obtained by calculating using the formula:

$$C = \frac{\sum_{k=1}^n \frac{(O_k - n_k \pi_k)^2}{n_k \pi_k (1 - \pi_k)}}{\dots \dots \dots} \dots \dots \dots (8)$$

Where O_k denotes the no of groups n_k is the number of observation in the k th group, O_k is the sum of the y values for the k th group. Hosmer and Lemeshaw (1980) demonstrated that under

the null hypothesis that the fitted logistic regression model is the correct model, the distribution of statistic C is well approximated by the chi squared distribution with $g - 2$ degrees of freedom. This test is more reliable and robust than the traditional chi square test.

3.8.3. The Wald Statistic

The Wald statistic is an alternative test, which is commonly used to test the significance of individual logistic regression coefficients for each independent variable (that is to test the null hypothesis in logistic regression model that a particular logit coefficient is zero). If the Wald test is not significant, then these explanatory variables can be omitted from the model. Wald χ^2 statistic was used to test the significance of individual coefficients in the model and is calculated

$$\text{as: } Z = \frac{\beta_j}{\text{Se}(\beta_j)} \dots \dots \dots (9)$$

Each Wald statistic is compared with a distribution with 1 degree of freedom. Wald statistic is easy to calculate but their reliability is questionable, particularly for small samples.

3.8.4. R^2 Statistic

A number of measures have been proposed in logistic regression as an analog to R^2 in multiple linear regressions. The Cox and Snell measure is based log-likelihoods and considers sample size. The maximum value that the Cox and Snell R^2 attain is less than 1. The Nagelkerke R^2 is an adjusted version of the Cox and Snell R^2 and covers the full range from 0 to 1, it is often preferred. Therefore, in this study R^2 statistic to indicate how useful the explanatory variables are in predicting the response variables were used (Bewick and Jonathan, 2005).

$$R^2_{\text{Logistic}} = \frac{-2\ln_{\text{null}} - 2LLK}{-2LL_{\text{null}}} \dots \dots \dots (10)$$

Where the null model is the logistic model with just the constant and the k model contains all predictors in the model. The Cox and Snell R^2 are computed as follows:

$$\text{Snell and cox pseudo } R^2 = 1 - \left[\frac{-2LL_{\text{null}}}{-2LL_k} \right] / [1 - 2\ln_{\text{null}}]^2_n$$

3.9. Data Processing and Analysis

The sources of data were analyzed using both qualitative and quantitative methods. The statistical package for social sciences (SPSS) version 26 was used for processed and analyzed the

data obtained from questionnaires. Descriptive statistics like frequencies, percentage, Inferential Statistics Based on the nature of the study and objective stated in the introduction part the relevant inferential statistics were used and binary logistic model (to test the significance level of tax incentive and the growth of SMEs) were applied to facilitated analysis and interpretation of the collected data. Qualitative data obtained through interviews were analyzed through qualitative analysis method.

3.10. Ethical consideration of the research

The research was based on certain important ethical principles. These are respect for persons, informed consent, confidentiality, honesty and avoiding plagiarism. The researcher has taken great care not to transgress those ethical issues which are considered as bad, and maintained those ethical issues which are considered as good throughout the research process.

3.11. Operational Definition of terms

Incentive: An incentive is a form of aid, informs of a reduction in or an exemption from someone, a firm, or an industry would normally be legally responsible.

Tax Incentives: These are reliefs granted to taxpayers or industries in form of an offset from the total profit before tax liability is determined. In case of industries and firms, tax incentives are given, inform of tax holidays, which is established by the legislative authorities on such payment of taxes.

Capital gain exemption: is Exemptions from various taxes: are the exemptions from certain taxes, most of the time those collected at the border such as tariffs, excises and VAT on imported inputs.

Income Tax Exemption: Any investors who invest to establish a new enterprise in manufacturing, agro-processing, production of agricultural products and information and communication technology development are entitled to income tax exemptions. Any income tax derived from approved new investment shall be exempted for periods of 1 to 8 years, depending upon the priority area of investment activities and the geographical location of the investment.

Loss carry forward: Business enterprises that suffer losses during the income tax exemption period can carry forward such losses, following the expiry of the exemption period, for half of the tax exemption period.

Investments allowance/Accelerated depreciation: is the deduction of some fraction of an investment from taxable profits (in addition to depreciation).

Special zones: are placed in geographically limited areas where qualified companies can locate and hence benefit from the exemption of various scopes of taxes or administrative requirements.

Tax: is a compulsory levy payable by individual economic units or corporate bodies to government without any direct quid pro quota from the government.

Small Scale Business: It is defined as any business undertaken, owned, managed and controlled by not more than two entrepreneurs, has no more than twenty employees, has no definite organizational structure (i.e. all employees report to the owners) and has relatively small shares of its market.

Business Growth: this refers to the increase in the size, value and financial performance of a firm or company.

CHAPTER FOUR

RUSELTS AND DISCUSSIONS

4.0. Descriptive Statistics

In this chapter, the data collected through different data collection methods and tools are discussed and analyzed carefully in order to show and analysis tax incentive and the growth of SMEs. As the researcher indicated in the methodology in the preceding chapters, Questionnaires was distributed to 288 systematic Sampling chosen from owner, organization. All the survey respondents were located in Ambo town Out of this sample, 230 questionnaires were returned, making a response rate 80%. While the remaining 20% are not complete fill the questionnaires and not responded. The response variable considered in this study was the benefits of tax incentive to the growth of SMES (either Benefits or not benefits).

The main goal of the study is to analysis tax incentive and the growth of SMEs in case of Ambo town. The response variable considered in this study is binary with having two possible expected outcomes coded as 0 form others using tax incentive and 1 for owners not using tax incentive.

The result of Descriptive and Inferential Statistics are summarized and described in this chapter in order to analysis tax incentive and growth of SMEs in the study area. The data were analyzed using SPSS version 26.

4.1. Results of descriptive Statistics

Of the target population, 230 owners and organization was selected in the study. From the graph below it is observed that majority (79.1%) owners decided as tax incentive benefits while only 20.9 % decided as tax incentive not benefits. The descriptive bar graph is given here below (Figure 2).

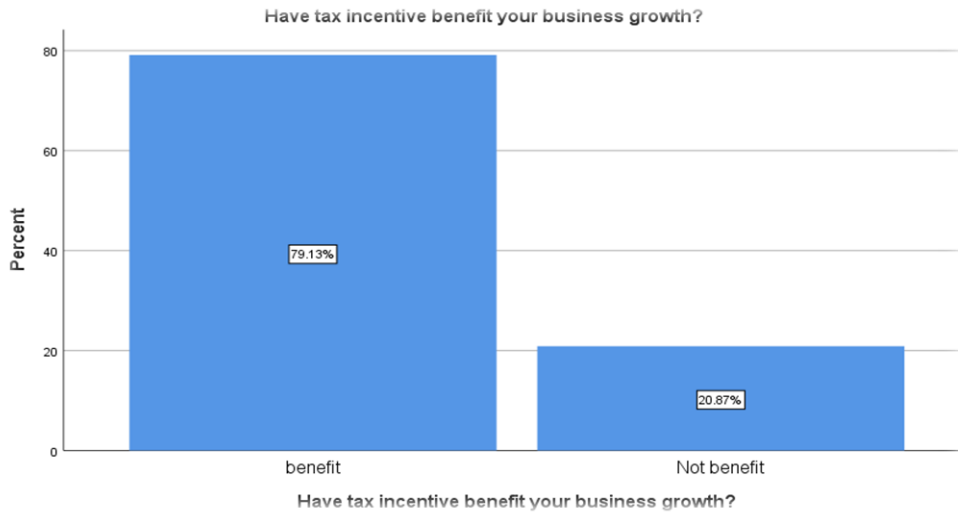


Figure 2: Simple Bar chart of to assess the benefits of tax incentive in Ambo Town. 2020

4.1.1. Presentation and Analysis of data collected from Small and Medium Enterprises owners

Table 4.1: Results of Demographic Characteristics (Ambo Town, 2020)

Explanatory variables	The benefit of tax incentive on SMEs in Ambo town					Total	
	Category	Benefit		Not benefit		Count	%
		Count	%	Count	%		
Sex of the respondents	Male	115	50 %	15	6.52 %	130	56.5%
	Female	67	29.13 %	33	14.35 %	100	43.5%
Age of the respondents	Blow 25	37	16.09%	15	6.52%	52	22.6%
	26-30	62	26.96%	24	10.43%	86	37.4%
	31-40	35	15.22%	4	1.74%	34	17%
	41-50	30	13.04%	3	1.3%	33	14.3%
	Above 50	18	7.83%	2	0.87%	20	8.7%
Education Level	Primary school	37	16.09%	13	5.65%	50	21.7%
	12 th complete	30	13.4%	25	10.8%	55	23.9%
	Diploma	69	30%	8	3.48%	77	33.5%

	BA/BSC	39	16.39%	1	0.43%	40	17.4%
	MA/MSc	2	0.87%	1	0.43%	3	1.3%
	PH.D	5	2.17%	0	0	5	2.2%
Marital status	Married	107	45.62%	22	9.57%	129	56.1%
	Single	65	28.26%	26	11.3%	91	39.6%
	Divorce	10	4.35%	0	0	10	4.3%
When did your SMEs established	Before 1991	29	12.61 %	18	7.83 %	47	20.4 %
	1992- 2000	9	3.91 %	20	8.7 %	29	12.6 %
	2001- 2010	72	31.30 %	4	1.74 %	76	33.0%
	Above 2010	72	31.30 %	6	2.61%	78	33.9 %
Sector of your investment	Manufacturing	42	18.26 %	12	5.22%	54	23.5 %
	Service	54	23.48 %	29	12.61 %	83	36.1 %
	construction	36	15.65 %	1	0.43 %	37	16.1 %
	Urban						
	Agriculture	0	0	0	0	0	0
	Trade	50	21.74 %	6	2.61 %	56	24.3%

Source-data from survey and SPSS

As can be seen in Table 4.1, out of 230 owner and organization considered in the analysis, 20.9% owners have no benefits from tax incentive for the growth of SMEs and 79.1% have benefits of tax incentive for the growth of SMES at the time of data collection. In case of Sex of the respondents 56.5% of sample was male and 43.5% of sample was female. While 56.5 % male and 43.5% female were decided that benefit tax incentive for growth of SMEs. In the case of Age of the respondents on SMEs' show that , 21.34%, 34.78%, 18.7%,15.65% and 9.56% were Blow 25, 26-30, 31-40, 41-50 and Above 50 respectively. From these 16.09%, 26.96%, 15.22%, 13.04% and 7.83% were Blow 25, 26-30, 31-40, 41-50 and above 50 who were benefited for the growth of SMEs respectively. Marital status is also important factor that affect growth of SMEs.

Based on the table 4.1, 56.1%, 39.6% and 4.3% were single, married and divorce of respondents respectively. While 45.62%, 28.26% and 4.35% are single, married and divorced who were benefits for the growth of SMEs respectively. Education Level other important factor for the growth of small and medium enterprises. Based on table 4.1, 21.7%, 23.9%, 33.5%, 17.4%, 1.3% and 2.2% were Primary school, 12th complete, Diploma, BA/BSC, MA/MSc and PH.D respectively. While 16.09%, 13.4%, 30%, 16.39%, 0.87% and 2.17% were Primary school, 12th complete, Diploma, BA/BSC, MA/MSc and PH.D who are benefit for the growth of SMEs respectively. When your SMEs established did was other important factor that affects the growth of small and medium enterprises. According to the table 4.1. 20.4 %, 12.6 %, 33 .0% and 33.9 % were before 1991, 1992-2000, 2001-2010 and after 2010 respectively. From these 12.61 %, 3.91 %, 31.30 % and 31.30 % were before 1991, 1992- 2000, 2001- 2010 and after 2010 who were benefits for the growth of small and medium enterprises.

Finally sector of your investment were important factor for the growth of small and medium enterprises. From the table 4.1, 23.5 %, 36.1 %, 16.1 %, 24.3% were Manufacturing, Service, construction and Trade respectively. While 18.26 %, 23.48 %, 15.65 % and 21.74 % who were benefits for the growth of small and medium enterprises.

4.1.2. Bi variate Analysis

This section reports the association between the outcome variable, Tax incentive and the growth of SMEs and each predictor of the variables. This was done by cross tabulating each predictor variables against the outcome variable and tested using chi-square and likelihood ratio tests. Also, frequency distributions of each category of predictor variables were included.

Bi variate Association of Tax incentive and the growth of SMEs and Explanatory Variables

Pearson's chi-square was used to investigate the association between tax incentive and the growth of SMEs and explanatory variables of demographic, socio-economic and service provision explanatory variables and Spearman's correlation coefficients were used to measure of association between tax incentive and other nominal variables. Table 4.2 indicates that tax incentive like Capital gain exemption; Loss carried forward, Income Tax Exemption, Investment allowance and Special zone were associated with growth of SMEs of respondents at 0.05 levels of significance.

Table 4.2: The Result of test Association between predictors and the growth of small and medium enterprises.

Variables	Cramer's V		Contingency Coefficient		Pearson Chi-Square		
	Value	Sig.	Value	Sig	Value	df	Sig
Capital gain exemption	.654	0.000	.547	0.000	89.091	1	0.000
Tax holiday	.502	0.000	.449	0.000	57.973	1	0.000
Special zone	.533	0.000	.470	0.000	65.309	1	0.000
Investment allowance	.507	0.000	.452	0.000	59.175	1	0.000
Loss Carried forward	.670	0.000	.556	0.000	103.098	1	0.000

Source-data from survey and SPSS

4.1.3. Results of analysis of binary logistic Regression

In this, the result of binary logistic regression and significance and impact of each explanatory variable on the response variable is discussed.

Table 4.3. Omnibus test of model coefficients

Omnibus Tests of Model Coefficients

		Chi-square	Df	Sig.
Step 1	Step	141.659	5	.000
	Block	141.659	5	.000
	Model	141.659	5	.000

The table 4.3 Shows model which includes all predictors. Values shown in the Omnibus Tests of Model Coefficients is given in a Chi-Square of 141.659 which is significant at 0.05. This is a test of the null hypothesis that adding the predictors to the model has not significantly increased our ability to predict benefits of tax incentive made by our subjects. Since our omnibus test is significant at 5% level of significance it can be concluded that adding the predictors to the model have significantly increased our ability to predict tax incentive. Likelihood ratio test is the most common assessment of overall model fit in logistic regression, which is simply the chi-square

difference between the null model (i.e., with the constant only) and the model containing the predictors. Under Model Summary above we see that the -2 Log Likelihood statistics is 141.659. This statistic measures how poorly the model predicts the benefits of tax incentive, the smaller the statistic the better the model.

Table 4.4. Model summary
Model Summary

Step	-2 Log likelihood	Cox & Snell R Square	Nagelkerke R Square
1	93.964 ^a	.460	.717

a. Estimation terminated at iteration number 6 because parameter estimates changed by less than .001

SPSS does not give us this statistic for the model that had only the intercept; we know it to be 235.623 (93.964+ 141.659). Adding the predictors reduced the -2 Log Likelihood statistics by 18235623 – 93.964 = 139.138, which is the χ^2 statistic for omnibus test. The value of Cox & Snell R^2 and Nagelkerke R^2 are good enough. Cox and Snell or Nagelkerke R^2 is an analogous statistic in logistic regression to the coefficient of determination R^2 in linear regression, but not close analog. The model summary provides some approximation of R^2 statistic in logistic regression. Cox and Snell's R^2 attempts to imitate multiple R^2 based on likelihood. In this study Cox and Snell R^2 indicates that 46 % of the variation in the dependent variable benefits of tax incentive was explained by the explanatory variables. Nagelkerke R^2 in model summary table above is 0.717, which indicates that 71.7 % of the variability in the dependent variable benefits of tax incentive was explained by the explanatory variables.

Table 4.5 Hosmer and Lemeshow Test

Hosmer and Lemeshow Test			
Step	Chi-square	Df	Sig.
1	7.037	5	.218

As it is observed from the table 4.5, P-value = 0.218 which is greater than the level of significance $\alpha=0.05$, hence data fits the model well. Therefore our fitted logistic regression model is good fit (**Table 4.6**)

Table 4.6 Contingency Table for Hosmer and Lemeshow Test

		Have tax incentive benefit your business growth? = benefit		Have tax incentive benefit your business growth? = Not benefit		Total
		Observed	Expected	Observed	Expected	
Step 1	1	89	88.229	0	.771	89
	2	18	17.517	0	.483	18
	3	22	21.237	0	.763	22
	4	22	23.699	3	1.301	25
	5	21	19.706	3	4.294	24
	6	7	9.775	16	13.225	23
	7	3	1.837	26	27.163	29

The Hosmer- Lemeshow test is performed by dividing the predicted probabilities into 7 groups based on percentile ranks and then computing a Pearson chi-square that compares the predicted to the observed frequencies. A non significant chi square indicates a good fit to the data and also p value is 0.218 which is significant therefore our fitted logistic regression model is good fit. This means, the null hypothesis that tax incentive was not positive effect or not significant to the growth of SMEs was fail and reject null hypothesis and accept H1.

Observed - This indicates the number of 0's and 1's that are observed in the dependent variable (benefits of tax incentive).

Predicted - These are the predicted values of the dependent variable based on the full logistic regression model. Table 4.7 shows how many cases are correctly predicted (6 cases are observed to be 0 and are correctly predicted to be 0; 26 cases are observed to be 1 and are correctly predicted to be 1) and how many cases are not correctly predicted (196 cases are observed to be 0 but are predicted to be 1; 2 cases are observed to be 1 but are predicted to be 0).

Table 4.7. Classification Table

	Observed		Predicted		
			Have tax incentive benefit your business growth?		Percentage Correct
			Benefit	Not benefit	
Step 1	Have tax incentive benefit	benefit	176	6	96.7
	benefit your business growth?	Not benefit	11	37	77.1
	Overall Percentage				92.6

a. The cut value is .500

Overall Percentage - This gives the overall percent of cases that are correctly predicted by the full model. Overall our predictions were correct 213 (176 + 37) out of 230 times, for an overall success rate of 92.6 %. As we can see, this percentage has increased from 79.1% (Table 4.1) for the null model to 92.6% for the full model (Table 4.7). We could focus on error rates in classification. A false positive would be predicting that the event would occur when, in fact, it did not. Our decision rule predicted the benefits of tax incentives 187 (176 + 11) times. That prediction was wrong 187/202 times, for a false positive rate of $11/202 = 5.88\%$. A false negative would be predicting that the event would not occur when, in fact, it did occur. Our decision rule predicted that not benefits tax incentives are 43 times. Since, most of the covariates are categorical to compute odds ratio we need to have a reference category. Result of binary of logistic the multiple logistic regression coefficients can be estimated using the maximum likelihood estimation method implemented in the SPSS package (Table 4.8). The estimated coefficients and standard errors of the estimates that are used in computing the Wald statistic and the odds ratio ($\text{Exp}(\beta)$) are presented in Table 4.8. The significance of the Wald statistic indicates the importance of the predictor variable in the model.

Table 4.8. Results of the Final binary Logistic Regression Model

Variables	B	S.E.	Wald	Df	Sig.	Exp(β)	95% CI for EXP(β)	
							Lower	Upper
Age Below 25 (Ref.)			10.492	4	.033			
25-35	-0.46	.389	.014	1	.905	.955	.045	2.048
36 -45	-1.266	.601	4.307	1	.038	.282	.085	.932
46 – 55	-1.400	.678	4.256	1	.039	.247	.065	.933
Above 55	-1.294	.806	2.580	1	.108	.247	.056	1.330
Constant	-.903	.306	8.700	1	.119	.405		
Educational level Primary school (Ref.)			25.675	5	.000			
12 th complete	.864	.421	4.207	1	.040	2.372	1.039	5.413
Diploma	-1.109	.493	5.049	1	.025	.330	1.25	.868
BA/BSC	-2.618	1.063	6.066	1	.014	.073	.009	.586
MA/MSc	.353	1.266	.078	1	.781	1.423	.119	17.031
PH.D	-20.157	1797 4.863	.000	1	.999	.000	.000	.
Constant	-1.046	.322	10.525	1	.001	.351		
Marital status married(Ref.)			4.076	2	.130			
Single	.665	.330	4.076	1	.043	.1945	1.02	3.712
Divorce	-19.621	1271 0.133	.000	1	.999	.000	.000	.
Constant	-1.582	.234	45.658	1	.000	.206		

Sector of investment Manufacturing (Ref.)			16.110	3	.001			
Service	.631	.400	2.487	1	.115	1.880	.858	4.118
Construction	-2.331	1.065	4.787	1	.029	.097	.012	.784
Trade	-.868	.542	2.561	1	.110	.420	.145	1.215
Constant	-1.253	.327	14.648	1	.000	.286		
Enterprise established Before 1991(Ref.)			48.775	3	.000			
1992 -2000	-1.275	.501	6.477	1	.011	.0358	.094	1.283
2001 -2010	-2.413	.595	16.457	1	.000	.090	.009	.117
After 2010	-2.008	.520	14.901	1	.000	.134	.004	.093
Constant	-.477	.300	2.526	1	.112	.621		
Who benefited No one (Ref.)			9.375	3	.025			
Foreign investors	.825	.383	4.633	1	.031	.2283	1.07 7	4.840
Domestic investors	-.452	.616	.538	1	.463	.636	.190	2.129
Other investors	-.482	.811	.353	1	.553	.618	.126	3.028
Constant	-1.658	.315	27.717	1	.000	.190		

Ref. = Reference group, Source-data from survey and SPSS

The estimated coefficients and standard errors of the estimates that are used in computing the Wald statistic and the odds ratio ($\text{Exp}(\beta)$) are presented in table 4.8. The significance of the Wald statistic indicates the importance of the predictor variable in the model.

The log odd of respondents who were benefits using tax incentive for the growth of SMEs in the age interval 36 - 45 increased by the amount of 28.2% as compared to the age interval below 15 controlling other variables in the model (Coefficient = -1.266, OR=.282, P= .038, CI= [0.085, 0.932]). The log odd of respondents who were benefits using tax incentive for the growth of SMEs in the age interval 46 -55 is increased by the amount of 24.7 % as compared to the age interval below 15 controlling other variables in the model (Coefficient = -1.400, OR=0.247, P=

.039, CI= [0.065, 0.933]).The log odd of respondents who were benefits using tax incentive for growth of SMEs in the age interval above 55 is increased by the amount of 24.7 % as compared to the age interval below 15 controlling other variable in the model (Coefficient = -1.294, OR=0.247, P= .108, CI= [.056, 1.330]).

Level of education is other covariate which shows significant impact on the growth of SMEs. The log odd who were benefits using tax incentive for the growth of SMEs in the 12th complete increased by 2.372 times as compared to primary school controlling variables in the model (Coefficient = .864, OR=2.372, P= .040, CI= [1.039, 5.413]).The log odd who were benefits using tax incentives for the growth of SMEs in the Diploma increased by 33 % as compared to primary school controlling variables in the model (Coefficient = -1.109, OR=0.330, P= .025, CI= [1.25, 0.868]).The log odd who were benefits using tax incentives for the growth of SMEs in the BA/BSc increased by 7.3 % as compared to primary school controlling variables in the model (Coefficient = -2.618, OR=0.073, P= 0.014, CI= [0.009, 0.586]).

Marital status is also other covariate which shows significant effect on the growth of SMEs. The log odd who were benefits using tax incentive and the growth of SMEs in the single increased by 19.45 % as compared to married controlling variables in the model (Coefficient = .665, OR=0.1945, P=0.043, CI= [1.02, 3.712]).

Sector of investments are other covariate which shows significant impact on the growth of SMEs. The log odd who were benefits using tax incentives for growth of SMEs in the construction sector increased by 9.7 % as compared to manufacturing sector controlling variables (Coefficient = -2.331, OR=0.097, P=0.029, CI= [0.012, 0.784]).

Other important covariate that shows significant effect on the growth of SMEs is enterprises establishment period. The log odd who were benefits using tax incentives and the growth of SMEs in period interval 1992 -2000 E.C increased by 35.8 % as compared to Before 1991 E.C controlling variable (Coefficient = -1.275, OR=0.358, P=0.011, CI= [0.094, 1.283]).The log odd who were benefits using tax incentive for the growth of SMEs 2001 -2010 E.C increased by 9% as compared to before 1991 E.C controlling variables(Coefficient = -2.413, OR=0.090, P=0.000, CI= [0.009, 0.117]). The log odd who were benefits using tax incentive for the growth of SMEs After 2010 E.C increased by 13.4 % as compared to before 1991 E.C controlling variables(Coefficient = -2.008, OR=0.134, P=0.000, CI= [0.004, 0.093]).

Finally the one who benefited by tax incentives are significantly impact on the growth of SMEs. The log odd who benefited by tax incentives are foreigners which increased by 28.3% as compared to no one controlling variable (Coefficient = .825, OR=0.283, P=0.031, CI= [1.077, 4.840]).

4.1.4. Reason SMEs had for not applying tax incentive

This study aimed to address the problem why SMEs are not taking the advantage of tax incentive. With the reference of data collection and analysis many of SMEs have not taking the advantage of tax incentive. Table 4.9, confirms that most of SMEs are not aware of the existence of tax incentive available to them.

Table 4.9 Are you aware of tax incentive offered to SME in Ethiopia?

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	yes	96	41.7	41.7	41.7
	No	134	58.3	58.3	100.0
	Total	230	100.0	100.0	

Source-data from survey and SPSS

The table 4.9.Indicates that only 96 of 230 were aware tax incentive. This means that most of SMEs are not aware of tax incentive. To analysis this issue further across tabulation between the SMEs that had applied for tax incentive and SMEs that were aware of the existence of tax incentive was done.

Table 4.10. Are you aware of tax incentive offered to SME in Ethiopia? * have you applied tax incentives Cross tabulation

		have you applied tax incentives		Total
		Yes	No	
Are you aware of tax incentive offered to SME in Ethiopia?	Yes	47	49	96
	No	51	83	134

Total	98	132	230
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Source-data from survey and SPSS

From table 4.10. It can be seen that out of 96 that aware of tax incentive only 47 decided to apply them. it can be deducted that though entrepreneurs are aware of the existence of these incentive they still decide not to apply for them may be because they do not have confidence in the tax system they assume that there are a lot of bureaucratic procedures involved or tax incentives are only meant of foreign investor not Ethiopians or domestic investors. The table below indicates the SMEs knowledge who benefit from tax incentive.

Table 4.11. Who you know benefiting from tax incentive?

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	No one	75	32.6	32.6	32.6
	Foreigner	99	43.0	43.0	75.7
	domestic investor	37	16.1	16.1	91.7
	Other	19	8.3	8.3	100.0
	Total	230	100.0	100.0	

Source-data from survey and SPSS

The number of SMEs who thought that foreigners were the only beneficiary of tax incentives 99 of 230. This represents 43% of the sample are foreigners. 16.1% of sample mention are beneficiary are domestic investors while 32.6% of sample mention that no one are beneficiary from tax incentives and 8.3 % did not indicate who are beneficiary from tax incentive. Major reason most SMEs are not apply tax incentive was lack of awareness and they do not have confidence in the tax system they assume that there are a lot of bureaucratic procedures involved.

4.1.5. SMES view of Ethiopian tax system

SMEs consider taxes to be one of the constraints of business experiences (WEBS, 2002). One of other objective of the study was to find out whether SMEs consider the tax system to be burdensome. Initially the study looked at how many entrepreneurs had knowledge of tax law in Ethiopia. The results follow.

Table 4.12. Do you understand tax system in Ethiopia?

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Yes	148	64.3	64.3	64.3
	No	82	35.7	35.7	100.0
	Total	230	100.0	100.0	

Source-data from survey and SPSS

From table 4.12. It can be seen that a majority, 64.3% of SMEs owners do understand the tax system of Ethiopia. The study also considered the types of tax paid by SMEs this is always that gained some insight to how many of SMEs actually do pay some sort of tax to the government.

Table 4.13. Which tax rate are you subject to?

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Income tax	59	25.7	25.7	25.7
	Turn over tax	82	35.7	35.7	61.3
	Import and excise tax	20	8.7	8.7	70.0
	VAT	55	23.9	23.9	93.9
	Other	14	6.1	6.1	100.0
	Total	230	100.0	100.0	

Source-data from survey and SPSS

The table 4.13. show suggest that tax commonly paid by SMEs are turn over tax, VAT tax, income tax, import and excise tax and other which account 35.7% ,23.9,25.8.7, and 6.1 respectively.

4.1.6. Qualitative Analysis of Interview with DBA Administrators

Interviews types of questionnaires were administrated to DBA administrators in Ambo towns. These were used to establish the views the administrators had on tax system and the benefits of tax incentive to growth of SMEs.

The mission of the DBAs is to provide business expansion service to SMEs such as training, information, networking, advocacy affordable credit in order for them to contribute to the economic development of the nation. The overall view of the administrators is that the tax system is not efficient and does not exhibit fairness. The tax system was not fair as some of the tax policy implemented such as the increment of the VAT threshold, did not encourage SMEs. They claimed that SMEs in the formal sector were obligated to pay taxes due to the narrow of tax base and large informal sector. This was attributed to the fact that the government is not doing enough to educate people in the informal sector on the benefit of paying tax. On other they do not blame those SMEs that evaded tax because tax rate are too high and consume part of the profits.

The main opinion the administrators had on tax incentive is the most SMEs do not know about their existence. Deliberate measure should to exist educate and sensitized SMEs on tax incentives. They indicated that they response rate of SMEs to the tax incentives has been low because the relevant authorities do not published them.

The administrators also mentioned that foreign investors have been offered better tax incentives and information if efficiently giving out to them. The most SMEs assumed that tax incentives existed only for foreign investors as was stated by one administrator.

In response to the SMEs lack of awareness of tax incentives, DBAs have implemented measured to increase the response rate of SMEs to tax incentives such as applying the government through ERCA to review tax policy and formulate programs to educate SMEs. Other efforts the administrators have made place to stay in submission behalf of the SMEs to budgeting committee. On the overall the tax system was declared to have negative on the growth of SMEs.

Generally in Ambo town there is the obstacle of infrastructure involves, and lack of electricity constitutes one of the constraints to MSME performance. This calls for urgent attention by the government. Corruption comprises of illegal payoffs, government officials extorting money from various businesses, the misuse of government funds that could have been used to develop various sectors are channeled to other directions.

Most of the operators have no desire to create new products and expanding it. They just want to proceed with what they have but not more. The poor implementation of policies including

administration of incentives and measures aimed at facilitating MSMEs growth and development have had accidental effects on the sub Sector. Misallocated skilled manpower Individuals are observed working irrelevant jobs with their profession. For instance, youth graduated in construction observed to be engaged in the manufacturing sector. The one graduated in manufacturing engaged to the sector of construction. This renders them nonproductive and non benefit them act in their skills. Therefore, it is better if they can act as per their skill category and Institutional Coordination Problem and etc.

4.2. Discussion

The study has provided an insight into the tax incentive and the growth of SMEs in Ambo town. According to the results, about 79.1% of the respondents have benefited for the growth of SMEs. Out of the owners who have benefited from tax incentive 50 % and 29.13 % were male and female respectively.

The most of the important variables used by binary logistic are Capital gain exemption; Loss carried forward, Income Tax Exemption, Investment allowance and Special zone. The first factor which affects benefits of tax incentive on the growth of SMEs was Capital gain exemption. Pearson Chi-Square test for custom duty is 0.0000 which is below both 5 & 1 percent level of significance. Pearson's chi-square that was used to investigate the association between tax incentive and the growth of SMEs and explanatory variables and Spearman's correlation coefficients were used to measure of association between tax incentive and other nominal variables show there is positive and strong relationship between custom duty and the growth of SMEs. Similar Studies by Meron, (2016) indicate that Capital gain exemption has strong positive and significant between tax incentive and domestic investment.

The Other important Variable that affect the growth of SMEs was loss carried forward. Pearson Chi-Square test for loss carried forward was 0.000 which is below both 5 & 1 percent level of significance. According to Pearson's chi-square and Spearman's correlation coefficients were used to measure of association between tax incentive and other nominal variables show that there is positive and strong relationship between loss carried forward and the growth of SMEs. Similar study by Daniel (2019) indicates that loss carried forward there was a strong positive and significant relationship between loss carried forward and the growth of small and medium enterprises in Rwanda.

In addition tax holiday was other variables that affect the growth of SMEs. Pearson Chi-Square test for tax holiday (income tax exemption) was 0.000 which is below both 5 & 1 percent level of significance. Pearson's chi-square and Spearman's correlation coefficients were used to measure of association between tax incentive and other nominal variables show that there is positive and strong relationship between tax holiday and the growth of SMEs. Similar study by Ogbonna and Ebimobowei (2012) that tax incentives are positively and significantly related to economic growth and that tax incentive stimulates economic growth.

Investment allowances also other important variable that affect the growth of SMEs. According to the person chi square test for investment allowance was 0.000 which is below both 5 & 1 percent level of significance. Pearson's chi-square and Spearman's correlation coefficients were used to measure of association between tax incentive and other nominal variables show that there is positive and strong relationship between tax holiday and the growth of SMEs.

Finally special zone was other important tax incentive that affects the growth of SMEs. According to the person chi square test for Duty drawback scheme was 0.000 which is below both 5 & 1 percent level of significance. Pearson's chi-square and Spearman's correlation coefficients were used to measure of association between tax incentive and other nominal variables show that there is positive and strong relationship between tax holiday and the growth of SMEs. Therefore the hypotheses H01 to H05 are rejected and accept H1 to H5.

CHAPTER FIVE

CONCLUSION AND RECOMMENDATION

5.1. Conclusions

The study conducted to analysis the benefits of tax incentives on the growth of small and medium enterprises in Ambo town. The paper analyses whether the existing incentives available to the Ethiopian SMEs particularly in Ambo town. The study was conducted using Binary logistic regression model. Control variables included in the model are age of respondent, educational level of respondents, marital status, when did your SMEs established and sector of your investment and who benefited and tax incentive. Besides, Pearson's chi-square, Likelihood-Ratio Test, the Hosmer and Lemeshow Test Statistic, the Wald Statistic, R^2 Statistic and Odds ratio were applied to optimize the utility of the model.

The result of this study shows that SMEs owners who decided that tax incentive were benefits for the growth of SMEs are very high as compared to those who were not benefit it in Ambo town but, they still decide not to apply for them may be because they do not have confidence in the tax system they assume that there are a lot of bureaucratic procedures involved or tax incentives are only meant of foreign investor not Ethiopians or domestic investors. In addition to this, age of respondent, educational level of respondents, sex of the respondents, marital status , when did your SMEs established and sector of your investment are statistically significantly associated with the benefit for the growth of SMEs. Moreover, the result of binary logistic regression model shows that Capital gain exemption; Loss carried forward, Income Tax Exemption, Investment allowance and Special zone on the growth of SMEs were potential explanatory variables that have a significant effect on the benefits of SMEs growth. The overall view of the administrators was that the tax system is not efficient and does not exhibit fairness. The main opinion of the administrators had on tax incentive was Most SMEs do not know about their existence. Generally in Ambo town there was the obstacle of infrastructure involves. Finally District business administration's of Ambo town have Mention various measured to increase the response rate of SMEs on tax incentives, to include in submission on behalf of the

SMEs to budgeting committee, facilitating MSMEs growth and development and Act as per their skill category and Institutional Coordination Problem and etc.

5.2. Recommendation

To the government

Enterprises and policy frame workers should be provided in the collaboration with the sensitized programs to educate SMEs on the provision of tax incentive for SMEs and its growth. Government and tax authorities should carefully consider and re visit the tax incentive policy to determine effective types of tax incentive and its implementation. The current investment act which is geared at foreign direct investment should be consider and adjusted to accumulate and encourage local investment. Government should promote the growth of small and medium enterprises by creating the necessary enabling frameworks and relax the burden of regulating measures and ensure that their efforts are geared towards granting tax incentives to micro, small and medium enterprises.

To small and medium enterprises

Establish channel by which proposition, queries, and complaints may reach relevant authorities such as government and the tax authorities concerned with formulation and implementation of tax incentive. Make effort to join any of the establishment of the institutions and supporting SMEs in order to well inform of the business environment. Develop attitude to merge with other SMEs in order to create stronger and more profitable SMEs. SMEs should be educated on the importance and benefits of keeping books of accounts and paying of tax in order for them to apply for the tax incentive.

To Ambo investment center

The center should ensure that the private sector is well informed on the existence of tax incentive for both local and foreign investors through countries wide sensitization programmers. Appeal to the government to have the tax incentive run on a long term basis and not change as the budget changes yearly so as to increase and ensure their effectiveness.

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APPENDIX I

JIMMA UNIVERSITY

COLLEGE OF BUSINESS AND ECONOMICS

DEPARTMENT OF ACCOUNTING AND FINANCE

Questionnaires for Members/Owners of SMEs Enterprises of Ambo Town.

Dear Respondent: This questionnaire is designed for studying **tax incentive and the growth of small and medium enterprises in** Ambo town. The aim of the study is only for academic purpose and not to abuse or defame the enterprises or **SME** agency. All responses are confidentially kept and used for the stated purpose only. Thus, I would kindly request you to go through all questions and respond the solid reality regarding each issue. Put (√) Mark on the space provided; write your suggestions, reasons and recommendations in the blank space left for you.

Thank you in advance.

A. Personal information

1.1. Age 18- 25 26-30 31-40 41-50 above 50

1.2. Sex M F

1.3. Marital status: Married Single Divorce

1.4. Education level Primary school 12th complete Diploma Degree
(BA/BSC) MA/MSc PhD

1. When did your Small/medium Enterprise established? (DD/MM/YY) _____

2. Sector of your investment (Manufacturing, Trade, Agriculture, etc) _____

B. Ethiopian tax system

1. Do you understand tax system in Ethiopia? 1. Yes 2. No

2. Which tax rate are you subject to?

1. Corporate tax
2. Vat
3. Import and excise tax
4. Presumptive tax
5. Other -----

3. How long does it take the Ethiopian revenue authority to alert you of your tax liability?

1. 1-3 weeks
2. 4-8 weeks
3. 9-12 weeks
4. Over 12 weeks

C. Tax incentive

1. Are you aware of tax incentive offered to SME in Ethiopia?

Yes no

2. Have tax incentive affect your business growth?

Yes no

3. What impact of tax incentive on your business profit?

Increase 0-20%

Increase 21-50%

Increase 50-100%

No impact

4. Have tax incentive enable you to expand your business?

Yes no

5. How do you investigate your growth as you obtain the Capital gain exemption?

Benefit not benefit

6. How do you investigate your growth as you obtain the Income Tax Exemption?

Benefit not benefit

7. How do you investigate your growth as you obtain the Loss carried forward?

Benefit not benefit

8. How do you investigate your growth as you obtain the investment allowance?

Benefit not benefit

9. How do you investigate your growth as you obtain the special zone?

Benefit not benefit

10. Mention who you know is benefiting from tax incentive. -----

Appendix II

QUESTIONNAIRE TO BE FILLED BY SME'S DEVELOPMENTAL ORGANIZATION

The following questionnaire is part of a survey being conducted on Assessing the performance of Small and Medium Enterprises in Ambo town:. This information is purely for survey purpose and therefore its confidentiality is highly guaranteed. You are therefore kindly requested to provide accurate answer to the ensuring questions. Your co-operation and support will be appreciated.

SECTION A

Name of the organization-----

Position -----

Mission-----

1. What are you view on Ethiopia tax system?

2. What is your opinion on tax incentive offered to SMEs in Ambo town?

3. Do you think they have an effect on the growth of SMEs in Ambo town?

4. Have you seen an increasing in investment or establishment of SMEs in favor sector of the economy due to tax incentive?

5. Why do you think the response rate of SMEs to tax incentive is low in Ambo town?

6. What you doing about it?

7. List the Major challenges that face SME's in Ambo town?

8. Why do you see them as challenge?

9. In your view, how can these challenges be solved?

Appendix I
JIMMA UNIVERSITY
COLLEGE OF BUSINESS AND ECONOMICS
DEPARTMENT OF ACCOUNTING AND FINANCE

Gaafannoo miseensota/abbootii Qabeenyaa waldaalee IMX Bulchiinsa magaalaa

Ambo tiif dhihaate.

Kabajamtoota deebii kennitootaa; Gaafannoon Kun Mata duree **gibira onnachiftuu fi guddinaa IMX maagalaa Amboo** jedhu irratti qorannoo gaggeessuuf kan qophaahedha. Kaayyoon qorannoo kanaas waldaale IMXs ta'e waajjiraalee ol'aanoo isaaniin to'atan kallattii hin malleen ibsuuf osoo hin taane rakkoolee guddina isaanii qorannoo qabatamaadhaan adda baasuun yaada furmaataa kaa'uu qofadha .Deebiin isin kennitan qaama kamiifuu haala kamiin iyyuu darbee hin kennamu; dhimma qorannoo kanaan ala tajaajila biroofis hin oolu. Kanaafuu xiyyeeffannoo guddaa kennuun deebii sirrii fi dhugaa ta'e akka nuuf kennitan kabajaan isin gaafanna . Deebii keessan saanduqa gaaffii fuula dura taa'e keessa mallattoo (√) kaa'uu fi Iddoowwan duwwaa kennaman keessatti yaada keessan barreeffamaan ibsuun kennaa.

Deeggarsa nuuf gootaniif dursinee isin galateeffanna.

A. Haala dhuunfaa keessanii.

1.1 **Umurii:** 18- 25 26-30 31-40 41-50 50 ol

1.2. **Korniyaa:** Dhiira Dubartii

1.3. **Haala gaa'elaa:** Kan fuudhe/heerumte Kan hin fuune/herumne kan hiike/hiikte

1.4.**Sadarkaa Barumsaa** Sad, 1ffaa 12ffaa kan xumure Diploomaa

Digirii 1ffaa (BA/BSC) Digirii 2ffaa MA/MSC PhD

Kan biraa (ibsaa) _____

1. Waldaan keessan Bara kam hundaaha? _____
2. Sektarri waldaa keessanii isa kami (Manufacturing, Daldala , Qonnaa, kkf) _____

B. Adeemsa Gibira Ithoopiyaa

3. Adeemsa gibira ithopiyaa hubatta? 1. Eeyeen 2. Lakkii

4. Gosa gibiraa kamiti dhimma baataa/fayyadamta?

1. Corporate tax

2. Vat

3. Import and excise tax

4. Presumptive tax

5. Kan biroo -----

5. ERAn liqii ofirraa baasus yeroo eeannoo hangami siif kenna

1. 1-3 torbee

2. 4-8 torbee

3. 9-12 torbee

4. Over 12 torbee

C. Gibiraa onnachiiftuu

1. Akkaa gibirri onnachiiftuun IMX Itoopiyaaf kenamuu beekta?

Eeyyeen

lakkii

2. Gibirrii onnachiiftuun guddinaa bizinasiif gahee qaba?

Eeyyeen

lakkii

3. Dhiibbaan gibirrii onnachiiftuun bu'aa bizinasii keesani irrattii qabu hangami?

1. 0-20% dabaluu

2. 21-50% dabaluu

3. 50-100% dabaluu

4. Dhiibbaa hin qabu

4. Gibirrii onnachiiftuun bizinaasii keetiif agarsiistuudha?

Eeyyeen

lakkii

5. Gosa investmentii ykn bakka inveestimentii (tax holiday) irratti hundaa'un gibiraa irraa bilisa ta'uun guddina sector keesanif akkamit laalta?

Ni fayyada hin fayyadu

6. Kasarra si muudate dandamaachuuf gibirra irraa bilisaa ta'uun guddina sector keesanif akkamit laalta?

Ni fayyada hin fayyadu

7. Mi'aa dheedhii alaatti erguuf alaa galchuun ykn biyyaa keessa bituun gibira irraa bilisaa ta'uun guddina sector keesanif akkamit laalta?

Ni fayyada hin fayyadu

8. Investmeentii biyyaa keessaa jajjabeesuuf kappitala ykn information alaa galchuun gibirra bilisaa tahuun guddina sector keesanif akkamit laalta?

Ni fayyada hin fayyadu

9. Haala bakka hojjiikeerratti hunaa'uun gibira ykn dirqamaa qabdurra bilisaa yoo tatuu guddina sector keesanif akkamit laalta?

Ni fayyada hin fayyadu

10. Gibiraa onaachiftuun kun kan fayyadee jettee beektuu ibsimee?

APPENDIX II

GAAFANNOO WAAJJIRAALEE OL'AANNOO IMXF MAGAALAA AMBOOF DHIYAATE

Kabajamtoota deebii kennitootaa;

Gafaannoon kun mata duree gibiraa onnachiftuu fi guddinaa IMX magaalaa Amboo irraatti qorannoo gaggeessuuf kan qophaahedha. Kaayyoon qorannoo kanaas waldaale IMXs ta'e waajjiraaalee ol'aannoo isaaniin to'atan kallattii hin malleen ibsuuf osoo hin taane rakkoolee guddina isaanii qorannoo qabatamaadhaan adda baasuun yaada furmaataa kaa'uu qofadha .Deebiin isin kennitan qaama kamiifuu haala kamiin iyyuu darbee hin kennamu; dhimma qorannoo kanaan ala tajaajila biroofis hin oolu. Kanaafuu xiyyeeffannoo guddaa kennuun deebii sirrii fi dhugaa ta'e akka nuuf kennitan kabajaan isin gaafanna . Deebii keessan saanduqa gaaffii fuula dura taa'e keessa mallattoo ($\sqrt{\quad}$) kaa'uu fi Iddoowwan duwwaa kennaman keessatti yaada keessan barreeffamaan ibsuun kennaa.

Deeggarsa nuuf gootaniif dursinee isin galateeffanna.

SECTION A

Maqaa dhabbataa keessani -----

Gahee hojii-----

Ergama -----

1. Adeemsa gibira ithoophiyaa irraa maaltu mul'ata?

2. Gibira onnachiftuu IMX magaalaa Amboof kennemuf ilaalcha maali qabda?

3. Guddina IMX Magaalaa Ambootiif gahee qaba jettee yaada?

4. Sababa gibira onnachiftuutiin IMX hundeeffame fi investmentiin simboon isa dabalee argitee beekta?

5. IMXn Magaalaa Amboo, deebi isaan gibira onnaachiftuuf qaban Sababni dhibbentaan xiqqoo ta'eef maali jettee yaada?

6. Kanarratti maal hojachuu qabna jetta?

7. Rakkoon IMX magaalaa Ambo gurguddoo maalidha?

8. Maalif akkaa rakkootti ilaaltee?

9. Akkaa yadaa keetti rakkoon Kun akkamiti furmataa argata?
