The Role of Small and Medium Enterprises in Job Creation: A Case Study of Karachi, Hyderabad and Sukkur

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Abstract

Small and Medium Enterprises (SMEs) play a vital role in Pakistan's economic development, particularly in job creation and poverty alleviation. This research paper examines the impact of SMEs on employment generation in three major cities of Sindh province: Karachi, Hyderabad, and Sukkur. Utilizing both quantitative and qualitative methodologies including surveys and interviews with SME owners, employees, and government officials the study offers a comprehensive analysis of the contribution of SMEs to local economies. The research findings given in this Paper reveal that the Small and medium enterprise played a due role to reduce poverty in the country through SMEs because in every SMEs 110-15 people were working for their livelihood. The analysis also demonstrated that through SMEs employment dramatically improved in the study region. The people income, saving and expenditure increased significantly, due to this reason expend more for their health. The findings reveal that while SMEs significantly contribute to employment, they also face numerous challenges such as limited access to finance, regulatory constraints, and inadequate infrastructure. Despite these obstacles, SMEs demonstrate considerable resilience and possess strong potential for future growth.

Keywords: Small and Medium Enterprises, Job Creation, Pakistan, Karachi, Hyderabad, Sukkur, Employment, Economic Development.

Introduction

Small and Medium Enterprises (SMEs) are widely recognized as the backbone of developing economies. In Pakistan, SMEs comprise over 90% of all business enterprises, contributing significantly to the national GDP and employment generation. This study focuses on three key cities within the Sindh province i.e Karachi**,** Hyderabad**,** and Sukkur each representing diverse economic and industrial landscapes.

SMEs play a pivotal role in creating employment and generating income, particularly for low-income groups. These small-scale enterprises are often more efficient in terms of resource utilization and adaptability, and they foster an entrepreneurial culture that strengthens the economy, especially during times of economic crises marked by low per capita income, poverty, and high unemployment. In many developing countries, SMEs serve as a critical source of livelihood for urban populations and are essential to national development strategies.

Definitions of micro and small business enterprises vary globally. According to Carpenter (2003), the classification criteria may include a combination of factors such as the number of employees,

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financial strength, sales value, relative size, initial capital investment, and industry type. For instance, the European Commission uses three key indicators to define enterprise size: staff headcount, annual turnover, and balance sheet total. Micro-enterprises are those employing fewer than 10 people with an annual turnover or balance sheet total not exceeding €2 million. Small enterprises employ fewer than 50 people, with turnover or balance sheet totals below €10 million (Kushnir et al., 2010).

Developing countries face a multitude of socio-economic challenges, including extreme poverty, high unemployment, low per capita income, and inequitable income distribution. Governments are, therefore, increasingly relying on SMEs as a strategic tool to address these challenges. One key approach to fostering inclusive economic development is the promotion and support of SMEs, which can absorb a significant portion of the labor force and stimulate wealth creation.

Micro and small-scale enterprises are widely regarded as critical engines for socio-economic development in both developed and developing nations. Their contribution is particularly significant in the context of developing countries, where unemployment and poverty levels are high. Multiple studies have emphasized the role of SMEs in employment creation and economic growth, highlighting their importance in achieving global development objectives such as the Millennium Development Goals (MDGs). Chief among these goals is the reduction of poverty through sustainable employment, wealth generation, and improved living standards.

This literature review draws on national and international research to frame the context of the present study. The primary objective is to analyze the role of SMEs in job creation while exploring the regional differences in the challenges and opportunities faced by these enterprises in Karachi, Hyderabad, and Sukkur.

Objectives

Based on the general objective, the specific objectives are:

- To examine the contribution of Small and Medium Enterprises (SMEs) to employment creation and the sustainability of such employment in the study area.
- To evaluate the role of SMEs in income generation for individuals and households within the study area.
- To identify the key opportunities (prospects) and major challenges (constraints) facing SMEs in the study area.

Literature Review

Several studies underscore the pivotal role of small and medium enterprises (SMEs) in economic development. According to the Small and Medium Enterprises Development Authority (SMEDA), SMEs contribute approximately 40% to Pakistan’s GDP and employ nearly 80% of the non-agricultural labor force. Despite their significance, the literature highlights persistent systemic barriers that hinder their growth and sustainability. These include limited access to capital, insufficient policy support, inadequate infrastructure, and a lack of training and development programs. Addressing these challenges is essential to unlocking the full potential of SMEs and fostering inclusive economic growth.

The Role of Small and Medium Enterprises in Economic Growth

In many developing countries, there has been a significant shift in focus toward the development of micro and small-scale enterprises. This shift stems from the crucial role these enterprises play in economic development, as they often align closely with the socio-economic realities of these nations. Small and Medium Enterprises (SMEs) due to their relatively small size, strategic locations, moderate capital requirements, and substantial employment-generating capacity—have demonstrated a powerful and dynamic impact in fostering rapid economic growth (FDRE, MoTI, 1997).

It is widely acknowledged that in most developing countries, a large portion of the population is engaged in micro and small-scale enterprise activities, which are distributed across both urban and rural areas. This widespread presence makes SMEs a vital component of these countries' economic fabric. Unlike larger firms, SMEs tend to have more flexible organizational structures, allowing them to withstand adverse economic conditions and survive downturns where many larger enterprises might fail (Aryeetey & Ahene, 2004, p. 3).

Furthermore, the inherent flexibility of SMEs enables them to adapt quickly to changing customer demands and market conditions, providing a competitive advantage in dynamic environments (Kayanula & Quartey, 2000, p. 10). This adaptability ensures that the economic needs of a broad base of the population can be met more effectively through the development and support of the SME sector.

In summary, the role of SMEs extends beyond economic activity; they serve as critical engines for employment generation, poverty reduction, and inclusive growth in developing countries. Their ability to operate in diverse locations and respond to market needs positions them as essential drivers of sustainable economic development.

Employment Generation

Available evidence suggests that micro enterprises typically do not exhibit significant employment growth (Mead & Liedholm, 2000). Although small firms are characterized by high rates of both job creation and job destruction, job losses during economic downturns tend to be lower in small enterprises than in larger ones, possibly due to greater wage flexibility in smaller firms (Snodgrass & Biggs, 1998). In contrast, large firms generally offer superior employment conditions, including better wages, fringe benefits, skill development opportunities, favorable working environments, and greater job security (Snodgrass & Biggs, 1998).

A study by Liedholm (2002) highlights that the failure rate of SMEs in developing countries is highest during their initial years. For example, in Kenya, Botswana, Swaziland, and Zimbabwe, more than 50% of small firms shut down within three years of starting operations. Furthermore, Liedholm (2002) notes that because small firms exhibit higher gross job creation and destruction rates compared to large enterprises, they may offer less job stability. In the United States, job durability for both new and existing roles tends to improve with increasing firm size (Ibid).

Income

While there are many exceptions to this general trend, evidence suggests that larger employers typically offer better jobs, characterized by higher wages, more generous fringe benefits, improved working conditions, greater opportunities for skill development, and enhanced job security. In low-income countries, small enterprises often have significantly lower productivity than larger firms, resulting in lower wages and fewer non-wage benefits. However, some studies indicate that as countries undergo industrialization and economic development, the disparities in labor productivity and wage levels between small and large firms tend to diminish (Snodgrass & Biggs, 1998).

Employment Opportunities

Micro and small enterprises (MSEs) inherently possess the capacity to create substantial employment opportunities for unskilled and semi-skilled labor, which are abundantly available in most developing countries. Studies conducted in five African countries—Botswana, Kenya, Malawi, Swaziland, and Zimbabwe—indicate that MSEs generate nearly twice the level of employment compared to registered large-scale enterprises and the public sector.

Similarly, in many Latin American countries, MSEs employ over half of the working population. An ILO (2005) study examining firms with fewer than 10 workers found that they accounted for 58% of total employment in Paraguay, 54% in Mexico, and 53% in Bolivia. By increasing employment opportunities for the active labor force, MSEs provide livelihoods to a significant portion of the population in both developing and developed countries.

All small enterprises exhibit a remarkable capacity to absorb labor, thus helping to alleviate unemployment. Consequently, technologies that are more labor-intensive and require less capital investment should be favored, especially in labor-rich economies. Given their labor-intensive and capital-saving nature, MSEs can play a critical role in addressing many of the socio-economic challenges facing countries like Ethiopia. Moreover, MSEs typically employ workers with limited formal training (Andualem, 2004), further highlighting their importance in inclusive economic development.

Contribution to the economy and income source for the poor

The contribution of micro and small enterprises (MSEs) varies significantly across countries. In Pakistan, for example, MSEs contribute approximately 31% to the economy. Many policymakers view MSE development as a strategic approach to increasing the incomes of the poor. The economic impact of MSEs is reflected in their contribution to output, employment, income, investment, exports, and other key economic indicators. Due to their size, geographic spread, and capacity to generate employment, MSEs serve as vital drivers of growth, job creation, social progress, and overall economic development.

In many developing countries, the smallest firms also function as a crucial social safety net. They offer temporary employment to vulnerable populations and provide a means of sustenance for their owners and employees (Esubalew, 2006). In Ethiopia, where capital scarcity, high unemployment, and low levels of industrialization and productivity persist, micro, small, and medium-sized enterprises play a critical role in the national economy. They contribute significantly to GDP and are recognized for fostering the growth of the small-scale industrial sub-sector. According to Adil (2007), MSEs also promote equitable income distribution, stimulate competition, exploit niche markets, and drive productivity, technological advancement, and economic development.

Constraints in the development and promotion of SMEs

Various studies have identified several major constraints affecting Micro and Small Enterprises (MSEs), including policy and institutional bottlenecks, limited access to capital, shortages of human and material resources, and inadequate equipment and technology. The development of the sector is further hindered by these diverse constraints. The small size and structural diversity of MSEs also contribute to the wide range of challenges they face, which significantly vary across countries and even among communities within the same country.

These problems are influenced by differing levels of socio-economic development and socio-cultural contexts. Consequently, the nature and severity of the challenges are not uniform but are shaped by each country's macroeconomic policies and the specific strategies and programs implemented to support the sector (Dagnaw, 2009).

Methodology

The research employs a mixed-methods approach, combining both primary and secondary data collection. Primary data were collected through structured questionnaires and in-depth interviews with 804 SME owners, of whom 566 (70%) are facilitators and 238 (30%) are non-facilitators, across Karachi, Hyderabad, and Sukkur. Secondary data sources include reports from SMEDA, the Pakistan Bureau of Statistics, and World Bank publications. The collected data were analyzed using statistical tools alongside thematic content analysis.

Result and Discussion

Karachi is the economic hub of Pakistan, Karachi hosts a large number of SMEs across various sectors such as manufacturing, retail, and services. The study found that SMEs in Karachi contribute significantly to job creation, especially for semi-skilled and unskilled labor. However, issues like urban congestion and inconsistent power supply affect productivity.

Hyderabad SMEs in Hyderabad are primarily engaged in textile, handicrafts, and food processing. The city benefits from a skilled labor force and historical industrial base. However, outdated technology and limited innovation hinder growth. Despite this, SMEs are vital in absorbing the local labor force.

Sukkur in Sukkur, SMEs are smaller in scale but crucial for the regional economy. The enterprises are mainly in agriculture-based processing and small retail businesses. The major challenges here include lack of access to markets, inadequate financial services, and insufficient training facilities.

Socioeconomic characteristics of the respondents

This section covers the demographic and socio-economic background of the respondents. It includes general information about the facilitators' age, marital status, and education, duration of association with SMEDA, and types of businesses.

Table 1: Profile of the Respondent (Facilitators& Non- facilitators)

Status of Respondent	No. of SME holders	Percentage
Facilitators	566	70%
Non-Facilitators	238	30%
Total	**804**	**100%**

Furthermore, Table 1 presents the distribution of facilitators and non-facilitators in the study area. Out of a total of 804 respondents, 70% (566 individuals) are facilitators (beneficiaries), while the remaining 30% (238 individuals) are non-facilitators."

Table 2: Gender status of the Respondent (Facilitators& Non- facilitators)

Status of Respondent	Facilitators	Percentage	Non- facilitators	Percentage
Gender	Frequency	%	Frequency	%
Female	355	62.7	152	63.9
Male	211	37.3	86	36.1
Total	**566**	**100**	**238**	**100**

Similarly, Table 2 illustrates the distribution of respondents by gender. It is evident from the table that in both the treatment and control groups, the majority of respondents are female, accounting for 62.7% and 63.9% of the total, respectively. Male respondents constitute 37.3% in the treatment group and 36.1% in the control group."

Table 3: Age of the Respondent (Facilitators& Non- facilitators)

Age	Frequency (Facilitators	Percentage	Frequency (Non-Facilitators)	Percentage
18-24	42	7.42	21	9
21-31	98	17.31	53	22.11
32-38	194	34.27	89	37.39
39-45	124	22	42	17.64
46 and above	108	19	33	13.86
Total	**566**	**100**	**238**	**100**

Table 3 presents the age distribution of respondents. The majority of respondents in both the treatment and control groups fall within the 32–38 age range, accounting for 33.81% and 37.39% respectively."

Table 4: Education Level of Respondent (Facilitators& Non- facilitators)

Education Level	**Frequency (Facilitators**	**Percentage**	**Frequency (Non-Facilitators)**	**Percentage**
No School	389	68.73	171	71.82
Middle	67	11.84	21	8.82
Matric	48	8.48	25	10.50
Inter	27	4.77	13	5.46
Others	35	6.18	8	3.4
Total	**566**	**100**	**238**	**100**

Although the majority of respondents had attended some form of education—73.33% in the treatment group and 70.17% in the control group—most were still functionally illiterate, with 68.73% in the treatment group and 71.82% in the control group unable to read or write."

Table 5: Marital status of the Respondent (Facilitators& Non- facilitators)

Marital Status	**Frequency (Facilitators**	**Percentage**	**Frequency (Non-Facilitators)**	**Percentage**
Married	492	86.9	198	83.2
Single	50	9.8	27	11.34
Divorce	8	1.1	5	2.1
Widow	16	2.2	8	3.36
Total	**566**	**100**	**238**	**100**

Similarly, with respect to marital status, a large proportion of respondents in both the treatment group and the control group are married—86.9% and 85.5%, respectively. Fewer respondents are either divorced or widowed."

Table 6: of Households (Facilitators& Non- facilitators)

House Hold Members	**Frequency (Facilitators**	**Percentage**	**Frequency (Non-Facilitators)**	**Percentage**
5-7	160	28.27	53	22.28
8-10	296	52.30	147	61.76
11 above	110	19.43	38	15.96
Total	**566**	**100**	**238**	**100**

Similarly, among both facilitators and non-facilitators, 51.02% of families in the treatment group and 61.76% in the control group have between eight and ten members."

Table 7: Employment Generation of the Respondent

Status of Respondent	Borrower	Percentage	Non Borrower	Percentage
2-5 worker	356	62.8	166	69.7
5-10 worker	165	29.1	59	24.7
More then 10	45	7.9	13	5.4
Owner ship of the Business				
Own Business	549	96.9	227	95.3
Rented Business	16	3.1	11	4.6

Employment generation is a key objective of small and medium enterprises (SMEs), aimed at promoting the utilization of job opportunities among beneficiaries. According to Masumbuko et al. (2014), the establishment of new ventures contributes to employment creation through better allocation of human resources, reduced transaction costs, and the cultivation of a savings culture among clients. Overall, individuals who are able to save part of their income are generally more resilient to income shocks and other economic vulnerabilities. Moreover, they are better positioned to invest in income-generating sectors, thereby reducing their likelihood of unemployment.

In the study area, most participants—beneficiaries of the Small and Medium Enterprises Development Authority (SMEDA)—were found to have generated opportunities in both monetary and non-monetary forms. A significant reason for non-monetary savings was the lack of institutions offering formal savings services, which compelled participants to rely on durable assets and livestock as alternative forms of saving. Additionally, the loan amounts provided were often too small to enable substantial savings, limiting clients to minimal financial reserves.

Table 8: Monthly Consumption of Household

Dependent Variable : Monthly consumption of House hold					
Variables	Std. Error	Beta	T	Sig	VIF
Constant	712.075		.55	.557	
Employees	178.787	.038	.610	.542	3.538
Supervision	4.260	.0.09	.148	.883	3.693
Monthly income	0.16	.354	6.219	.000	3.011
Age	5.034	.0140	3.689	.000	1.333
Education	6.645	.059	1.697	.090	1.123
Family Size	22.826	.034	.968	.333	1.159
Technical Support	117.976	.042	1.019	.309	1.591

Savings	130.524	.027	.768	.443	1.109
Health fasc:	312.066	.029	.885	.377	1.009
Training	135.670	.110	2.307	.021	2.095
F=15.524 0(0.0000)					
Adjusted R Square =.135					
N=804					
Breusch-Pagan and Koenker test statistics and sig-values					
	LM		Sig		
BP	185.468		.000		
Koenker	82.886		.000		

In Table 8, the researcher examines the effect of small and medium enterprises (SMEs) on employment generation among the beneficiaries of SMEDA. The coefficient of determination (adjusted R-square) indicates that 13.5% of the variation in household savings is explained by the independent variables. According to Gujarati and Porter (2005), an R-square value between 10% and 90% is considered acceptable for cross-sectional data. The results indicate that only age, income, and access to health facilities have a statistically significant impact, while other variables such as education, training, family size, supervision, and savings are not significantly associated with employment generation.

The positive coefficients suggest that as the values of the explanatory variables increase, so does the dependent variable, indicating a growth in household savings. Table 8 presents the standardized beta coefficients for comparison across variables. Among the significant predictors, income has the highest impact on employment opportunities ($\beta = 0.354$), while age has the smallest impact ($\beta = 0.140$), suggesting that savings tend to increase with age.

The hypothesis regarding employment generation is statistically supported, as the dummy variable for employment status indicates improved opportunities for beneficiaries compared to non-beneficiaries. Consequently, the null hypothesis related to employment generation is accepted. This leads to the conclusion that SMEs have a significant effect on clients' monthly savings. Furthermore, multi collinearity is not a concern, as all Variance Inflation Factor (VIF) values are below the threshold of 10 (Vatcheva et al., 2016). However, the presence of heteroscedasticity is confirmed, as indicated by significant Breusch-Pagan and Koenker test results at the 0.05 level.

Challenges Facing SMEs

- Limited access to finance and credit
- Bureaucratic and regulatory complexities
- Lack of technological infrastructure
- Inadequate business development services
- Shortage of skilled labor

Conclusion

SMEs play a significant role in job creation in Pakistan, particularly in Karachi, Hyderabad, and Sukkur. Despite numerous challenges, they have demonstrated resilience and potential for growth. Targeted policy interventions and improved infrastructure can enhance their contribution to employment and economic development. This study underscores the need for a supportive ecosystem to enable SMEs to thrive and further contribute to the socio-economic development of Pakistan.

Policy Recommendations

- Improve access to credit through microfinance and SME-targeted lending programs
- Simplify regulatory and taxation processes
- Establish SME development centers in each city
- Promote public-private partnerships for skills training
- Enhance infrastructure, especially in less developed cities like Sukkur

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