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Firm Growth in Zambia

Daniel Gurara

SIP/2025/126

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Firm Growth in Zambia
Prepared by Daniel Gurara

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ABSTRACT: Firm growth in Zambia remains subdued, undermining the country's potential to create jobs, raise productivity, and drive economic transformation. Formal businesses face persistent barriers—most notably limited access to finance, unreliable electricity supply, and competition from a large informal sector. Using data from the World Bank Enterprise Surveys and cross-country entrepreneurship benchmarks, this paper examines how these constraints affect firm performance and contribute to Zambia's low rate of new business formation. Empirical analysis indicates that firms with access to credit and stable infrastructure grow significantly faster, while those facing severe constraints underperform. Moreover, Zambia's rate of new business entry remains low compared to aspirational peers, reflecting deeper regulatory and financial constraints. Removing key barriers to firm growth is essential not only to scale up existing businesses, but also to support structural transformation by facilitating the shift of labor into more productive, formal sector employment.

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SELECTED ISSUES PAPERS

Firm Growth in Zambia

The Republic of Zambia

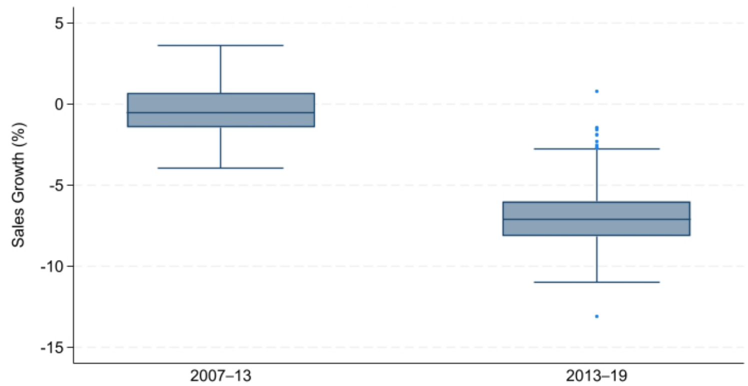
Prepared by Daniel Gurara[1]

[1] The author would like to thank Steven Qi (AFR) for his helpful assistance. The
views expressed in the paper are those of the author and do not necessarily represent the views of the IMF, its Executive Board, or IMF management.

FIRM GROWTH IN ZAMBIA

Firm growth in Zambia remains subdued, undermining the country's potential to create jobs, raise productivity, and drive economic transformation. Formal businesses face persistent barriers—most notably limited access to finance, unreliable electricity supply, and competition from a large informal sector. Using data from the World Bank Enterprise Surveys and cross-country entrepreneurship benchmarks, this paper examines how these constraints affect firm performance and contribute to Zambia's low rate of new business formation. Empirical analysis indicates that firms with access to credit and stable infrastructure grow significantly faster, while those facing severe constraints underperform. Moreover, Zambia's rate of new business entry remains low compared to aspirational peers, reflecting deeper regulatory and financial constraints. Removing key barriers to firm growth is essential not only to scale up existing businesses, but also to support structural transformation by facilitating the shift of labor into more productive, formal sector employment.

Text Figure 1. Zambia: Real Sales Growth: 2007-13 and 2013-19



Source: Computed based on World Bank Enterprise Survey Data 2007, 2013, 2019

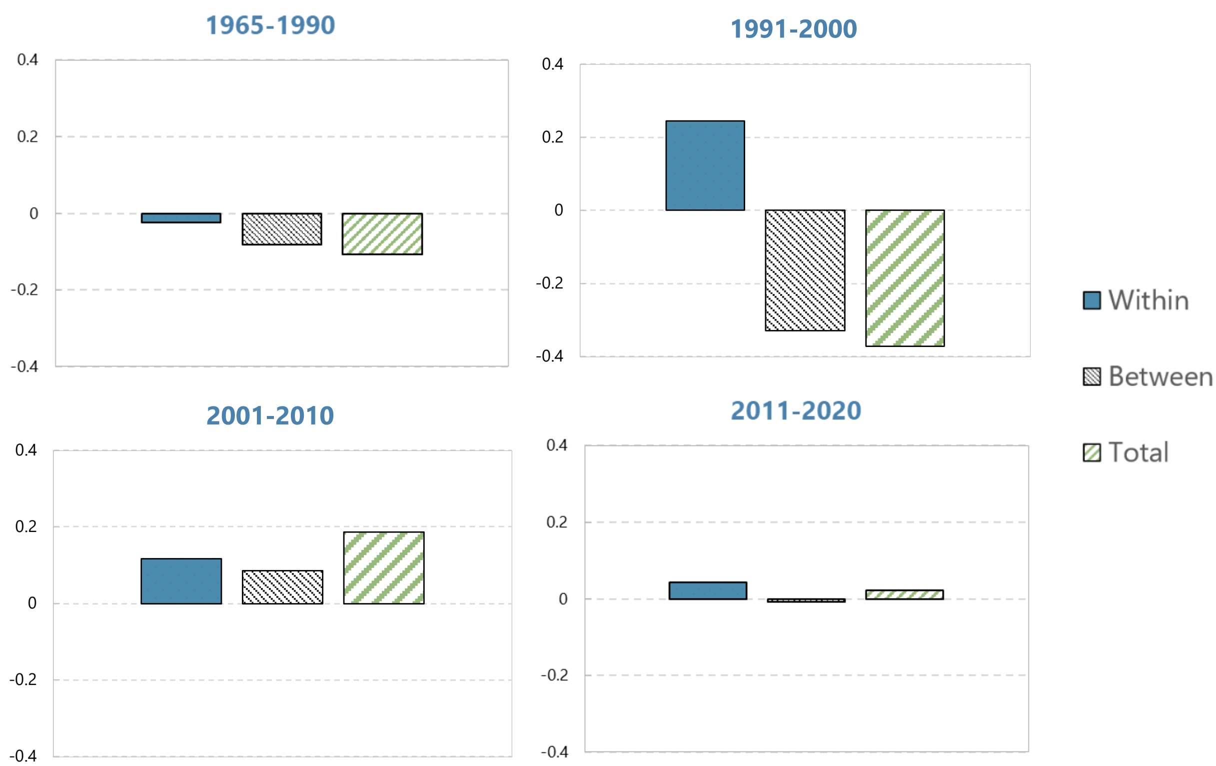
A. Introduction

1. Firm growth in Zambia has been slow, limiting job creation and productivity gains. Despite episodes of macroeconomic expansion—particularly during the 2000s commodity boom—many formal businesses have not grown meaningfully in real terms. Enterprise Survey data show stagnant median sales growth during 2007–13, followed by widespread declines in 2013–19. The distribution of firm outcomes has deteriorated over time, with more businesses reporting declining sales and fewer experiencing growth (see Text Figure). This deterioration in firm-level performance has weakened the private sector's role in driving employment and inclusive growth.

2. The sluggish expansion of firms has constrained Zambia's structural transformation. Structural transformation—the shift of labor from low-productivity activities, such as subsistence agriculture and informal trade, to more productive sectors like manufacturing and services—has progressed slowly (Figure 1). Much of the labor force remains in low-wage informal work, while the economy remains heavily reliant on mining.

Figure 1. Zambia: Labor Productivity Growth: Within vs. Structural Reallocation

Productivity growth in Zambia has been modest and increasingly driven by within-sector gains, with limited contribution from structural transformation.



Source: Staff estimate based on World Bank, 2021. Global Productivity: Trends, Drivers, and Policies

Note: "Within" refers to productivity growth occurring inside individual sectors. "Between" (structural change) captures the contribution from labor shifting across sectors—e.g., from low-productivity agriculture to higher-productivity industry or services. "Total" reflects the combined effect of both components. See McMillan, M., & Rodrik, D. (2011). Globalization, Structural Change, and Productivity Growth. In: Bacchetta, M. and Jansen, M. (Eds.), Making Globalization Socially Sustainable, Chapter 2, pp. 49–84. Geneva: International Labor Organization and World Trade Organization.

3. **Private sector dynamism is essential to accelerate this transformation.** Enabling existing firms to grow and encouraging the creation of new businesses can help reallocate labor to more productive jobs and diversify the economic base (Ayyagari et. al., 2014; Rodrik, 2013). Strategies that support firm growth, especially in labor-intensive sectors, are critical for absorbing Zambia's expanding workforce.

4. **This paper analyzes the constraints to firm growth in Zambia and their impact on business expansion and entrepreneurship.** It focuses on three key obstacles consistently cited by businesses: limited access to finance, unreliable electricity, and competition from informal firms. These constraints not only hinder the expansion of existing enterprises but also suppress the emergence of new ones. The analysis draws on empirical evidence from the World Bank Enterprise

Surveys (2007, 2013, 2019), and the World Bank Entrepreneurship Database to quantify the impact of these barriers and benchmark Zambia's entrepreneurial activity against peer economies.

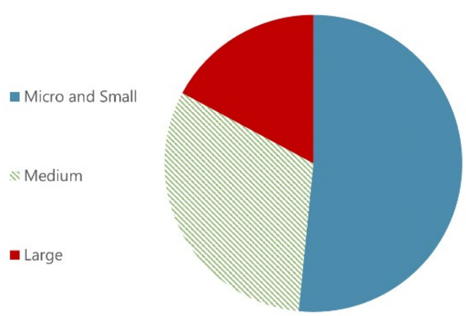
B. Firm Landscape

5. Zambia's private sector exhibits a dual structure that limits broad-based growth (Figure 2). A small number of large firms—typically in mining, finance, and telecommunications—coexist with a vast number of micro and informal enterprises, while formal small and medium-sized enterprises (SMEs) remain relatively scarce (World Bank, 2024). According to the Zambia Labor Force Survey 2023, about 76 percent of the workforce is employed in the informal economy, and estimates suggest that the informal sector accounts for about 40 percent of GDP (Elgin et al., 2021).. This widespread informality reflects a business environment where many firms operate outside formal regulatory and tax systems, reducing their access to finance, technology, and growth opportunities, and constraining the economy's ability to generate quality jobs and expand the tax base.

Figure 2. Zambia: Firm Structure and Employment Patterns

Most formal businesses in Zambia are micro and small enterprises, while medium and large firms account for only a small fraction.....

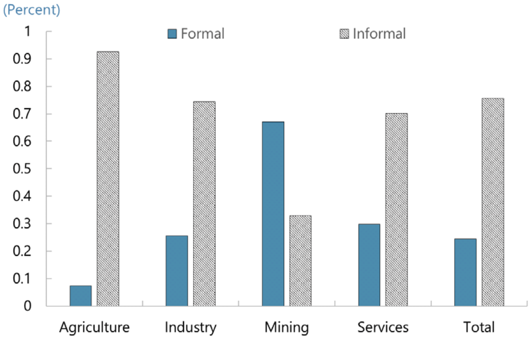
Zambia: Firms Distribution
(Percent: 2019)



Sources: World Bank Enterprise Survey Data 2019

....and informal employment dominates across all sectors, especially in agriculture and services, reflecting the limited reach of formal job creation.

Formal and Informal Employment
(Percent)



Sources: Zambia 2023 Labor Force Survey

6. This high level of informality is both a consequence and a cause of the limited development of the formal sector. Many entrepreneurs remain informal due to regulatory barriers and high compliance costs (World Bank, 2020), while the prevalence of informal competitors discourages formal firms from expanding. As a result, much of the labor force remains in low-productivity activities, constraining overall productivity and income growth.

C. Constraints to Firm Growth

7. Zambian businesses consistently identify three most binding obstacles to firm growth: limited access to finance, unreliable electricity supply, and competition from informal firms. These issues have consistently topped the World Bank Enterprise Survey rankings in 2007, 2013, and 2019 (Table 1), far outweighing other concerns such as tax rates, corruption, or labor skill shortages. In the 2019 Survey, 28.5 percent of firms cited access to finance as their biggest obstacle (up from 18.1 percent in 2007), 25.8 percent flagged electricity constraints (rebounding after a temporary dip in 2013), and 12.8 percent pointed to informal competition (down from 22.6 percent in 2013, but still among the top concerns). Moreover, Zambian firms report these issues more frequently than their peers in other countries. In 2019, the share of firms citing finance as the top constraint stood at 28.5 percent in Zambia, compared to 23.2 percent in Sub-Saharan Africa and 15.6 percent in lower-middle-income countries. Similarly, electricity was cited by 25.8 percent of Zambian firms versus 12.7 percent regionally, and informal competition by 12.8 percent compared to 10.4 percent in Sub-Saharan Africa.

Table 1. Zambia: Top Business Constraints Reported by Firms
(Percent of Firms)

	2007	2013	2019	2019 SSA	2019 Lower Middle Income
Access to finance	18.1	26.0	28.5	23.2	15.6
Access to land	8.3	8.1	1.5	5.4	3.9
Business licensing and permits	1.2	2.4	1.2	1.8	2.8
Corruption	4.0	5.1	5.3	8.3	9.3
Courts	0.7	0.1	—	0.6	1.0
Crime, theft and disorder	9.1	3.1	0.7	3.2	3.6
Customs and trade regulations	2.3	2.5	4.7	4.7	4.1
Electricity	14.4	12.2	25.8	12.7	9.4
Inadequately educated workforce	3.3	2.8	1.2	2.3	5.2
Labor regulations	0.5	2.6	0.8	1.0	2.4
Political instability	0.3	1.0	3.0	9.9	13.5
Competitors in the informal sector	14.3	22.6	12.8	10.4	13.6
Tax administration	1.2	1.1	2.7	4.1	3.6
Tax rates	16.8	5.6	9.8	9.5	9.1
Transport	5.5	1.9	0.7	2.6	3.0

Source: World Bank Enterprise Surveys 2007, 2013, and 2019

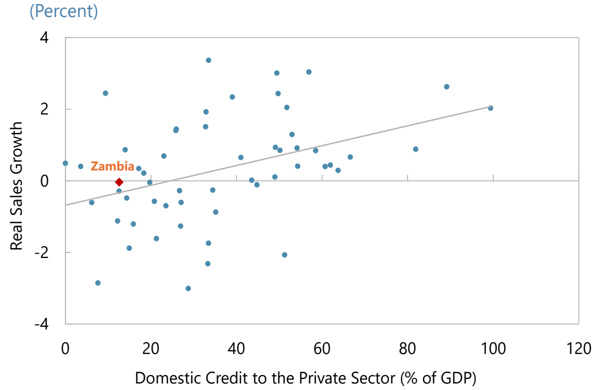
8. Access to finance remains a major constraint to firm growth in Zambia, including for large firms (Figure 3). Although nearly all formal firms have a bank account, only about 10 percent have a bank loan or line of credit—well below the Sub-Saharan Africa average of around 20 percent and the lower-middle-income average of 26 percent (World Bank, 2020). Consistent with this, the 2022 MSME Finance Survey found that 69.3 percent of Zambian business owners relied on personal funds to start their businesses, while only 3.3 percent accessed formal external sources such as commercial banks, microfinance institutions, or government programs (Bank of Zambia, 2022). This heavy reliance on internal and informal financing highlights the persistent barriers SMEs face in accessing credit, which limits their ability to invest and grow. Empirical literature consistently identifies access to finance as a key determinant of firm expansion (Beck, et al, 2005; Ayyagari, et al, 2008; Fowowe, 2017), and the lack thereof as a particularly binding constraint for small and medium-sized enterprises. In Zambia, persistent challenges such as high interest rates, strict collateral requirements, and underdeveloped financial infrastructure—including limited credit information systems—have curtailed lending to SMEs (Bank of Zambia, 2022).[1] Private sector credit as a share of GDP remains low.

Figure 3. Zambia: Access to Credit and Firm Performance

Zambia's low private sector credit is accompanied by weak firm growth, highlighting the link between limited financing and underperformance.....

Firm Growth and Access to Credit

(Percent)

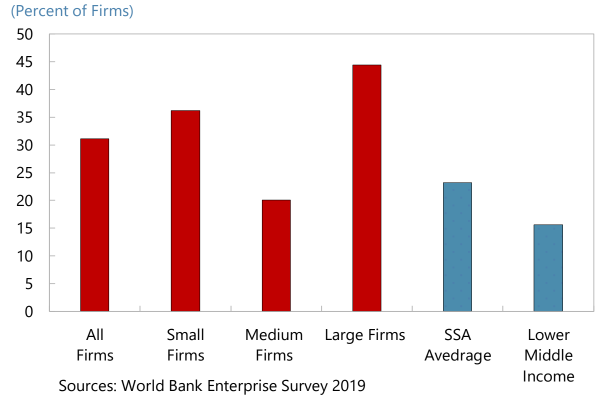


Source: Computed from World Bank Enterprise Surveys and World Development Indicator Database

Access to finance is a major constraint for Zambian firms—including for large ones—highlighting more severe financing challenges than in peer countries and the SSA average.

Access to Finance as Top Constraint

(Percent of Firms)



Sources: World Bank Enterprise Survey 2019

9. Electricity supply challenges are another critical barrier to firm performance. Despite Zambia's substantial hydropower resources, electricity supply often falls short of demand and remains erratic partly due to recurring droughts. According to the 2019 Enterprise Survey, 87 percent of firms reported experiencing power outages, averaging 13 outages per month—higher than the regional average of 8.6 outages per month. Inadequate power supply forces firms to depend on expensive generators or accept productivity losses, which raises costs and reduces profitability. This deters firm expansion, especially in energy-intensive sectors. Reliable infrastructure—including power, transport, and telecommunications—is foundational to a supportive business environment, and Zambia's current infrastructure quality has not kept pace with the demands of its private sector.

10. Informal competition also poses a persistent challenge to firm growth and formal sector development. Firms that comply with regulations, pay taxes, and follow labor laws face significant disadvantages when competing against informal enterprises that avoid these obligations.

[1] Average retail lending rate of about 28 percent in 2024.

The high prevalence of informality—reflected in both employment and firm counts—distorts competition, discourages formalization, and limits long-term investment. While the government has taken steps to simplify business licensing and reduce compliance burdens, regulatory complexity and enforcement inconsistency continue to inhibit the transition from informal to formal operations. Senior managers in Zambia report spending more time on regulatory compliance than their counterparts in peer countries (World Bank, 2024). Reforms such as the national e-Registry of licenses and risk-based regulation frameworks are welcome, but further streamlining and predictable enforcement will be essential to reduce the cost of doing business and support private sector development.

11. Regression analysis confirms that access to finance, electricity, and informal competition have statistically significant and economically meaningful effects on firm growth. Table 2 presents fixed-effects panel estimates using firm-level data on real sales growth, controlling for time, firm, sector, and location effects. The results indicate that access to credit, stable electricity supply, and a level playing field are all critical to enabling business expansion.

12. Access to finance shows the strongest individual effect. Firms with access to an overdraft facility—used as a proxy for credit access—grew on average 4.4 percentage points faster in annual real sales compared to those without, controlling for other factors (column 2). Conversely, firms that reported finance as a major constraint experienced 8.1 percentage points lower growth per year. Even when other constraints are considered jointly (column 4), the finance constraint remains significant and negative, reinforcing its central role. This finding aligns with survey evidence showing that only about 10 percent of formal Zambian firms have access to a loan or credit line, while the majority rely on internal funds for investment. Structural factors such as high collateral requirements, limited financial products for SMEs, and weak creditor rights continue to impede credit access and constrain firm expansion.

Table 2. Zambia: Panel Fixed Effect Estimates Firm Growth

Dependent: Sales Growth	(1) Power	(2) Finance	(3) Informality	(4) Major constraints
Access to Overdraft Facility		4.4447**		1.9607
		(1.6986)		(1.5820)
Finance Major Contraint		-8.1283***		-5.6604***
		(0.9757)		(1.0751)
Frequency of Power Outage	-0.1837***			-0.1335**
	(0.0635)			(0.0618)
Informality Constraint			-3.6575***	-2.3703*
			(1.2518)	(1.1900)
Constant	-1.5967***	-3.4857***	-1.0120	-0.6104
	(0.5180)	(0.5250)	(0.7132)	(0.9227)
Observations	86	86	86	86
R-squared	0.4899	0.4643	0.3235	0.6190
FE	Yes	Yes	Yes	Yes

Robust standard errors in parentheses; *** p<0.01, ** p<0.05, * p<0.1

13. **Electricity reliability also emerges as a statistically significant drag on growth.** The frequency of power outages is negatively correlated with sales growth: each additional outage per month is associated with a 0.18 percentage point decline in annual real sales growth (column 1). While seemingly modest, the cumulative effect of multiple outages compounds over time, especially for energy-intensive sectors. This quantifies the cost of Zambia's erratic electricity supply, which remains a top concern for firms despite abundant hydropower potential. The impact is even stronger when outages are considered alongside other constraints (column 4), indicating that electricity disruptions independently erode firm performance. This finding underscores the need for investments in both generation and grid reliability to stabilize supply and reduce business costs.

14. **Informal competition also has a dampening effect on firm performance.** Firms that identified informal competitors as a major constraint grew on average 3.7 percentage points slower than others (column 3). This effect remains statistically significant in the full model (column 4), suggesting that unfair competition from informal enterprises can materially hinder formal firm growth. Informal businesses often avoid taxes, labor laws, and quality standards, enabling them to undercut prices and gain market share at the expense of compliant firms. In highly competitive sectors such as retail and services, this creates an uneven playing field and discourages formalization and long-term investment. With informality accounting for over 70 percent of employment and around 40 percent of GDP in Zambia, addressing this constraint is essential not only for firm-level outcomes but also for macroeconomic performance.

15. **Overall, the econometric analysis supports the perception-based survey findings.** A access to finance, power reliability, and informality are not only commonly reported barriers—they are empirically linked to weaker firm growth. Tackling these constraints through targeted policy

reforms could unlock significant productivity gains and support Zambia's broader development objectives.

D. New Firm Formation

16. Zambia's rate of new business formation remains low relative to global benchmarks, reflecting deeper constraints on entrepreneurship. A dynamic private sector requires a steady inflow of new firms to drive innovation, competition, and job creation. However, Zambia registers only about 1.6 new formal businesses per 1,000 working-age adults annually—above the average of 0.9 to 1 for low-income and lower-middle countries, but well below the 5–7 observed in upper-middle and high-income economies. While Zambia performs better than many low-income peers, it lags behind its income comparators and aspirational groups.

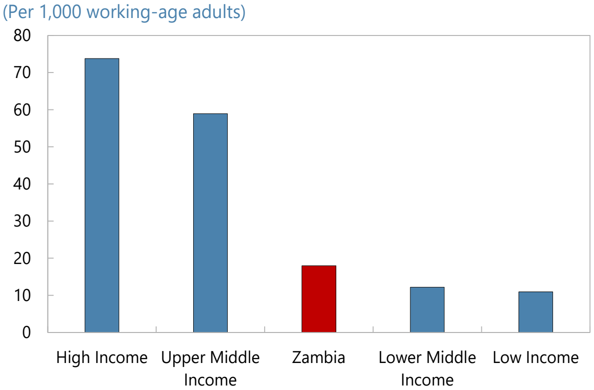
17. Zambia's stock of formal firms is modestly above its income group average but far below advanced economies (Figure 4). Total business density stands at about 18 registered firms per 1,000 working-age adults, compared to roughly 12 in the lower-middle-income group, 60 in upper-middles, and 74 in high-income countries. The gap is even more pronounced in new firm entry. This underscores that Zambia's formal private sector is not only small but also slow to renew.

Figure 4. Zambia: Formal Business Density: Zambia vs Comparators

Zambia's formal business stock exceeds its income group average but remains well below higher-income countries, reflecting a small formal sector….

Business Density

(Per 1,000 working-age adults)

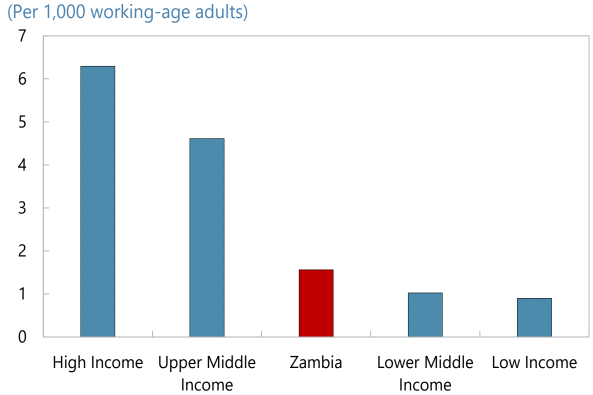


Sources: World Bank Entrepreneurship Database

…as does its new business density.

New Business Density

(Per 1,000 working-age adults)



Sources: World Bank Entrepreneurship Database

18. New firms are essential for economic dynamism and job creation. Evidence from both developed and developing economies shows that young firms—not necessarily small ones—are responsible for most net job creation (Haltiwanger, Jarmin, & Miranda, 2013). In Zambia's narrow and concentrated private sector, expanding the flow of new, growth-oriented firms is vital for diversification and inclusive employment.

19. Entry barriers suppress formal entrepreneurship. Regulatory hurdles and administrative complexity increase the cost and uncertainty of starting a business. Cross-country evidence shows that heavy entry regulation reduces both the number and quality of new firms, particularly in lower-income settings (Klapper, Laeven, & Rajan, 2006). While Zambia has made progress in simplifying procedures—such as digitizing registration (GSMA, 2024)—further reforms are needed to lower entry costs and sustain momentum.

20. New firm formation is often constrained by limited access to finance. Many entrepreneurs lack collateral, credit histories, or tailored financial products, leaving them unable to secure startup capital. Liquidity constraints are a well-documented barrier to entry (Evans & Jovanovic, 1989; Kerr & Nanda, 2009). In Zambia, the 2022 MSME Finance Survey confirms that most new firms rely on own funds, with only a small fraction accessing formal credit. Expanding SME finance initiatives, improving credit infrastructure, and promoting alternative funding sources such as fintech and leasing can address this gap. As highlighted in the GSMA (2024) report, digital financial services, particularly mobile money and emerging fintech innovations, are increasingly enabling access to credit and savings for underserved SMEs and informal businesses, especially in rural areas. Scaling up these solutions alongside a supportive regulatory environment can play a transformative role in broadening financial inclusion and supporting enterprise growth.

21. High levels of informality also inhibit the growth potential of new firms. Many businesses remain informal to avoid taxes or regulatory obligations, but such firms often stay small, unproductive, and excluded from financial and technical support. This reduces overall firm quality, erodes the tax base, and distorts competition (La Porta & Shleifer, 2014). Encouraging formalization through simplified registration and tax procedures, targeted support services, digital tools, and balanced enforcement can help transition informal entrepreneurial activity into the formal sector (Box 1).

Box 1. Good Practices to Support Formalization

Successful formalization strategies are typically integrated, incentive-driven, and tailored to national contexts. Rather than viewing formalization as a binary shift, effective approaches recognize it as a gradual process along a continuum, requiring a combination of simplified regulations, targeted support, and enabling technologies. Drawing on international experiences compiled by IOE (2024), the following good practices have emerged as effective in supporting the transition from informal to formal economic activity:

- Simplifying registration and compliance. Complex procedures discourage formalization. Benin's "entreprenant" status allows free, same-day registration for small businesses. Cambodia's CamDX portal enables registration with multiple agencies through a single digital platform.
- Implementing simplified tax regimes. Streamlined tax systems reduce compliance costs and promote formalization. Brazil's Simples Nacional and IME schemes offer simplified filing and fixed monthly fees with access to social protection. Mexico's Régimen de Incorporación Fiscal provides temporary tax discounts and simplified VAT rules.
- Leveraging digital tools. Technology enhances efficiency and transparency. In Nigeria, digital systems halved tax compliance time. Indonesia's JMP app handles over 70% of social security claims. Argentina uses a real-time worker registration database to cut inspection times from 40 days to one.
- Providing targeted support. Business support helps firms overcome capacity barriers. In Montenegro, grants boosted productivity and formalization. Indonesia's APINDO and Mexico's business chambers provide SMEs with training, market access, and digital tools.
- Combining enforcement with support. Enforcement is most effective when paired with education and incentives. In Colombia, increased inspections raised formal employment. In Nigeria, penalties are combined with measures such as reduced initial social security contributions to lower the cost of formalizing.

Source: International Organization of Employers (IOE). (2024). Innovative Approaches and Good Practices to Drive Formalization.

22. Much of Zambia's entrepreneurship is necessity-driven rather than opportunity-driven (Box 2). In the absence of formal jobs, many individuals turn to microenterprise as a livelihood strategy. However, these necessity-driven firms often lack the ambition or capacity to grow (de Mel, McKenzie, & Woodruff, 2010). To foster a more dynamic and opportunity-driven startup ecosystem, Zambia should complement entry reforms with targeted support—such as training, mentorship, and incubators focused on high-potential sectors like agribusiness, light manufacturing, and digital services.

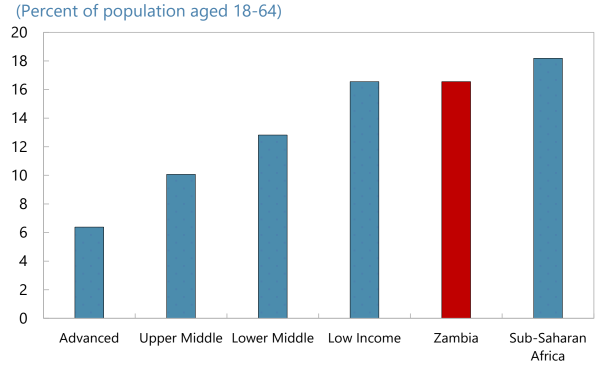
23. Improving firm survival and scale-up is just as important as entry. Many new firms fail early due to weak managerial capacity, limited market access, and vulnerability to shocks. Global experience emphasizes the value of a robust entrepreneurship ecosystem—including advisory services, incubators, and buyer linkages—to support growth beyond startup (Ayyagari, Demirgüç-Kunt, & Maksimovic, 2011). Strengthening these support systems in Zambia would raise the productivity and employment impact of new firms.

Box 2. Entrepreneurship Landscape in Zambia

Zambia exhibits one of the highest rates of early-stage entrepreneurial activity in Sub-Saharan Africa. According to the Global Entrepreneurship Monitor (GEM), 39 percent of the adult population was engaged in starting or running a new business in 2013—well above the average for resource rich economies. This level of entrepreneurial engagement reflects a strong culture of initiative and self-employment.

However, the bulk of this activity is necessity-driven rather than opportunity-motivated, with many individuals starting businesses due to the lack of formal employment options. As a result, Zambia's entrepreneurial landscape is dominated by informal, low-growth microenterprises that primarily serve local, subsistence-level markets. These businesses tend to operate outside of regulatory frameworks and often lack access to finance, business development services, or scale opportunities. **While the country shows strong entrepreneurial intent, firm sustainability remains a challenge.** Zambia's rate of established business ownership—defined as firms older than 3.5 years—is less than one-tenth of its early-stage rate. This gap highlights a high level of business discontinuation, underpinned by weak firm survival and limited transition from startup to maturity. Indeed, Zambia ranks among the highest globally in terms of business exit rates, pointing to structural barriers that constrain long-term firm viability.

Necessity Entrepreneurs
(Percent of population aged 18-64)



Sources: Global Entrepreneurship Monitor (GEM) 2013

Source: Global Entrepreneurship Monitor, 2013.

E. Conclusion and Policy Implications

24. Unlocking Zambia's firm growth potential requires decisive policy action to address long-standing structural constraints. This paper's findings underscore the critical importance of expanding access to finance, ensuring reliable electricity supply, and establishing a more level playing field for formal enterprises. Targeted reforms—such as deepening credit markets, strengthening financial infrastructure, investing in power infrastructure, and simplifying regulatory processes—would enable existing firms to expand and compete more effectively. Equally, policies that support new firm creation, including improved access to startup capital and tailored support for entrepreneurs, are essential to spur innovation and job creation. Together, these measures would accelerate structural transformation, raise productivity, and foster more inclusive and resilient economic growth.

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