



Factors Affecting the Economic Growth of Small and Medium Sized Enterprises: Case Study of Mutendere East, Lusaka District, Zambia

Stalin Muthuswamy*† and Castrol Kafweta

Chreso University, Nangwenya Road, Lusaka, Zambia

Received: 23 January, 2022; revised received: 27 February, 2022.
Month and Year of Publication: June, 2022.

Abstract

SMEs are the driving force for the promotion of an economy. This research work investigates the pitfalls which have affected the financial performance of the SMEs in Zambia. SME does not also necessarily mean a small struggling business operating from a back street establishment. Some SMEs are pretty solid. It may just be that their set-ups have simple processes and few employees. At present, the Zambia Development Agency (ZDA) act of parliament of 2006 does seem not to be having any impact at all on the promotion of the Zambian entrepreneur through SMEs, and most SMEs in Zambia are ignorant of the provisions and powers given to them through this act. Small and Medium sized Enterprises (SMEs) are the backbone of virtually all economies in the world. However, the process has long been constrained by various factors, one of such constraints is the limited availability and accessibility of financial resources to meet a variety of operational and investment needs within the SME sectors. The main objective of this research paper is to identify factors affecting the financial growth of SMEs in Lusaka, Zambia.

This study adopts a descriptive survey research which will use the qualitative approach. Data collection consists of surveys, observations and interviews with various officers heading the Government agencies, heads of the Micro financing institutions, commercial and procurement managers of the big companies and other Parastatals and the SMEs company managers. The study concludes that access to finance and availability of managerial skills and experience are the key socio-economic factors affecting the growth of businesses in Lusaka district. These two have the potential of leading to improved business performance. The other key factors that were found to affect growth of micro and small enterprises in Lusaka district are: access to business information, government policy and regulations and access to infrastructure.

Keywords: SMEs, Zambia, Zambia Development Agency, Micro financing institutions.

*Corresponding author; Email address: stalinrocks86@gmail.com

†Director, Examinations, Chreso University, Lusaka, Zambia.

Introduction

Overview

The small and medium sized enterprises (SMEs) have been a subject of continual interest to both researchers and practitioners (Watson, 2010). This enlightenment research project investigates the pitfalls which has affected the financial performance of the SMEs in Zambia. SMEs despite their significant roles in the economies of scale are however often overshadowed by the big conglomerates. However, SMEs by nature feed into the conglomerates and provide employment resulting into a strong middle class – the consumption class which drives the economy. Some businesses which start off as SME graduate into corporates and with time may mature into multinationals. From the author's perspective, SME does not also necessarily mean a small struggling business operating from a back street establishment. Some SMEs are pretty solid. It may just be that their set-ups have simple processes and few employees.

According to (Subhan et al., 2013), SMEs are the driving force for the promotion of an economy. Due to their significance, all the countries either, developed or developing, are concentrating on the development of SMEs. He also argued that, Small enterprises are considered as main driver for innovation, poverty reduction, employment generation, and social integration. SMEs sector may amplify the production capacity which has significant impact for the promotion of economic and social development. Avendano (2013) mentioned that, SMEs provide the vast majority of employment in developing countries and are keystones in the productive structures of emerging economies.

Background of the Study

Before the economic reforms were undertaken in the early 1990s, Zambia's economy was a government driven. This was so, for good and obvious reasons, some of which included the duty on the part of the government to provide employment, and the necessary social services that the government was obligated to, soon after independence in 1964. In the pursuit of achieving these objectives the government formed a number of companies in which it injected a lot of capital and also had to nationalize a lot other in the program called nationalization. Born out this, government initiative were companies like Mwaiseni stores, Niec stores ZCBC, United Bus Company of Zambia (UBZ) INDECO milling brought on board to provide goods and services to the public. (Mwitwa, 2006)

However, as early as 1981 the Zambian government recognized the importance of the SME sector and its contribution to economic development. At the same time, the government recognized the challenges that the sector was facing and therefore, through the Small Industries Development (SID) Act of 1981 made an attempt to enhance the effectiveness of the sector's contribution to the national economy by establishing the Small Enterprise Development Organization (SIDO). In support of the SID Act, provisions were made for the Fourth National Development Plan of 1989 to provide infrastructure for operations of SMEs, promote access to credit by SMEs with growth potential and to improve production capacities of SMEs with the view to increase incomes and employment (Chiumya, 2006).

Small and Medium sized Enterprises (SMEs) are the backbone of virtually all economies in the world. However, the process has long been constrained by various factors, one of such constraints is the limited availability and accessibility of financial resources to meet a variety of operational and investment needs within the SME sectors. SME and entrepreneurs play a significant role in all economies and are key agents of employment, innovation and growth. A significant number of entrepreneurs and SMEs could use funds productively if they were available, but are often denied access to financing, thus impeding their creation, survival and growth. (Chiumya, 2006).

Statement of the Problem

The economic climate for carrying out business for SMEs in modern society differs from state to state. As such, the appropriate policy for one country would not necessarily be appropriate for

another. With privatization of 1991, the economy become more liberal which resulted in increase of difficulty for local SMEs to grow and face up to competition being created by foreign companies. In view of this, the fairness of the economic policies governing the way business is conducted in Zambia on the basis of companies being local SMEs and foreign conglomerates is being questioned. The whole purpose of empowering local Zambians is being defeated because they cannot face up to competition from foreign companies in terms of capacity, quality of goods, access to financing and general management (Chiumya, 2006).

At present, the Zambia Development Agency (ZDA) act of parliament of 2006 does seem not to be having any impact at all on the promotion of the Zambian entrepreneur through SMEs, and most SMEs in Zambia are ignorant of the provisions and powers given to them through this act. Given the circumstance how adequate are the provisions contained in the ZDA act to empower the Zambian SMEs and what strategies and methods is the ZDA going to use to ensure that the Zambian entrepreneurs are aware of the various provisions and policies the act brings on board to empower them. Although the SMEs in the private sector in Zambia have such great potential for economic development, equitable wealth redistribution and poverty alleviation, they face many business constraints and challenges which hinder growth and limit their ability to contribute effectively to national economic development.

Research questions

- What are the factors effecting the growth and success of small and medium sized enterprises in Lusaka District?
- What should be done to mitigate these factors in order to necessitate the growth and success of Small and Medium Enterprises?
- How should an enabling business environment for stimulating the growth of the SMEs sector be created?

Research Objectives

Main Objective

The main objective of this research paper is to identify factors affecting the financial growth of SMEs in Lusaka, Zambia.

Specific Objectives

The specific objectives include:

1. To highlight the specific factors affecting the financial growth of SMEs.
2. To determine the accessibility of finances by SMEs.
3. To identify key collateral requirements that hinder SMEs from fulfilling certain contractual obligations in their quest to do business.
4. To identify the key support structures and aspects of the support environment for Zambian Enterprise growth activities.

Scope of the Study

This research will be limited to the study of the various SMEs in Lusaka District to find out what problems they face in the quest of carrying out business and their growth. It is the desire of the researcher to interview various government agencies and Non-Government Organizations whose role relate to SME sector growth, on what policies government and NGOs has put in place to promote the growth of SMEs in Zambia and how well these are being implemented.

The researcher will examine the various journals and publications that have to do with the issue of small and medium scale enterprises in Africa and beyond in order to ascertain the views and opinions of the writers. The various small and medium scale enterprises in Lusaka's metropolitan area will also be examined with a view of finding their response. Also, the researcher will examine some individuals in the metropolis of Lusaka town in a bid to ascertain their own views and opinions. The study is therefore confined to SMEs operating in Lusaka, and yet it is easy to use the result of this research to gain insight into the whole country.

Literature Review

Theoretical

The financing constraint literature has been the first to recognize that partitioning firms helps to provide important insights into their behaviours.

Fazzari, Hubbard and Petersen (1988), pointed out the fact that firms are definitely not homogeneous. They classify firms according to their dividend payout ratio. Their main aim in doing this is to show that firms that have different dividend payout ratios and therefore belong to different categories, have differential access to finance. Some firms are financially constrained while others are not.

According to Aghion (2007), access to external finance improves market selection by allowing small firms to be more competitive. Additionally, financial accessibility significantly facilitates the growth of firms. Unlike large firms, SME are restricted in their funding options. Tambunan (2010) argues that SMEs in developing countries can survive, and even grow in the long run, as they create a niche market for themselves, they act as a last resort for the poor, and they will continue to grow alongside larger enterprises for which they often supply required inputs.

Empirical

Despite the macroeconomic reforms undertaken by the government aimed at macroeconomic stabilization for example, liberalization, privatization among others, the SMEs sector has not yet significantly benefited from them. There have been a number of constraints that have hindered the growth of SMEs in Zambia. The Task Force on SMEs (2014) identified some of the constraints affecting the Zambian SMEs as:

Research Methodology

Introduction

This chapter outlines the methodology on how data and information relevant to the research will be gathered and analyzed in order to achieve the objectives of the study.

Research design

This study will adopt a descriptive survey research which will use the qualitative approach. Descriptive survey design is a method of collecting information by interviewing or administering questionnaires to a sample of individuals hence suitable for extensive research.

Study Population

The research intends to cover SMEs, various government Agencies set up under the acts of parliament (ZDA, ZRA, and NCC). Other targeted are Micro finance lending Institutions, and SME sector Associations.

Sample size

The research will be focused on a fairly small sample size to facilitate meaningful depth of analysis in the light of time and resource constraints. This is to enable the sample with reasonable accuracy, to reflect the thinking, opinions, attitudes and behaviours of the entire population. The sample size makes it possible to integrate and critically examine theory and practice (Ngwenya & Ndlovu, 2003). For the purpose of this study, a sample of 15 will be used included among these are Government agencies, ZDA, and ZRA. The SMEs and big companies like First National Bank Zambia (FNB) will also be surveyed for their business conditions, experience, constraints and expectations. The 15 firms will be chosen in order to get a better representation about the number of medium and small sized businesses in the Country and also the policy facilitating agencies. To enable us draw valid conclusions from the survey as applicable to small and medium sized enterprises generally, representative companies from each

of the different groups (suppliers, and contractors) will be studied so that at the end, different companies with different categories of business and processes will have been studied.

Data collection

Both primary and secondary data will be used in collecting information. Data collection will consist of surveys, observations and interviews with various officers heading the Government agencies, heads of the Micro financing institutions, commercial and procurement managers of the big companies and other Parastatals and the SMEs company managers. Initially, a survey instrument to measure how ideal and convenient are the government policies in promoting SME sector growth are, will be speculated and also how ideal and convenient are the lending conditions from the Micro finance leading institutions.

Data Analysis Tool

Data will be analyzed according to a frame work that will be as follows:

The first part of the study will review literature from different parts of the world including Zambia and describe and evaluate different SME policies in these countries and compare them with our Zambian policies. This will be basically a desk research which will examine previous research papers and practices in these countries in order to map the current understanding of SME enterprise development and to identify critical issues.

The second part will critically analyze the genesis of the SMEs in Zambia focusing on the role of Government in promoting SME development. This will involve careful study and analysis of literature and documents in Libraries, at the ministry of commerce Trade and industry, Zambia Development Agency, Zambia Revenue Authority (ZRA).

Sampling Techniques

The general population for this study is composed of Small scale and medium Enterprises in Zambia. Basically these respondents will be asked regarding the current status of policies, procedures, collateral requirements, tendering process, registration and the general playing ground is fair for all to participate in business and compete effectively with outside companies.

Summary, Conclusions and Recommendations

Introduction

This chapter provides a summary of the study, discussions and conclusions drawn thereof. The researchers then present the major limitations of the study and the recommendations for both the research and for the policy change and practice.

Access to business information services

The study established that access to business information affects growth of businesses in Lusaka district to a moderate extent and this information was not readily available at the Zambia Development Agency. Even the available information was not deemed to be relevant nor does it inform the respondents of the changes in the business environment on time. Overall, the business information services in Lusaka district affect the performance of businesses to a small extent.

Access to Finance

The study established that access to finance exposes businesses in Lusaka district better opportunities to a great extent while it also leads to improved business performance to a great extent. The study also found out that access to capital for businesses is very challenging to a greater extent. Overall, access to finance affects the financial growth of SMEs in Lusaka district to a greater extent.

Managerial Skills

The study further found out that availability of managerial skills and experience affects businesses in Lusaka to a great extent while the respondents felt that training on managerial skills are required in the businesses to a great extent. Further, the respondents reported that they do not get trainings on business management skills frequently. Overall, availability of managerial experience affected business performance only to a moderate extent.

Access to Infrastructure

On infrastructure, the study established that good road network is available to the business people around Lusaka and it's easy for them to do their business. The respondents' reported that the working space allocated to them is accessible to a great extent but is sufficient only to a moderate extent. The road becomes only bad during the rainy season. However, electricity power is real challenge and water, most business do not have running water. Study also found out that infrastructure affects the financial growth of businesses to a greater extent.

Recommendations

Access to business information

There is scarcity of business information in Lusaka district. The government of republic of Zambia should work in collaboration with the Zambia Development Agency so as to organize seminars and business drills for these SMEs. Other development partners like banks and saving and credit organizations should also educate these SMEs so that they may perform better.

Access to Finance

The study found out that most SMEs prefer to use personal savings and contributions from relatives because they find it very difficult to access financing from commercial banks due to strict requirements such as collateral security and high repayment costs. The study therefore recommends that banks and other credit giving financial institutions should come up with creative policies that make it easy for the SMEs to access financing.

The government should start offering basic business and financial management skills as this will enable the SMEs to make informed investment decisions. This will enhance their entrepreneurial skills that will enable them to recognize and exploit the available business opportunities in the country.

Access to Infrastructure

Access to infrastructure affects the growth of SMEs only to a moderate extent. However, the study recommends renovations of public goods such as roads, electricity power and water to weather changes.

Government Policy and Regulations

The study found out that the government policy and regulations has a moderating effect on the financial growth of SMEs. The study therefore recommends that the government should move in quickly to create policies that favour the growth and expansion of SMEs in Zambia. This will save the businesses from the challenges they face when trying to access financing from mainstream commercial banks.

Areas for Further Research

Arising from this study, the following directions for future research should be carried out. This research only covered micro and small enterprises in Lusaka district, particularly mutendere east. However, there are other enterprises that are medium and large firms in the same district. Researchers are encouraged to research on them. In future, other SMEs in other towns should be involved to enable the researcher to make adequate conclusions.

This research didn't concern itself with the challenges and possible solutions hindering SMEs from accessing financing by credit giving institutions. In future, a research should be

instituted to establish the challenges and the possible solutions. In future, a comparison should be done between the financial performance of SMEs that have received microcredit and the ones that have not received the financing. This will help in shedding light on whether accessing microcredit helps the SMEs to perform better than other businesses.

Conclusion

The objective of the study was to establish the factors affecting the financial growth of micro and small enterprises in Lusaka district. The study concludes that access to finance and availability of managerial skills and experience are the key socio-economic factors affecting the growth of businesses in Lusaka district. These two have the potential of leading to improved business performance. The other key factors that were found to affect growth of micro and small enterprises in Lusaka district are: access to business information, government policy and regulations and access to infrastructure.

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