

# Factors influencing development survival small businesses in nigeria economics es...



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In recent times, significant attention has been focused on small and medium scale enterprises in developing countries because of their potential for diversification and expansion of industrial production, as well as the role they play in the attainment of the objectives of development.

According to Navidi and Schmitz (1994) these roles are (a) small scale enterprises utilize large labour surplus that exist in developing economies; (b) they yield quick returns; given their capital requirements, they facilitate the exploitation, mobilization and utilization of local capital resources. Thus, in any economy where capital and institutional savings as well as management and technical skills are inadequate, the contribution of these small firms cannot be over emphasized.

### Structure and Characteristics of the Nigerian SMES

The choice of literature for this study is limited to those that are vital to the contribution about the factors influencing the survival of smes in developing countries.

In Nigeria, there a lot of definition of SMES, the central bank of Nigeria (CBN) in its monetary policy circular No 22 of 1988, defined SMES as having a turnover not exceeding 500, 000 Naira. Also by 1990 commercial banks define SMES as those enterprises with annual turnover not exceeding 500, 000, while for the merchant banks, they have defined SMES as those enterprises with annual turnover not exceeding two million naira. In addition, the CAMA of Nigeria of 1990 defines a small business as one with annual turnover of not more than two million naira and a net value of not more than

one million naira. However the definition of SMES varies from country to country.

The nation needs the Small and Medium Enterprises (SMEs) because they contribute meaningfully to economic development. They are in the forefront of output expansion, employment generation, income redistribution, promotion of indigenous entrepreneurship and production of primary goods to strengthen industrial linkages.

The sector is responsible for about 70 percent of the total industrial employment in our country and between 10-15 percent of the total manufacturing output. The agricultural sector which comprises mainly of SMEs has promoted indigenous technology and increased utilization of local raw materials. They are the strongest promise we have for industrial growth.

SMES play a vital role in both rural and urban economies of Nigeria and they abound in all sectors of the economy. According to Adegbite (1997), a study conducted by the international finance cooperation estimated 125, 000 in 1983. The number has been estimated to above 200, 000 in 1997 however excludes the numerous ones that are operating in the informal sector of the economy; there are indicators that SMES account for about 70% of industrial employment and 10% to 15% of manufacturing output (CBN 2000).

A sectional composition analysis of Nigeria industrial structure by CBN (2000) shows that while over 90% of industrial establishment engaged less than 50 persons, only 2. 5% engage more than 25%.

Over the year government has pursued policies that would provide favourable conditions for small business including trade liberalization and some incentives therefore making the environment friendly to entrepreneurs. IMF and other organization agreed to support the economic growth of Nigeria by helping to finance infrastructure improvements. Okpara (2007). Some of the scheme embarked upon by government includes; the introduction of fiscal incentive . i. e. granting small business tax holiday for the first six years of it operation. To give financial support, the Central Bank of Nigeria set credit guidelines requiring commercial bank to allocate set aside certain percentage of their funds to small business. Several developmental financial institutions and schemes were also established to aid small businesses, including the Nigerian Bank of Commerce and Industry (NCBI), the Nigerian Industrial Development Bank (NIDB), and the World Bank SME I and SME II initiatives. There were also export incentives from the Nigerian Export-Import Bank (NEXIM) to stimulate export loan facilities to small businesses as well as export duty exemptions administered by the Nigeria Export Promotion Council (NEPC). Other small business incentive programs included personnel training, repair and maintenance of specialized machines, and extension services. Small-business assistance programs have also been established by local and state governments. Okpara(2007)

With the various programs and support, it is logical to assume that small businesses/ small scale sector in Nigeria would have gradually taken its place as the instrument to change the Nigerian economy has anticipated by researchers. However, reverse is the case has failure rate of businesses continue to increase and the effectiveness of the programs remains unclear.

With the increase in the failure of SMEs the future of this sector looks bleak, and this could change the notion held by some economists and researcher that SMEs could be a major driving force in reintegrating Nigeria into the global economy.

To understand the topic further I will be considering the various reasons for starting up a business. Stoke (2009) found that reasons for starting a business as accounted for the failure of some business. For instance during the dot. com boom so many business sprang up because some many entrepreneur saw it as a way to get rich quickly therefore going into the business without adequate preparation and this saw many of them going out of business.

The motivation for the start up

With the increase in new small business only a tiny minority have being recorded to have experience substantial growth or grow to a large enterprise. Many ceases to exist only few years usually 1-2 years into trading this may be as a result of fading of heroic visions or inappropriate “ home work”, some of whom quickly return to other types of employment or sadly unemployed. The decision to start a business is always a courageous one regardless of the type or business or circumstances surrounding the decision. There are many reasons for starting up a business, stokes (2010) identified this reasons under the term pull and push influences. An individual can either be pushed into self employment because there was no other alternative or one can be pulled into self-employment to pursue a business opportunity.

According to Grilo et al (2006) pull factors refer to the expectation of being better off as an entrepreneur (i. e., attracted to self-employment with the expectation that it will provide greater (im)material benefits), and that push factors is the conflict between one's current and one's desired occupational status (i. e., associated with some level of dissatisfaction). Push and pull effects are comparable to necessity-based entrepreneurship and opportunity-based entrepreneurship, respectively. Opportunity entrepreneurs are influenced by pull factors to start a business, while necessity entrepreneurs are affected by push factors.

Pull factors include

Desire for independence: this when one desire to be boss of oneself and not wanting to be pushed or under someone. This reason is believed to be common among female entrepreneur.

Desire to be exploit opportunity: the identification of a gap or opportunity in the market through experience or observation is a common reason for starting a new business. The desire to explore this opportunity is a positive motive and can be done through applying specialist knowledge or developing a new product, or through hiring the appropriate technology.

Turning a hobby or previous work experience into business: according to research may founders establish businesses in the area in which they have prior knowledge or experience, example of Bill Gate and other great entrepreneurs.

Financial incentives: the probability of having access to large fund and earn large salary.

Push Factor;

Redundancy: this is considered a push factor lately with the advent of the recession which started with the housing crisis in 2008 where there has being thousand of redundancies across the world. Men and women are faced with no job and on income and this has them pushed to set up their own business using the generous handshake accompanied with redundancies in some cases.

Unemployment: job insecurity and unemployment varies in significance by region, and by prevailing economic climate. According to scott et al (1986) a study of 25 per cent business founders in the late 1970s were pushed, while later research showed a figure of 50 per cent when unemployment nationally are much higher.(stoke et la 2010).

Disagreement with previous employer: uncomfortable relationships at work has influence people to start their own small business

According to survey it has shown that small business owner that are pulled rather than pushed have higher chances of succeeding. Put differently, a positive motivation (pull factor) to start a business will in the long run have a positive effect on the performance of the business, on the other hand those who are self employed based on the push factors will less likely be successful because they are being pushed due to circumstances they find themselves

therefore start a business as a last resort, most time they are not ready for the challenges associated with small business.

To further explore the factor that at influence the small businesses: I will be taking a cue from the previous researches where various researchers who have identified numerous factor affecting small business. Stoke (2010) identified some factors which he termed “ a matter of life and death of small firms” in his book. These factors can be generally divided two factors external and internal factors. The internal factor revolves around the characteristics and behaviour of the entrepreneur. The external factors are largely beyond the control of the entrepreneur.

Some researchers are of the opinion that, it is the combination of less controllable (external factors) together with the more controllable (internal factors) arising from personal attributes, management competencies and behaviour of entrepreneur which influence the start up or survival of small businesses. Stokes (2010)

Over the years researchers identified internal factors as the major cause of failure of small business in developing countries. Kazooba (2006) revealed that poor recordkeeping and lack of basic business management experience and skill was the major contributor. He further identified inadequate managerial skills, inexperience in the field of business, lack of planning, lack of technical knowledge and lack of market research. (okpara, 2007). Also many literatures have supported this notion. However, according to Barclays bank business bulletin (2000), they were of the opinion that the high failure of small business is as a result of the economic cycle or economy of a given



country. They accounted in 2000 which was a year with relative economic prosperity there was high rate of small business survival. Hall (1995) established that a business has a higher chance to survive given a good business environment. For the purpose of this study I will be focusing on the external factors.

There are many factors in the macro-environment that effect the decisions of the managers of any organisation. Tax changes, new laws, trade barriers, demographic change and government policy changes are all examples of macro change. Adelaja (2006) identified it as operating environmental challenges

To help analyse these factors I will categorise them using the SLEPT analysis model. Every Business is generally affected by the economic, social, legal, technological and political factors. These factors collectively form the business environment. Business environment involves those external forces, factors and institutions that are beyond the control of individual business organisations and management but affect the business enterprise. Some of the forces affect the business directly while others have indirect effect on the business.

#### Economic factor

Economic factor refers to the total nature of economic system of a country, the structural composition of the economy to economic policies of the government the organisation of the capital market, business cycles, the socio-economic infrastructure etc. These are some of the variables in an economy that affect the demand/supply for good and service. Successful <https://assignbuster.com/factors-influencing-development-survival-small-businesses-in-nigeria-economics-essay/>

businesses think about the external factors affecting the business, anticipating the future market situations and makes appropriate decisions to get the maximum with minimize cost. Examples of the economic factors are discussed briefly below

**Inflation:** is a general rise in the level of prices. High inflation increases the price of raw materials as a result increases the cost of doing business.

Business have the option of accepting reduced profit or pass the higher costs to consumers in the form of higher prices. By increasing prices this might discourage consumer especially those who are not employed because their purchasing power is low and this will ultimately affect the sales and profit. When continued for long businesses might not have enough funds to run the enterprise.

Generally in developing countries inflation are high e. g. Nigeria's inflation rate went from 12. 5% to 10. 3% in July 2009 and June 2010 receptively this can be credited to the economic reforms. (Thandeka 2008)

**Interest rates:**

The rate of interest represents two main things: It is the cost of borrowing money and it is the reward for saving money. However interest rates are set by the apex bank of a country. An economy characterised with high interest rates show that the costs of borrowing funds from financial institutions are more expensive and this discourages borrowing. This is often the case in developing countries such as Nigeria, interest rate was 11% in 2003 due to economic reforms and economic policy has seen it drop to 6-8% in March 2010. But when compared with other developed countries it is high. This has <https://assignbuster.com/factors-influencing-development-survival-small-businesses-in-nigeria-economics-essay/>

accounted majorly for the poor state of the small scale industry in Nigeria. Low interest rates facilitate access to capital and thus resources required for entrepreneurship (Ligthelm & Cant, 2002: 5).

### Exchange rates

Exchange rates are a major factor in entrepreneurship (Viviers et al, 2001: 4; Ligthelm & Cant, 2002: 5). because some small business raw material or product are sourced or demanded abroad. In a situation where there is high fluctuation of exchange rate this might make planning very difficult for business. E. g. Nigeria's weak naira means that there are more opportunities in the export market but, there is less capital for investing in local SMEs.

### Taxation

One of the key factors slowing down SME development is taxation. The complexity and multiplicity of the tax system raises the cost of doing business, as many SME do not have the capacity to administer tax returns and thus need to consult experts for a fee in order to meet these legal requirements. Also costs associated with meeting VAT and corporate tax is among the highest in the world.

Unemployment: This is generally a negative influence on businesses, especially small businesses. When unemployment increases, more people are out of work and so their income falls. When income falls, people have to cut down on their spending, this of course means they go out and spend less on the products and services provided by businesses. As the sales of business products and services falls, then so will the revenue and profit of

businesses. As revenue and profit falls, some businesses may find that they can no longer continue in business i. e. they close down; this in turn may create even more unemployment. An advantage of unemployment is that more workers are available, and small business can easily find skilled labour at a reduced pay.

Lack of Infrastructure: the unavailability of basic infrastructure as been a major hindrance to the development of small scale industry in Nigeria as the country does not have adequate electricity, good road networks, water, communication and internet facilities. Which modern businesses require to function effectively. Due to the presence of few of these facilities the prices are high which is sometimes beyond the reach of small businesses. However, where the small business could afford it, it makes the cost of business to increase which entrepreneurs either totally/partly passes to the consumer in form of high price.

#### Social factor

The social factor of a nation determines the value system of the society which, in turn affects the functioning of the business. Social factors such as costs structure, customs and conventions, cultural, lifestyles, view toward wealth and income and scientific methods, age distribution, mobility of labour etc. have an extensive impact on the business. These factors determine the work culture and mobility of labour, work groups etc. For instance, the nature of goods and services to be produced depends upon the demand of the people which in turn is affected by their attitudes, customs, so as cultural values fashion etc. Socio-cultural environment determines the

code of conduct the business should follow. The social groups such as trade unions or consumer forum will intervene if the business follows the unethical practices. For instance, if the firm is not paying fair wages to its business in indulging in black marketing or adulteration, consumers forums and various government agencies will take action against the business. (Thandeka 2008) Businesses need to take a pro-active approach and be ahead of these changes, rather than hurriedly making alterations to products and processes in a reactive way.

#### Political factor

The political factor of a country is influenced by the political organisations such as political parties, ideology of government or party in power, nature and extent of bureaucracy influence of primary groups etc. political instability in the country, foreign policy, image of the country and its leaders in and outside the country these are some of the forces businesses have to understand how they work in order to survive. The political environment of a country influences businesses to a great extent.

#### Legal (regulatory) factor

Legal factor includes flexibility and adaptability of law and other legal rules governing the business. It may include the exact rulings and decision of the courts. These affect the business and its managers to a great extent.

#### Technical environment

The business in a country is greatly influenced by the technological development. The technology adopted by the industries determines the type  
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and quality of goods and services to be produced and the type and quality of plant and equipment to be used. Technological environment influences the business in terms of investment in technology, consistent application of technology and the effects of technology on markets. In India, advancements in automation and information technology have posed the challenging situation for the organisation in future.

There has been only little interest on the relationship of macroeconomic conditions on the performance of and survival of SMEs. Gordon (1988) recognises that macroeconomic conditions can affect the survival of any business. He was of the opinion that tight monetary policy and an increase in interest rate can sharply change the cost of borrowing for businesses and hence destabilize the sector. In the work of Wadhvani (1986) he investigated that changes in the level of inflation can affect the volatility of cash flow and reduces the firm's ability to pay interests on its debts in the case of high inflation, thus threatening the viability of many businesses. Liedholm and Mead (1998) concluded that a general economic fluctuation is directly related to the business survival/performance. Gonzalez (2002) examines the effect of economic control on firm growth, and finds that the economic development and efficient financial system are positively correlated with firm growth. He also looks at the relationship between firm growth and such factors as bank control, corporate law, bankruptcy law, accounting standards and fair market competition, and concludes that a highly effective legal environment not only can protect investors' interests and help growing firms raise equity capital from the market, but also can influence the financial market development, which, in turn, facilitates firm growth.

The studies on SMEs in developing countries have identified various factors that are related to SME survival and growth. Legal system, institutions and financing are the most claimed factors that have impacts upon the survival and growth of firms. Thorsten et al. (2002) in a survey study of 54 countries, find that firm growth is determined by legal institutions, corruption and financing, and small firms are affected most. Faultless legal system facilitates firm growth, while corruption and lack of finance adversely affects firm survival and growth. (liu and pang 2003) Their study suggests that countries, especially the developing countries where these problems are more prevalent, need to improve their financing environment and reform legal system as well as take proper measures to reduce corruptions to minimum to create an environment suitable for small businesses. Liedholm and Mead (1998) examine eight African countries and confirm that firm age and firm size are some of the important variables in analyzing the enterprise survival. Their work further show macroeconomic factors such as location, composition of activities, labour force and national income make up other important determinants of firm survival and growth.

From the various reviews various factors have accounted for the low survival of small businesses in developing countries, the external factor is not controllable and can best be anticipated given the various indicators so as to change the internal factors to fit the business environment or guide the way in which a business operates.