



Problems experienced by small businesses in South Africa

A paper for the Small Enterprise Association of Australia and New Zealand 16th Annual Conference, Ballarat, 28 Sept-1 Oct, 2003.

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Abstract

It is estimated that the failure rate of small, medium and micro enterprises (SMEs) is between 70% and 80%. Millions of Rands are being lost on business ventures because of essentially avoidable mistakes and problems. It is maintained that often the ideas are good and the people behind them are competent, but “they do not have a clue of how to run a business” and have no underlying appreciation of business fundamentals. Problems encountered by small businesses are numerous and can be described amongst others as being environmental, financial or managerial in nature.

The objective of this paper is to establish to what extent owners/managers of small businesses in a typical South African setting, experience selected problems or issues as negatively influencing the success of their small business. Further to this, the aim is to investigate whether relationships exist between these problem categories and selected demographic factors.

A questionnaire was constructed and judgement sampling was used to solicit the responses of 300 small businesses. The following were identified as the most prominent problem areas influencing small businesses in the Gauteng area of South Africa namely, economic factors, competition, socio-economic problems and change. Significant relationships were identified between demographic variables such as management qualification and background of the respondent and certain problem categories.



1 Introduction

The survival rate of SMEs (small and medium enterprises) is relatively low. Less than half of newly established businesses survive beyond five years. This is not only true for South Africa, but also a common phenomenon in the rest of the world. In the South African economy, more than one million jobs have been shed since 1990, bringing the unemployment rate, by February 2002, at 28 percent (Lighthelm & Cant, 2002: 1).

The SME sector is widely regarded as the driving force in economic growth and job creation in both developed and developing countries (Sunter 2000:23). The important contribution that SMEs can make to employment and income generation is recognised around the world, and in particular in South Africa.

Surveys of small business failure maintain that entrepreneurs often have good ideas and are competent but “they do not have a clue on how to run a business and have no underlying appreciation of business fundamentals” (Barron 2000:1; Brink 1997:364). The identification of their problems and development of appropriate training programmes to address these problems, should thus assist in equipping small business owners with the necessary managerial skills to survive in today’s competitive environment.

2 Research objectives

The main objective of this study is to establish which selected problems or issues are perceived by owners/managers of SMEs as negatively influencing the success of their businesses in Gauteng, a



province of South Africa. Further to this, the aim is to investigate whether there is any relationship between the perception of these problems and the level of managerial qualification.

3 Background

Small and medium-sized businesses form an integral part of the national economy and, as such are therefore influenced by various factors. In this context, the problems that SMEs face in conducting a successful business, can be categorised, based on their origin in the external (or macro) and internal environment (Cant, Strydom & Jooste 1999:23).

3.1 Macro environment

Management can exert no control over exogenous problems that manifest themselves in the economic, sociodemographic, political, technological and international spheres. The most prominent problems influencing SME success in this environment are the state of the economy, compliance with legislation, resource scarcity, HIV/AIDS, crime and corruption and rapidly changing technology. The entrepreneurs in the previously disadvantaged townships, for example, experienced problems with understanding the impact of technological development and the state of the economy on the success of their business (Brink 1997:354).

3.2 Market environment

As with the macro environmental issues, management has little or no control over external market factors such as market size, competitors, low demand and intermediary accessibility (Cant et al



1999:24). In the previously disadvantaged townships, for example, the entrepreneurs experienced problems with low demand and not enough knowledge of competitors, which was also due to the fact that they hardly ever conducted any marketing research on their competitors and the needs of their customers (Brink 1997:351).

- ***Internal market***

Deficiencies in the internal environment are the major cause of SME failures, and revolve around management skills, financial knowledge, lack of expertise in functional areas such as marketing, human resource management (Ligthelm & Cant 2002:3). Some of the problems emanating from these factors include specific management issues such as a lack of business management training and skills as well as a limited family business culture in South Africa. Other reasons for failure include the inability to act as entrepreneur, to control business growth and overemphasis on financial rewards. Management actions and behaviour which are lacking are inability to set strategic goals, plan forward, reluctance to seek advice, lack of management commitment and unwillingness to adapt to change (Ligthelm & Cant 2002: 6-7).

- ***Marketing factors***

Marketing factors such as poor location, insufficient marketing, inability to conduct marketing research, misreading the market, poor products or service, poor service, misreading customer trends and needs also impact on the success of SMEs.



- ***Human resource issues***

The labour market in South Africa is highly regulated with a high level of labour market rigidity. In this regard problems experienced include the inability to attract and retain suitable staff, loss of key employees, low productivity and inadequate training and development of employees.

- ***Production and operational issues***

The following operational aspects may impact on the success of SMEs: lack of proper quality control in the production process; lack of capacity planning, problems with suppliers of resources and limited attention to developing suitable products or services.

- ***Financial issues***

Financial management is a crucial field within the endogenous environment of SMEs that presents numerous potential obstacles. Management competence is often determined by the availability of management and financial information. Lack of financial sources is often reported as the major obstacle experienced by businesses. Financial issues important for business success are capital requirements, bookkeeping, financial planning, financial control, management of working capital and income generation.



The exposition of problems that may impact on the success of SMEs as identified above, forms the conceptual basis for the design of the research instrument used for this study.

3 Survey methodology

In order to fully understand the problems encountered by SMEs and the extent to which they negatively influence the success of small business, an empirical survey was conducted in selected provinces in South Africa.

The survey units extended across SMEs located in the above-mentioned six areas. For purposes of this study only businesses with a reasonable level of sophistication and understanding of concepts such as interest rates, exchange rates and inflation were included in the survey. Requirements were thus set prior to completion of a questionnaire at a particular business, namely: the SME had to have compiled an annual budget; operate from a demarcated business area (businesses operating from residential areas were excluded); occupy a permanent structure (businesses operating from temporary structures were excluded). These requirements excluded microbusinesses operating in the informal economy from the survey. However, to ensure surveying of business in the SME category, an upper employment limit of 50 full-time employees was set for inclusion in the survey.

A structured and pre-tested questionnaire was completed by 12 well-trained interviewers who lived in the survey areas and know them and the location of businesses well. The questionnaire consisted of two sections. Sociodemographic information, including aspects such as ownership, period of ownership, management qualification, number of full-time employees and annual turnover, was requested in section



A. Section B consisted of 51 items, divided into seven categories, five representing problem areas faced by SMEs according to various management functions (marketing, financial etc). Several statements relating to the various areas were phrased with a possible response continuum linked to a Likert-style five-point scale (1 = strongly disagree to 5 = strongly agree).

In the absence of a sample frame, a judgmental sample was conducted among small business owners/managers. The survey was conducted among 300 businesses in the six identified areas, namely Soweto, Tembisa, Mamelodi, Soshanguve/Mabopade, Johannesburg CBD and the Pretoria CBD, 50 respondents from each area, thus a total of 300.

Interviewers were instructed to complete the 50 questionnaires in each area according to the following sectorial distribution: retailers (18); services (personal, social and community,18); manufacturing/repairs (6); other (wholesalers, construction, transport etc) (8). Substitution was allowed after consultation with the researchers.

In total, 301 questionnaires were completed. This figure correlates closely with the 300 questionnaires initially planned for the survey. Limited divergence occurred from the initial 50 questionnaires planned in area, with numbers ranging from 59 in Tembisa to 51 in Soshanguve/Mabopabne and Johannesburg CBD.

The processing of data, ranging from checking to coding, data capturing and analysis was undertaken by the Bureau of Market Research of the University of South Africa.



The analysis is based on the following problem areas by SMEs: macroenvironmental, marketing-related, social, human resources and financial. It also covers management views on perceived success and the application of management actions.

Prior to a presentation of the results of the survey, it is in order to profile the survey population. This will establish the background against which responses on issues influencing the success of businesses should be interpreted.

The survey population portrays the following characteristics:

- Businesses with a reasonable level of sophistication were included in the sample. Only businesses operating from demarcated business premises, occupying a permanent structure and compiling an annual budget were selected.
- Only business owners or managers were selected as respondents. Almost two thirds (64,5 %) of the respondents acted as managers or had owned their businesses for more than three years.
- One in every four (24,6 %) respondents had a formal management qualification or certificate.
- Exactly half (50,8 %) the businesses operated as sole ownership enterprises while the rest were partnerships (12,8 %), private companies (16,2 %) and close corporations (19,9 %).
- The average employment of respondent businesses amounted to 3,8 full-time employees in 2001.
- Almost four in every five businesses (79,1 %) reported a turnover of less than R500 000 for 2001. Only 7,1 % generated a turnover in excess of R1 million.
- Seven in every ten businesses (70,3 %) were owned or managed by Africans, 14,3 % by Asians, 4,0 % by coloureds and 11,3 % by whites.



- Two thirds of the questionnaires were completed in township areas and one third in the CBD areas of Pretoria and Johannesburg.

The above composition confirms that, although an effort was made to select a relatively sophisticated business sample, respondent businesses were generally small to medium enterprises, mainly owned or managed by Africans with the overwhelming majority located in township areas.

4 Findings

The findings of the research are discussed under the following headings, namely the macro environmental variables, marketing-related issues, management skills, management actions, social problems, human resource problems, financial problems and business success.

- *Macro environmental variables*

The macro environmental variables which exert the most marked influence on business success were crime, inflation, unemployment, interest rates and exchange rates. The percentages of businesses that agreed or strongly agreed in this regard are as follows:



Table 1 *Macroenvironmental variables*

	Strongly disagree	Disagree	Neutral Agree	Agree	Strongly agree	Total
Interest rates	3.7%	9.0%	16.1%	30.1%	41.1%	100
Exchange rates	4.0%	9.0%	20.4%	34.4%	32.1%	100
Inflation	2.7%	6.7%	14.0%	31.4%	45.2%	100
Unemployment	4.0%	6.0%	13.7%	27.1%	49.2%	100
Crime	4.3%	7.4%	6.4%	20.7%	61.2%	100
HIV/AIDS	18.1%	15.4%	38.3%	11.1%	17.1%	100
Changing techniques	20.8%	21.1%	18.5%	24.5%	15.1%	100
Government legislation	11.3%	20.3%	29.6%	21.3%	17.6%	100

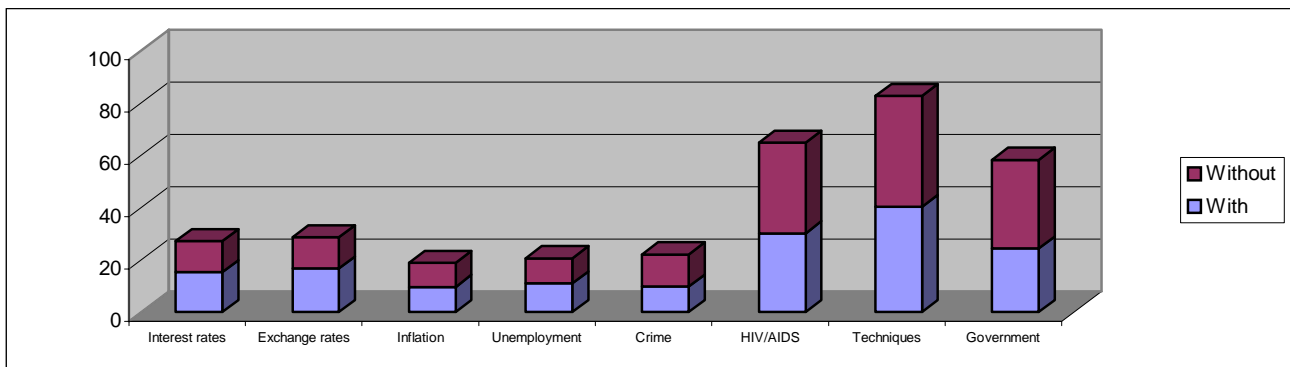
However, HIV/AIDS (28,2%), new government legislation (38,9%) and rapidly changing techniques (39,6%) are perceived as having the least influence on business success. Of particular importance regarding HIV/AIDS is the large percentage (38,3%) of respondents who remained neutral on the question, implying that they were still unsure what the possible future impact of HIV/AIDS would be.

The response regarding macro-environmental variables by respondents with and without management qualification indicated that those owners/managers with management qualifications are far less uncertain (neutral) about the perceived impact of macro-environmental factors on the success of their business. They also tend to be more in agreement that variables such as high interest rates, inflation, crime, HIV/AIDS and new government legislation would negatively impact on the success of their businesses.



This is illustrated in graph 1.

Graph 1 Macro environmental variables



- ***Marketing-related issues***

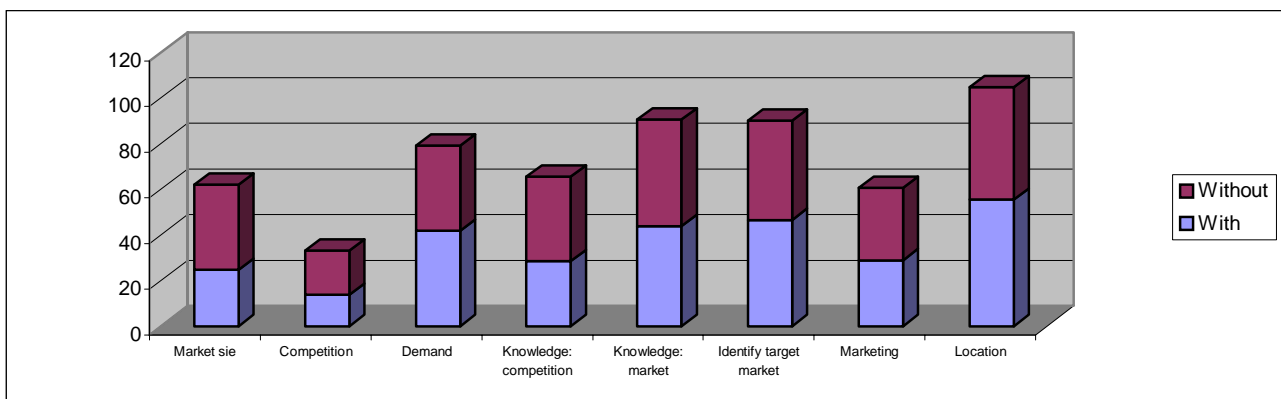
The response to the market-related issues having a negative influence on the success of the business, indicated that increased competition was the major marketing related issue faced by the respondent businesses, as 68,4% agreed or strongly agreed with this. Increased competition is also the single factors with the highest percentage of ‘strongly agree’ responses. With regard to the low demand for product, 43,5% regarded it as a big problem. This corroborates the literature that new competitors and insufficient demand are common problems.

The responses to the marketing-related issues with a negative influence on the business, showed little divergence in the perceptions of those with and those without management qualifications regarding the influence of the different issues on the success of their businesses. Respondents with management qualifications tend to be more in agreement with the negative impact of increased competition, lack of knowledge of competitors and ineffective marketing on the success of their businesses. This may



suggest that better insight into marketing-related issues is an important factor for business success. This is illustrated in graph 2.

Graph 2 *Marketing-related issues*



- **Management skills**

The majority of the respondents did not see management training as lacking and thus negatively influencing their businesses. This reaction was also experienced in similar studies and is explained as a form of response bias where respondents seek social approval in the eyes of the interviewer (Lighthelm & Cant, 2002: 24). A further possible reason for the survey result was that the screening question only allowed the inclusion of businesses that compiled annual financial statements. Budgeting implies activities such as planning and prioritising, suggesting that respondents already exercise some important business management function. They may, therefore, not regard management skills as lacking in their businesses. A further factor that should be considered when interpreting the response is that almost half those with management qualifications possess only a basic business



certificate. Only a small percentage (15,5 %) of the sample obtained a formal tertiary degree/diploma in business management.

Although the majority of respondents with and without a formal management qualification maintain the view that business skills are not lacking in their businesses, a larger percentage of those without management qualifications agreed that the lack of management training and skills impacted negatively on the success of their businesses.

- ***Management actions***

The lack of management skills does not present a serious problem to the success of businesses. Management actions, as described in the questionnaire, generally refer to the tasks of planning, organising, leading, coordinating and control. The respondents confirmed the importance of implementing effective management functions as a means of improving the success of SMEs.

The majority of business actions identified in the questionnaire are perceived by respondents as important for ensuring business success. The percentage of businesses in agreement (agree and strongly agree) with the various management actions are as follows:

	% agree and strongly agree
Change is an integral part of running a business	81,3
Failure is a valuable learning experience	72,7
Time is spent more effectively if I plan better	71,9
Involve employees in planning and decision making	68,4
Set time apart to plan and prioritise	68,0
Prefer to do most of the work to be in control of business	60,9



The management actions that elicited the least agreement from the respondents were:

	% agree and strongly agree
I neglect planning due to time pressure	24,4
Long-term goals are not meaningful	33,2
Daily routine tasks tend to take up most of my time	48,5

The latter statements largely confirm the importance attached by respondents to effective management actions as a means of ensuring sustainable business operations.

In line with previous results, respondents in the possession of management qualifications constantly attached greater priority to the execution of management actions such as effective planning, organising, leading and control. The importance of this finding is that it affirms that management training not only transfers management skills to learners but also reinforces the lateral perception that the application of skills contributes to business success.

- ***Social problems***

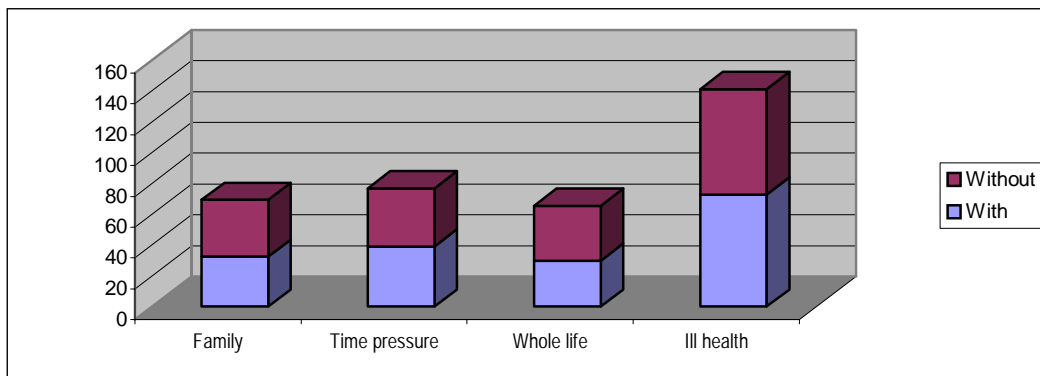
Social issues refer to the problems experienced by SME owners, where work tends to consume their personal life. Long hours spent at work place pressure on relationships with family members and friends. Pressure stems mainly from the dual roles that have to be performed by many owners as both diligent income providers and caring spouses.



Half the respondents indicated that too much time is spent at work (50,7 % agreed or strongly agreed), that the business has a detrimental effect on social/family life (45,7 %) and that the business consumes the business owner/manager's whole life (44,3 %). The fact that sizeable percentages of respondents (approximately one in every three) complained about the above issues is a matter of concern.

Slightly fewer respondents in possession of a management qualification suffered from a negative impact of their business activities on their family/social life. This is illustrated in graph 3.

Graph 3 Social issues



- **Human resource problems**

The human resource problem category reflected the extent to which SME owners experienced certain human resource issues as negatively influencing the success of their businesses. Generally, human resource issues are not regarded by respondents as a serious problem jeopardising the profitability of their businesses. The two most serious human resource problems, mentioned by approximately one in every three respondents (ie those who 'agree' and 'strongly agree' with the statements) were the



introduction of the new labour laws (35,6 %) and the inability to attract and find suitable staff (32,6 %). Least important of the human resource issues are poor labour relations (19,8 %), poor staff planning (20,6 %), high labour turnover (22,8 %), poorly trained employees (25,4 %) and low labour productivity (26,7 %).

The impact of human resource problems is more severe in businesses managed or owned by persons without management experience. Between 4 % and 6 % more businesses managed/owned by persons without management qualifications indicated human resource problems as a cause for failure. The largest divergence is in issues such as staff planning, labour relations and inability to appoint suitable staff.

- ***Financial problems***

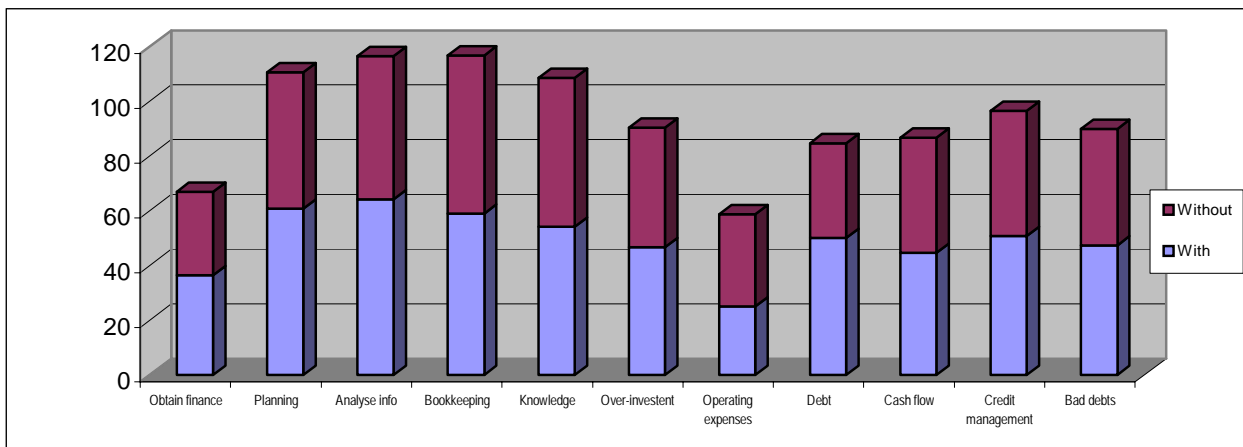
Financial problems having the most widespread impact were difficulty in obtaining finance/credit (53,9 % respondents 'agree' or 'strongly agree') followed by heavy operating expenses (51,8 %). As highlighted in literature, the granting of consumer credit also presents significant challenges for small businesses. No less than 41,8 % 'agree' or 'strongly agree' that bad debts pose a serious problem to their businesses. The following financial problems were highlighted as the least serious problems (mentioned by approximately one in every four businesses): overinvestment in inventories (22,2 %) and failure to analyse financial information (23,2 %). Problems agreed upon by approximately one in every three respondents were: inadequate credit management (28,2 %), insufficient knowledge of bookkeeping (29,2 %), failure to do financial planning (30,7 %) and poor cash flow management (34,8 %). In general the above shows that apart from obtaining finance and the burden of heavy operating



expenses, less than half the respondents reported a negative influence of other financial problems on their business success.

Interesting enough, owners/managers with a management qualification experienced fewer financial problems than those without management qualifications. However, with regard to some issues, such as the burden of heavy operating expenses and insufficient knowledge of bookkeeping, respondents without qualifications reported a less severe impact. This is illustrated in graph 4.

Graph 4 *Financial issues*



- ***Business success***

Selected items were used to establish whether small business owners perceived their businesses as being successful. Respondents were requested to indicate how they view their small businesses in terms of growth in turnover, profits and employees. In general, almost half the owners were of the opinion



(‘agree’ or ‘strongly agree’) that their businesses are successful in terms of turnover and profits. Just more than a quarter of businesses (28,7 %) indicated success in terms of additional employment.

A slightly higher success rate in businesses with owners/managers possessing management qualifications compared with those without. Half the owners/managers with management qualifications rate their businesses as very successful compared to 48,0 % without management qualifications.

5 Conclusion

The SME sector plays a very important role in South African economy in terms of its contribution to economic growth and job creation. The sample population, consisting of relatively small yet sophisticated businesses in township and CBD areas in Gauteng, emphasised that the following issues are of particular concern for the success of their businesses:

- inflation and interest rates,
- increased competition,
- crime and unemployment,
- regulatory and technological change,
- social pressure from family and friends, and
- credit management, heavy operating expenses and burdensome debt.



The respondents confirm that they regard all management functions as important for the success of their businesses. Slight variation was detected in the importance attached to issues. Marketing-related issues are singled out as the most important for business success, followed closely by financial issues, general management actions and lastly the impact of macro-environmental aspects on business activities. Furthermore, it became evident that managers or owners with some sort of qualification did not perceived aspects in the environment as threatening as managers without qualifications. Also, managers with some sort of qualification seemed to utilise opportunities more so than managers without some sort of qualification.

6 Recommendations

Training programmes in business management and entrepreneurship should endeavour to accommodate the above issues in their syllabi. Addressing the various issues in general in training material is not sufficient. The contents should be focused on the specific problems experienced by SMEs and allow for the practical application of concepts and procedures. This is the challenge for management and entrepreneurship training.



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