

EURASIAN JOURNAL OF SOCIAL SCIENCES

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CHALLENGES FACING SMALL TO MEDIUM ENTERPRISES IN METSIMAHOLO MUNICIPALITY, SOUTH AFRICA

Jeremiah Madzimure

Corresponding Author: Vaal University of Technology, South Africa
Email: jeremiahm@vut.ac.za

Lebereko Phillip Tau

MANCOSA College, South Africa
Email: phillip.lepena@telkomsa.net

Received: February 11, 2021

Accepted: March 27, 2021

Abstract

In South Africa, the failure rate of Small to Medium Enterprises (SMEs) amounts to 75% in an estimated interval of 42 months of operation. The purpose of this study is to determine the challenges facing SMEs in Metsimaholo municipality, Free State province of South Africa. Quantitative data was acquired from 102 Metsimaholo SME owners or their representatives, utilizing questionnaires which were completed, returned, and analyzed using Statistical Package for the Social Sciences (SPSS) version 26.0 software. It was then established that economic factors have realistic control on the sustainability of SMEs. In addition, further development of SMEs is restrained by competition from immigrant businesses, transportation of inventory, inadequate management skills, substandard marketing, miserable manipulation of financial activities and business, unreachable loans. Notwithstanding the afore-said outcome, SMEs must carefully look at obtaining business skills coaching and support, enlarge or vary the range of products, put back any profits made by a business into it in order to make it more successful. Cooperation amongst SMEs would be a strategy for them to challenge rivalry. Therefore, SMEs will bargain from transportation of goods bought in large quantities for a unit price that is lower than usual.

Keywords: Challenges, Failure Rate, SMEs, Municipality, South Africa

1. Introduction

Unemployment is a source of serious trouble to majority of South Africans families in black communities as they felt abandoned and extremely devastated. Consequently, the country is faced with 32.5% of unemployment in the last quarter of 2020 (Bowmaker-Falconer, 2020). With the hope of redressing that scourge and/or curse, Small to Medium Enterprises (SMEs), especially in the informal sectors of the country, was identified and backed-up by the South African government. South African government focused on programs that ensured productiveness of SMEs, the Department of Small Businesses ran a research plan wherein, important business skills and infrastructure was shared (Mukwarami and Tengeh, 2017).

However, the level of illiteracy and lack of business, financial and network management skills amongst the SME owners and their representatives excluded majority of black informal small business owners from participating in the mainstream of the economy.

Therefore, the objective of this study is to determine the challenges facing SMEs in Metsimaholo municipality, Free State. This municipality area was selected for this study because it is regarded as one of the worst performing municipalities in South Africa. Views from other researchers have established the following: SMEs were viewed as catalysts and engines of economic growth including generation of employment, but lacked financial planning, limited access to funding, lack of capital, low financial and strategic projections attributed to failure of SMEs (Taiwo, 2019; Lamb *et al.* 2019). SMEs that were resource constrained suffered a liability of compactness (Musawa and Ahmed, 2019). On the other hand, the performance and success of SMEs were ascribed to start-up planning, financial support, networking, and government support (Tan *et al.* 2019). Marketing skills included the capability of identifying new ideas, effective methods of advertising, new ideas capabilities signified a successful SME in the long term (Ramli and Razali, 2019).

SMEs were understood as a gateway to economic freedom where the historically handicapped number of people were left behind and were not part of formal or mainstream economy due to racially designed policies of the apartheid regime (Lamb *et al.* 2019). SMEs such as township spaza shops, added value in the township economic growth and local consumer spending. The Department of Small Businesses also invested millions of rand on projects focused at improving and re-establishing SMEs, but the development, continued existence of Metsimaholo municipality SMEs remained unconvincing, while the opposing businesses were increasingly controlling the marketing spaces and buying over businesses from them. Informal businesses in the region of 50% were foreign run businesses (Lamb *et al.* 2019). Majority of the SMEs in Metsimaholo municipality were run by immigrants due to good quality service, creation of a brand that local customers associated with and customer service.

SMEs are capacitated to significantly reduce a high number of joblessness and positively improved growth in own country's economy. SMEs in Rwanda were responsible for 98% of all businesses and employed almost all the private sector (Douglas *et al.* 2017). In South Africa, SMEs employed 68% of the population wherein not all SMEs attained their full capacity and growth while others failed in total (Douglas *et al.* 2017). SMEs are owner managed and small which created a challenge and/or threat (Ismail and Alam, 2019). SME's potential and growth were related to a prosperous product market-strategy, the ability to generate and utilize market opportunities while coping with challenges and greater tendency to compete on price (Masama and Bruwer, 2018).

Metsimaholo municipality experienced a high level of SMEs who either failed and others could not perform optimally and/or profitably, the research study was conducted to identify those critical factors that contributed to such failures and a remedy was established. As an alternative, Metsimaholo SMEs could have obtained gains if business owners collaborated with competitors in fighting the common challenges jointly with the sole aim of achieving competitive advantage and building alliance leading to shared ideas, knowledge, and skills. This study contributes to the gap in the literature on this topic by exploring challenges facing SMEs in South Africa as well as their contribution to the economy. The next section discusses the literature related to this study.

2. Literature review

South African National and Provincial governments employed regulations and policies aimed at supporting the SMEs sector, however, the small businesses experienced challenges regarding their organization and was maintained at a certain level. This perspective was endorsed by a local research project, which purported that 63% of SMEs failed in the initial 18 months of doing business (Mukwarami and Tengeh, 2017; Masama and Bruwer, 2018). In addition to the aforementioned, previous and local research projects traversed disputes or issues that had to do with SMEs broadly.

SMEs experienced challenges during start-up and were faced with this reality to date due to discriminatory regulations, which stopped and prevented black majority opportunities of learning including way into funds or assets (Mukwarami and Tengeh, 2017). Therefore, the legally mandated system of racialized segregation and discrimination resulted in majority of illiterate unskilled black people. SMEs were mostly short lived because of insufficient knowledge of taking risks, ill-advised fund capacity, wrong business positioning, bad marketing practices, poor implementation of internal controls, business plans lacked quality, inadequate market knowledge (Ndikubwimani, 2016; Golbahram and Chetty, 2018).

Given the recognition of Covid 2019, that is an illness produced by latest exertion of coronavirus in Wuhan China, had scrubbed beyond Europe, America and currently in Africa. It created destruction to lives and economy of countries, many human beings, suddenly passed away and others lost their remuneration entirely, the outbreak regulations were employed to lessen human activities and assembling of individuals in groups (Mukwarami *et al.* 2018). Covid-19 regulations also inflicted heavily on human being's commodities and companies, impacted lives and no rehabilitation or recourse was realized (Bruwer and Van Den Berg, 2017).

SMEs and informal businesses experienced difficulties when accessing funding from financial institutions as they did not meet the set criteria including evidence of good savings behavior and/or collateral resulted in no access to bank loans. SME owners in most cases lacked specialized knowledge of drafting sound business plan articulating their business requirements to financial institutions (Mukwarami and Tengeh, 2017; Bruwer and Van Den Berg, 2017). SMEs were exposed to financial pressures that incorporated lack of knowledge about the way to obtain funding, repressive borrowing tendered by commercial banks, under-banked, failed to receive the required finance, deficient financial documents that were needed by banking institutions and other reasons including banking institutions didn't have suitable layout or form of business transaction with SMEs (Ramli and Razali, 2019; Ndikubwimana, 2016; Nainer and Masson, 2018).

The expansion and survival of an SME was dependent on the owner's business skills and in the absence of those business skills, SME owners found it difficult and could not cope with growth demands (Mukwarami *et al.* 2018). Inadequate managerial skills and ability, individual attributes, poor state of economic, badly executed business plans were understood to be the course for start-up failure (Bamata *et al.* 2019). Failure of SMEs was mainly contributed by insufficient business knowledge and qualifications including poor personal training and development of bad treatment of clients (Rattanapongpinyo, 2018).

Relevant and appropriate business and leadership skills were highly required by SME owners to assist business leaders including employees in making quick and informed decisions rose above mediocracy and drove SME growth (Zondo, 2016). A significant number of SMEs originated from poor coursework backdrop rendering them unfit to control leadership roles such as organizing, staffing, directing, and controlling (Ramli and Razali, 2019). SMEs with managers who lacked skills and exposure constantly earned negative profits and lost market share to such an extent that they were likely to go out of business (Ramli and Razali, 2019). Professional experience acquired through work experience was all most nearly a significant outcome having a huge effect on many SMEs (Ramli and Razali, 2019). The activity of directly or indirectly managing certain activities was the most significant element in stimulating SMEs execution and results (Ramli and Razali, 2019).

Growth and success of SMEs was dependent on business networks, which ensured the platform for business owners to collaborate, share resources and information (Mukwarami and Tengeh, 2017). With healthy business networks, SME owners benefited from trustworthy counterparts, distribution of goods and services that resulted in expansion and growth of the businesses (Mukwarami and Tengeh, 2017). Social capital was understood to be the origin of sustainable competitive advantage and a scarce, important, imitable resource giving rise to different social networks and varying relationships (Lip Teh *et al.* 2018). It was learned from foreign owned businesses including Somali shops who utilized business networks to benefit from bulk purchases (Mukwarami *et al.* 2018).

Financial literacy constituted a risk, as most SME owners did not realize the significance of keeping accounting records. As a result, this behavior inhibited business owners from

securing and/or acquiring financial support from the financial institutions who always expected businesses to be financially accountable, proven by well-documented accounting records (Tengeh and Mukwarami, 2017). The ability of analyzing money, investments and the related systems were critical in the on-going success and growth of an SME and top of the mentioned expertise was the capability to clarify financial information including assets, liabilities, equities income and expenses and cash flow (Bamata *et al.* 2019). Management of finance was a relevant and/or a suitable way, which increased SMEs profitability assuming that business associated it as less important to the management accounting function of coordination, control and accountability (Lip Teh *et al.* 2018). Financial resources were used profitably to achieve a highly successful business (Lip Teh *et al.* 2018). Loss of production and revenue in SMEs was influenced by owner or leadership's inadequate management of funds and financial results, shortage of funds, misunderstanding the chosen business and insufficient allocation of business operating hours (Mbatha and Ngibe, 2018; Masocha *et al.* 2017). The next section is the research methodology undertaken for this study.

3. Research methodology

A quantitative approach was adopted mainly to show the significant role of quantitative research position regarding gathering and measuring information on variables of interest which was measured and put through statistical methods to endorse or invalidate and process it for studying purposes (Tengeh and Mukwarami, 2017; Al-Ababneh, 2020). Consequently, the questionnaire was conducted via non-probability in the form convenience sampling and was directed to SME owners or managers in Metsimaholo municipality, quantitative data accumulated was analyzed individually utilizing Statistical Packages for Social Sciences (SPSS) version 26 software (Tengeh and Mukwarami, 2017).

Data were collected from SME owners across Free State province, which was the unit of analysis. This municipality area was selected for this study because it is regarded as one of the worst performing municipalities. A total of 150 questionnaires were distributed of which 138 were returned and 102 were usable representing exactly a 68% response rate, which was considered reasonable for quantitative studies (Tengeh and Mukwarami, 2017). The questionnaires were self-administered by the two authors of this paper during the period of three months from February to April 2020. A total number of 13 questions constituted the questionnaire. All ethical practices were followed prior to conducting the study such as no respondent was forced to complete the questionnaire, there were also asked to withdraw anytime they feel so and they were told this study was not harmful in anyway. Lastly, they were told the data they provide would not be shared by third parties unless they agreed to do so. The next section is the results or findings of this study.

4. Research findings

This section includes the participants feedback collected from Metsimaholo SME owners or their representatives that was numerated, examined methodically and in detail.

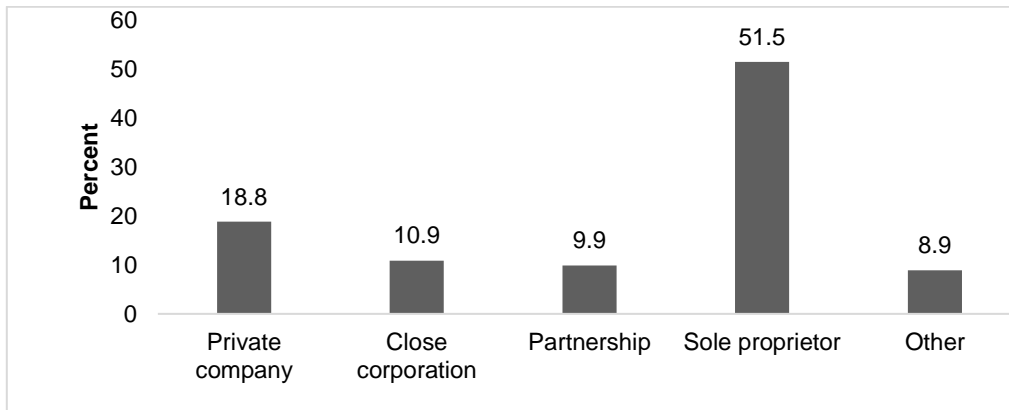


Figure 1. Legal status of a business

Figure 1 reflects a majority legal status of 51.5% by respondents, which is favored mostly by African business owners who prefers exclusive business ownership which in turn results in poor business network as narrated in the literature review.

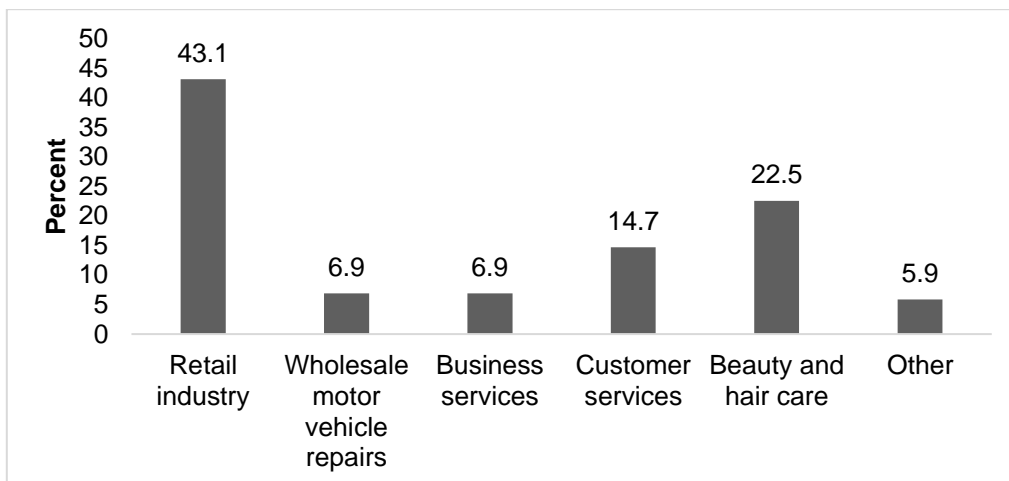


Figure 2. Sector of SME

According to Figure 2, retail industry appeared to be sought-after or desired by the respondents in Metsimaholo municipality followed by beauty and hair care. With the believe of addressing joblessness, hunger, poverty spaza shops classified retail business at a small scale and hair salons were resorted to as a means of survival amongst South African communities.

Table 1. Number of SME employees

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	1. Less than 5 people	72	70.6	70.6	70.6
	2. 5 to 20 people	26	25.5	25.5	96.1
	3. 21 to 50 people	4	3.9	3.9	100.0
	Total	102	100.0	100.0	

Table 1 is a reflection by respondents that 72% of SMEs in Metsimaholo municipality employ less than 5 people and can therefore be understood to be informal or mostly very small. It further attests to literature reviews that small to medium enterprises are mainly unsustainable and risk chances of failing at early stages of their operation (Golbahram and Chetty, 2018).

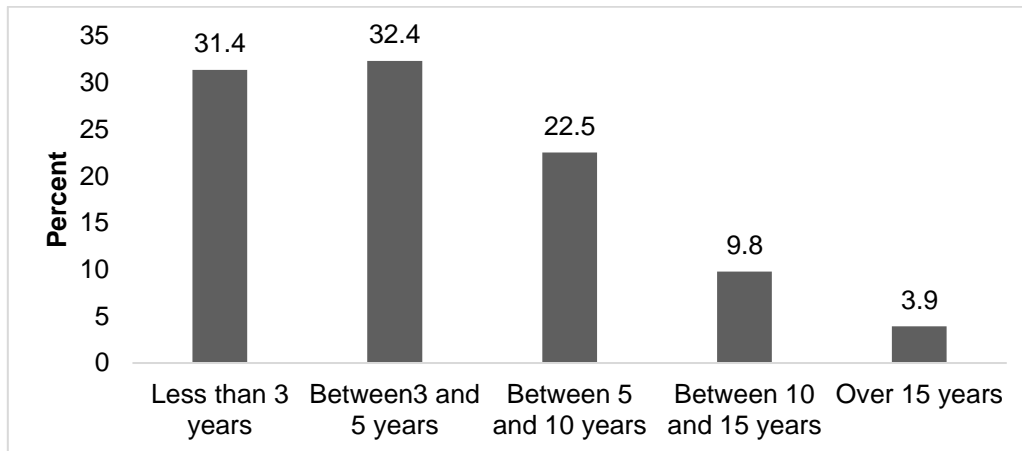


Figure 3. Business operation in years

According to Figure 3, 32% of SMEs revealed between 3 to 5 years in business operation. These SMEs still have to stand the test of time over the years going forward, attested to this is the fact that the business owners are required to perform all business functions alone including leadership, marketing, strong personal networks, financials, human resources, suitable business planning and face competition head-on. The trend of graphs in Figure 3 slopes from 32.4% to 3.9% for the period of between 3 – 15 years, which implies that most SMEs failed or closed business.

Table 2. Racial status

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	1 African	98	96.1	96.1	96.1
	2 Asian	1	1.0	1.0	97.1
	3 Colored	1	1.0	1.0	98.0
	4 White	2	2.0	2.0	100.0
	Total	102	100.0	100.0	

Table 2 reveals that 96.1% of the respondents were Africans. The rationale behind this information revealed above, should be mainly due to unemployment rate surrounding black South African and as a result, majority of black people resort to informal, small to medium enterprises as a means of survival, and also resulting in a noteworthy reduction of unemployment, and positively enhancing business growth, top line or revenue.

Table 3. Role in the business

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	1 Owner	43	42.2	42.2	42.2
	2 Manager	16	15.7	15.7	57.8
	3 Both	38	37.3	37.3	95.1
	4 Other	5	4.9	4.9	100.0
	Total	102	100.0	100.0	

Notwithstanding previous literature reviews from other researchers, the respondents further attested to the fact that Metsimaholo municipality SMEs in most cases carry dual responsibility of being both manager and owner, which is in the region of 42.2% to 37.3%. The afore-mentioned details or percentage in Table 3 further testifies that SME owners fill more roles at once than is realistically possible

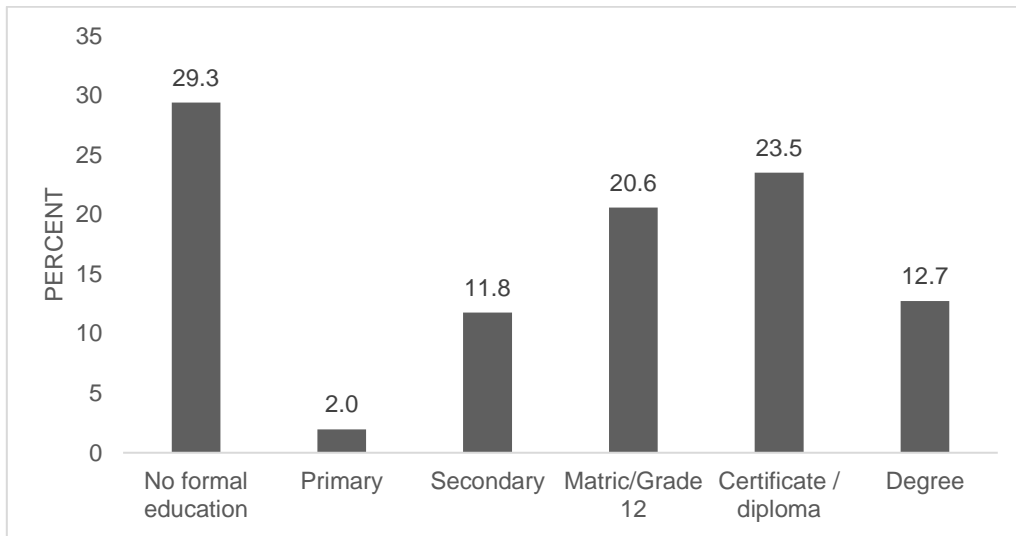


Figure 4. Level of education

Figure 4 referred to herein and as testified by the respondents, indicated that 29.4% of SME owners/managers had no formal education. This implies that continuous business improvement and other training including better business planning, the know-how on to formally talk recently discovered markets and clients, capacity on how to increase business revenue.

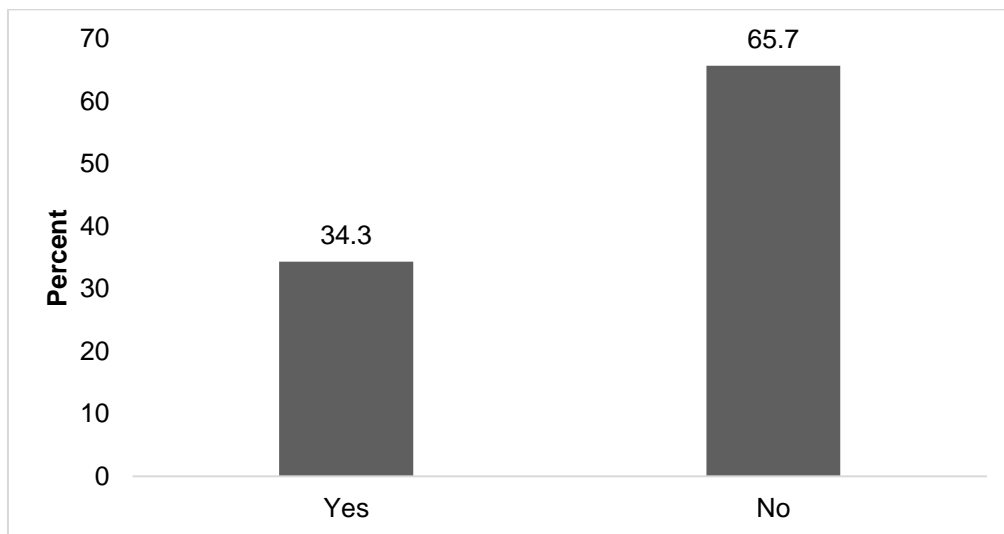


Figure 5. Do you outsource?

In Figure 5, the respondents of Metsimaholo municipality SMEs favoured not to outsource all business functions as detailed hereto below. The rationale behind SMEs for not outsourcing business function should be due to the respondent's businesses range from informal businesses to small and medium enterprises. As highlighted by literature in this study, these enterprises were founded in black townships, the respondents chose none outsourcing of business functions as follows: accounting 90.2%, human resources 99%, IT 97.1%, marketing 94.1% and other 94.1%. The analysis hereto above denotes that SMEs could not afford outsourcing the stated business functions either due to SME size or capacity based on revenue that they generate.

Access to finance remains crucial in a business environment as it attracts growth opportunities and also strengthens competition, this means if an enterprise has an added advantage of access to capital, SME owners will meet the customer needs competitively at

reasonable pricing. The respondent's choice wherein majority confirmed or agreed to the fact that competition poses a major challenge that troubles SMEs in Metsimaholo municipality. Although the respondents chose none in other questions, theory presented in the literature review of this study recapitulate that customer's ever changing needs and expectations give rise to amendments to competitive standards together with technological innovations (Tengeh and Mukwarami, 2017; Shamilee and Hoque, 2016). A high number of SMEs in Metsimaholo municipality continue to be successfully and competitively operated by non-South Africans due to good quality service, and brands, which clients could identify with. Over and above, the challenges of access to finance and competition from non-South Africans come out very strongly from the respondents. Previous literature has also found related results pertaining to this study (Bowmaker-Falconer, 2020; Douglas *et al.* 2017; Makhitha, 2017; Shamilee and Hoque, 2016; Utami *et al.* 2019; Mathu and Tlare, 2017; Tan *et al.* 2019). The last part of this article is the conclusion and recommendations.

5. Conclusion and recommendations

The purpose of the study was to investigate the challenges of small to medium enterprises in Metsimaholo Municipality, Free State province of South Africa. For these SMEs to be sustainable and generate profit, SME owners should be encouraged to collaborate with competitors to jointly tackle common problems and therefore achieve knowledge and skills to outperform in their roles.

The research was limited to the challenges of SMEs in one municipality in Free State province of South Africa. For purposes of future investigation, it will be beneficial if other municipalities are included for better results that will assist the province and or the country at large. The existing period of Covid -19 pandemic and lockdown levels posed a serious impact not only to the researchers but to the investigation in general.

Although several respondents indicated that their qualifications are post grade twelve, it will be beneficial for the SME owners and managers to impart knowledge and share the acquired business skills with their subordinates. Metsimaholo SME owners may also improve business relationship and networks with immigrant competitors and as a result learn better ways of being profitable.

Based on the fact that Covid-19 had a serious impact on the economy both locally and globally, destroying livelihoods, disrupting individual's lives and businesses, therefore future researchers still have a major task of ensuring that SMEs remain active, provide jobs and reduce high levels of unemployment.

SMEs will remain critical even in future due to their nature of absorbing the unemployed if managed correctly - it means future investigators will have to critically focus on initiatives that will caution SME owners from failing. Emphasis should be on further trainings on competition, rapid technology changes, market characteristics, financial management and customer focus.

Acknowledgements: The authors would like to thank all respondents for this research study.

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