

**THE INTERNAL AND EXTERNAL ENVIRONMENT  
FOR SMALL BUSINESS GROWTH IN  
PIETERMARITZBURG**

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## **EXECUTIVE SUMMARY**

This study investigated the internal and external constraints facing small business owners in the Pietermaritzburg (PMB) region. An attempt was further made to determine: whether the internal constraints or external factors constitute a greater burden on growth; whether policy focus should concentrate more on the internal constraints or external factors and determine the association between average growth (in terms of the number of employees) and the educational level and training of the owner/ manager, gender, ethnicity, business activity, legal status of the business and sources of start-up capital. Knowledge of the relative role of personal and environmental factors of this study in bringing about growth and expansion provides directions for government policy on Small and Medium Enterprise (SME) development.

By means of factor analysis the numerous internal and external environmental variables affecting business growth in PMB were reduced to a set of three factors, classified as management, financial and external. Collectively they accounted for 59.21% of the total variance of the model. The internal factors (management and finance) accounted for 48.95% of variance and it was concluded that internal factors are more burdensome to growth than external factors. As a result government support should focus more on the internal constraints facing the small business sector.

Further, multiple regression analysis was used to arrive at a parsimonious model that 'best' explained the regression model which accounted for 45.4% of variance with average growth. Average growth, in terms of the number of employees, was found to be a function of, the level of education of the owner / manager, legal status of the business, source of start-up capital, exposure to training and business support.

Internal factors such as obtaining finance, cash flow, recruiting and retaining staff, shortage of managerial skills / business expertise and lack of financial understanding prevent growth of the business. External factors such as the economy, taxation, regulation and laws, technology, competition, lack of business support and crime were found to inhibit the growth of the business.

A significant difference was found to exist between average growth and gender, legal status, business activity, source of start-up capital and the educational level and training of the entrepreneur/owner. These results also have implications for the management of the SME's as well as business networks such as the Chamber of Commerce and financial institutions.

### DECLARATION

I, Morgantheran Kumaruguru Pillay, hereby declare that the contents of this dissertation are my own work, and that all sources utilised, have been accurately reported and acknowledged. This dissertation has not, nor is submitted for any degree / examination at any university.

Signed: 

Date: 10/10/2026

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## **CHAPTER ONE**

### **INTRODUCTION**

#### **1.1 Background**

Small, medium and micro-enterprises (SMMEs) represent an important vehicle to address the challenges of job creation, economic growth and equity in our country. Throughout the world, one finds that SMMEs are playing a critical role in absorbing labour, penetrating new markets and generally expanding economies in creative and innovative ways (Horton *et al*, 2000: 1). At the heart of the small business is the entrepreneur / owner / manager. Since 1994 the government has devoted considerable resources to support small enterprises. However, Storey (1994: 79) states that the failure rate of the small business is large. Therefore knowledge of the relative role of personal and environmental factors in bringing about growth and expansion is important for boosting the SMME sector as well as to the field of entrepreneurship.

By conducting this study, the researcher provides evidence on the links between the external and internal environments with respect to growth. Knowledge of the relative role of personal and environmental factors of this study in bringing about growth and expansion provides insights for government policy. This cross-sectional, quantitative and multivariate study utilises a questionnaire and the survey method to obtain data.

#### **1.2 Research Question**

The research question can be stated as follows: “What are the perceptions among Pietermaritzburg small business owners / entrepreneurs of the internal and external business environments with respect to the growth of their ventures.”

#### **1.3 Objectives**

To achieve the above the researcher has formulated the following primary objectives:

- To evaluate the internal environmental conditions that favour or constrain entrepreneurship and small business development in the Pietermaritzburg region.



- To evaluate the external environmental conditions that favour or constrain entrepreneurship and small business development in the Pietermaritzburg region.
- To investigate whether the internal or external set of factors constitute the greater burden on business growth.
- To examine whether policy on small business / entrepreneurship should focus more on the internal conditions or external factors.

#### **1.4 Overview**

Chapter Two begins by examining the term ‘entrepreneur’ and explaining the entrepreneurial process of entrepreneurship. It also links the concept of entrepreneurship to the Small Medium Enterprise (SME). The SME is defined in terms of this study and a brief history and nature of the small business sector is provided.

Chapter Three reviews the SME sector in South Africa and the factors that constrain the growth thereof. This is achieved by reviewing the various studies that have been conducted in South Africa. The chapter begins by examining the contribution made by the SME sector to employment and the Gross Domestic Product. Secondly, it highlights the main findings of the Global Entrepreneurship Monitor (GEM) reports on the state of entrepreneurship in South Africa, the salient findings of the Investment Climate Survey (ICS) and the findings of the Small Business Project’s (SBP): Counting the Cost of Red Tape. Finally, the chapter evaluates the economic climate of Pietermaritzburg, the site for this study.

Chapter Four evaluates the internal and external factors under investigation in this study. Specifically, the educational level and training of the entrepreneur / business owner, the economy, access to finance, taxation, regulation and laws, human resource practices, technology and innovation, lack of managerial skills and crime, are examined.

Chapter Five provides a clear and detailed description of the research design followed by the researcher in order to test the formulated hypotheses. It explains the research methodology, the units of analysis of the study, the instrument used for data collection, the statistical approaches

followed. Specifically, chi-square test, multiple regression analyses, factor analyses, analysis of variance (ANOVA) and univariate analyses were used.

Chapter Six presents the results of the data analyses.

Chapter Seven provides an in depth discussion of the results obtained.

Chapter Eight provides conclusions with reference to all the stated objectives.

Chapter Nine suggests recommendations on the 'optimal' environment for SME development in Pietermaritzburg.

Chapter Ten highlights the limitations of the research and provides directions for future research.

Chapter Eleven provides a final conclusion for the research.

## CHAPTER TWO

### THE ENTREPRENEURIAL PROCESS

#### 2.1 Introduction

An understanding of the terms entrepreneur, entrepreneurship and the process of entrepreneurship is vital in determining the resources, skills and management competencies required to start and grow a business venture (Fry *et al*, 2001: 13). The aim of this chapter therefore, is to examine the term 'entrepreneur', explain the entrepreneurial process and link the concept of entrepreneurship to the Small Medium Enterprise (SME). Such an approach reveals the skills, resources and management competencies required for business growth.

#### 2.2 Entrepreneur

A look at the vast array of research on entrepreneurs indicates that there is still no standard universally accepted definition of an entrepreneur. The definition used in a particular study is dependent on what one's intent is, or what one hopes to accomplish. For the purpose of this study, a compact definition of an entrepreneur provided by Pickle and Abrahamson (1990: 59), will be used :

*"An entrepreneur is one who organizes and manages a business undertaking, assuming the risk, for the sake of profit. The entrepreneur evaluates perceived opportunities and strives to make the decisions that will enable the business to realize sustained growth."*

#### 2.3 Entrepreneurship

From the viewpoint of growth-oriented innovative companies, one of the best definitions of entrepreneurship is found in Ronstadt (1984: 28):

*"Entrepreneurship is the dynamic process of creating incremental wealth. The wealth is created by individuals who assume the major risks in terms of equity, time and / or career commitment or provide value for some product or service. The product or service may or may not be new or unique but value must somehow be infused by the entrepreneur by receiving and allocating the necessary skills and resources."*

Central to this definition and those provided by other authors are the following characteristics that consistently appear.

**2.3.1 Creation process:** Entrepreneurs will identify an opportunity and then create a product or service, a process or something of value for some market (Hisrich and Peters, 2002: 10). Creativity, innovation and vision are fundamental traits required by entrepreneurs, argue Hodgetts and Kuratko (1998: 32). The entrepreneurial process begins with an entrepreneur's ability to identify an opportunity. The entrepreneur will creatively devise ways to bring this opportunity to fruition (Timmons, 1999: 38). The importance of creativity and innovation cannot be overemphasized. Glancey and McQuaid (2000: 9), advocate that it is imperative for entrepreneurs to be creative in the multiple areas of the entrepreneurial process if they are to achieve their growth-oriented goals. Therefore, constant environmental scanning is required.

**2.3.2 Acceptance of risks:** The process of bringing the identified opportunity to fruition has its own unique set of financial risks, personal risks and social risks. Timmons (1999: 27) argues that, although the entrepreneur should accept both personal and financial risks, what is important is that the odds are manipulated in the entrepreneur's favour by creatively and innovatively using the resources available. Glancey and McQuaid (2000: 6) stress that it is important for entrepreneurs to be able to calculate, manage and minimise the risks associated with the entrepreneurial venture. Hisrich and Peters (2002: 10) emphasise the importance of taking calculated risks that reduces the potential for failure.

**2.3.3 Rewards:** Entrepreneurs accept the risks, allocate the resources and create the product or service for a reward. These rewards may be in the form of profits by growth of the venture, independence or personal satisfaction (Hisrich and Peters, 2002: 10). Timmons (1999: 27) adds that entrepreneurs create, enhance and realise their rewards, not only for themselves but also for all the relevant stakeholders. The result of entrepreneurs accepting the risks and uncertainty of their new venture is that they receive the potential benefits (Glancey and McQuaid, 2000: 6).

**2.3.4 Resource allocation:** Entrepreneurs will draw on all available resources to realise the opportunities that they have recognised (Hisrich and Peters, 2002: 10). Entrepreneurs will allot

the necessary time, effort and resources in order to achieve their goals (Hodgetts and Kuratko, 1998: 32). Entrepreneurs will need to manage many resources, some of which are readily available and others that are very scarce. All of the resources will contribute to the success or failure of the new venture (Timmons, 1999: 39). Glancey and McQuaid (2000: 7), add that one of the skills associated with entrepreneurship is the ability of entrepreneurs to control, coordinate and manage the limited resources at their disposal in order to achieve sustained growth.

Closely associated with entrepreneurship are the small business and its management. However, the underlying difference is that entrepreneurs are innovators and creators of wealth businesses. Wickham (2000: 24) argues that, although entrepreneurial ventures and small business pursue the same objectives (growth and profitability), there are some fundamental differences between the two. Entrepreneurs are innovative and creators of new products or services, processes and technologies and have high growth potential. Entrepreneurial ventures are concerned with growth targets, market development and positioning.

Small businesses, on the other hand, operate with established products in established markets and are primarily concerned with sales and profits. It can be argued that in order to achieve high profit and sales, growth is a pre-requisite. Therefore, common to entrepreneurship and small business is the concept of growth. For the purposes of this study, both entrepreneurs and small business owner-managers are considered, as growth in both ventures is of equal importance.

The definition of entrepreneurship highlights the importance of the process that entrepreneurs / small business owners will follow to achieve their goals. This necessitates an explanation of the entrepreneurial process.

#### **2.4 The Entrepreneurial Process**

It is extensively documented that entrepreneurs will follow a process in order for them to achieve their goal of starting a new venture (Nieman and Bennet, 2002: 61, Hisrich and Peters, 2002: 38, Hodgetts and Kuratko, 1998: 46, and Timmons, 1999: 4). This process emphasises four distinct phases through which entrepreneurs will pass in order for them to start and manage their new venture. These phases are as follows:

#### **2.4.1 Identify and evaluate the opportunity**

Entrepreneurs will need to identify opportunities. These opportunities present themselves within the entrepreneur's environment and have to be evaluated based on its feasibility (market and financial feasibility) and viability. The decision to either start the new venture or to reject the possibility of implementing the opportunity must then be made (Nieman and Bennet, 2002: 61 and Hisrich and Peters, 2002: 40).

#### **2.4.2 Develop a business plan**

Developing a business plan is by far the most important aspect of the entrepreneurial process as it will assist the entrepreneur to understand the resources required, the risks involved and how best to manage the possible venture. The business plan includes plans for the marketing, finance, organisation and operations of the venture. The business plan provides the entrepreneur with a guideline or a plan for the future as well as an understanding of, the organisation, the environment and future decisions that might need to be made in respect of these (Nieman and Bennet, 2002: 62; Hisrich and Peters, 2002: 223 and Wickham, 2001: 190).

#### **2.4.3 Determining the resource requirements**

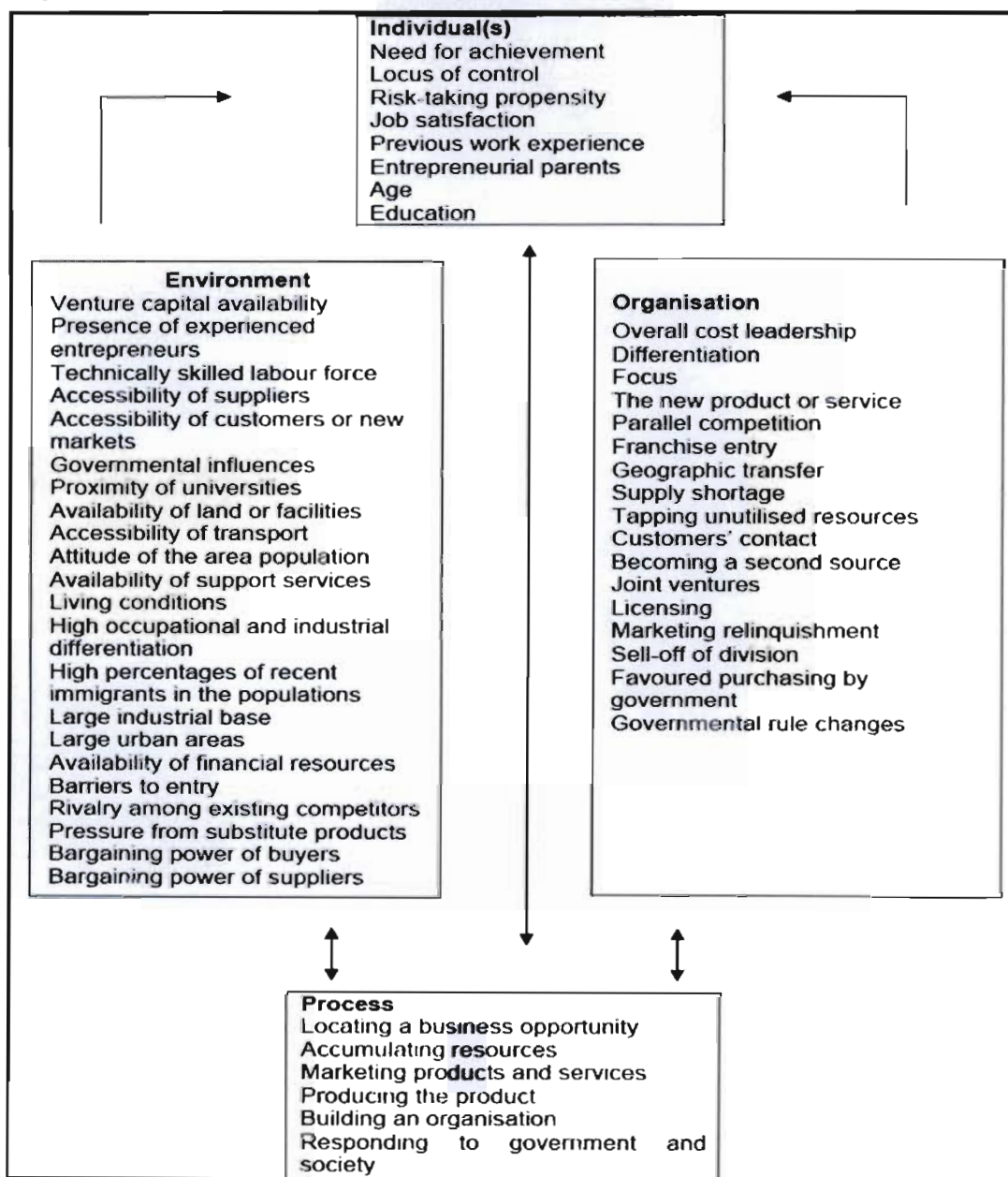
Entrepreneurs will need to establish the requirements for the new venture by ascertaining what resources are currently at their disposal, determining what resources are going to be needed, the time-frame within which these resources will be required and the human resource requirements. However, resources must be effectively managed as not all of these resources are required in the initial stages of the venture (Nieman and Bennet, 2002: 62 and Hisrich and Peters, 2002: 42).

#### **2.4.4. Start and manage the enterprise**

Once progress through the first three stages detailed above, has been accomplished, entrepreneurs will be ready to start the new venture. Entrepreneurs will implement their own management style, establish control systems and attempt to create an established business (Nieman and Bennet, 2002: 63 and Hisrich and Peters, 2002: 42). However, such a process approach is lacking in that it focuses mainly on the start-up of the venture. The focus of entrepreneurship should not be on venture start-up alone, but should also incorporate the individual, the environment and the venture. Gartner's multidimensional approach, as discussed in Kuratko and Welsch (1994: 7),

views the entrepreneurial process as a complex, multidimensional framework that comprises the entrepreneur, the environment and the organisation. This approach tries to identify most of the variables and influences that will impact on the creation of a new venture. Such a model is more applicable to this study as it incorporates the effect of the environments (internal and external) on the venture. The model is presented below.

Figure 2.1: A Multidimensional Entrepreneurial Process



Source : ( Kuratko and Welsch, 1994: 7).

The definition of entrepreneurship and the entrepreneurial process is now considered and a clear picture can emerge on the developmental stages of a business venture. As a business develops and grows, it will pass through several phases in its existence. Sullivan (2000: 164) has developed a life-cycle framework for small business, according to which an entrepreneurial venture will undergo. This framework consisting of five phases is discussed below:

## **2.5 The Business Life Cycle Framework**

### **2.5.1 Stage 1: Conception**

This initial stage involves the identification of an opportunity and the development of this opportunity. A business plan is developed and an assessment is made about whether to accept or reject the project. The entrepreneur starts the business and generates sales (Sullivan, 2000: 164). Other start-up activities, such as staff selection and legal considerations, will then be pursued (Nieman and Bennet, 2002: 64).

### **2.5.2 Stage 2: Survival**

The business breaks even and demonstrates its ability to operate at a very simple level, generating sales and cash flow and often showing signs of growth potential. Entrepreneurs normally have a very 'hands-on' approach (Nieman and Bennet, 2002: 64), to the conduct of their ventures.

### **2.5.3 Stage 3: Stabilisation**

The business venture can maintain its current levels, allowing the owner/manager to eliminate cash flow problems. The business can successfully remain in this stage if there is no major market or environmental changes. The entrepreneur's concerns focus on maintaining the business's current market base and will need to embrace the challenges of expanding that base (Sullivan, 2000: 164).

### **2.5.4 Stage 4: Growth**

The prevailing question at this stage is whether to grow the business. Entrepreneurs will try to obtain a larger share of the market resulting in increasing costs, which impacts on cash flow, on production and on the organisation as a whole. These changes will need to be successfully managed in order to meet the venture's new commitments. The business will need to reassess its



growth potential, as this will influence cash flow and other financial considerations (Churchill and Lewis, 1983: 40).

### **2.5.5 Stage 5: Maturity**

At this stage, the business venture needs to have financial controls, professional and skilled staff and well-developed systems (marketing and production) and resources. The business venture has the opportunity to develop further or it could risk stagnation and possible decline. To avoid decline, the business needs to be creative and innovative in order to develop new ideas to enable the business to maintain a competitive edge (Nieman and Bennet, 2002: 65).

From the above discussion it can be concluded that in order to start and successfully grow a business venture numerous skills are required. These skills are creativity and innovativeness, financial management, human resource management, generic management (planning, organising, leading and controlling) and strategic management skills (environmental scanning).

For the purposes of this study, two aspects of the statutory definition of Small, Micro, and Medium Enterprises (SMME's) will be used. The first is that SMME's are owner-managed and the terms entrepreneur / owner / manager will be used interchangeably as many of the skills of the owner / manager and the entrepreneur overlap.

The second deals with the definition of the small business. The definition of a 'small business' has been subject to considerable debate. The South African government (Government Gazette, 1995: 9) defines 'small business' as a separate and distinct business entity, managed by one owner or more. These businesses can be classified into micro-, very small-, small- or medium-sized businesses by satisfying certain criteria listed below:

- Ownership (organisational).
- Total full-time equivalent of paid employees (quantitative).
- Total annual turnover (quantitative).
- Total gross asset value (fixed property excluded) (quantitative).

This study is primarily concerned with the quantitative definition (number of employees) of the small business sector. However, this too is fraught with difficulty considering the changing labour market and the prevalence of practices, including sub-contracting, temporary employment contracts and part-time work. For the purposes of this study and the determination of the sampling frame, the small and medium enterprise (SME) is one that employs not more than 100 full time employees. The SME sector is managed by one or more owners and it is in this environment that entrepreneurs are likely to be found. It is, therefore, important that this study must consider the environment of the small and medium enterprise (SME) sector.

## **2.6 The Small and Medium Enterprise (SME)**

Small business has played a crucial role in history since the beginning of recorded time. It has flourished in almost all ancient cultures. The Arabs, Babylonians, Egyptians, Jews, Greeks, Phoenicians, and Romans excelled at it. It was largely through small business that civilisation was spread to all four corners of the then known world. Small business brought to the have-nots such things as Babylonian astronomy, Greek philosophy, the Jewish calendar, and the Roman law (Siropolis, 1994: 3).

During the 1980s and early 1990s, small business began to enjoy more esteem and prestige, no small thanks to its ability to invent new products and create new jobs. Even in times of recession, small businesses increased in numbers. Consequently, educators, journalists, and politicians alike now herald the achievements and opportunities, promise, and problems of small businesses (Siropolis, 1994: 3).

### **2.6.1 The Nature of SME's**

SME's are generally more labour intensive than larger businesses and on average generate more direct, and possibly also more indirect, job opportunities per unit of invested capital. In service industries the capital invested per job opportunity is even less (Cronje *et al*, 2000: 492). These authors further state, that SME's, are an instrument for utilising the talents, energy and entrepreneurship of individuals who cannot reach their full potential in larger organisations. SME's also serve as a breeding ground for entrepreneurial talent and a testing ground for new industries. The SME differs from large organisations in the following ways:

In many industries, small businesses can respond more quickly and at a lower cost than big businesses to the rate of change in products and services, processes and markets. This is due to its diminutive size as compared to the size of large corporate businesses (Siropolis, 1994:8). This characteristic according to Marx *et al* (1998: 731), keeps larger enterprises competitive.

Small business people tend to be mavericks, and extend the frontiers of knowledge. For example, General Electric, the world's largest electrical manufacturer, has credited small business with many of its product ideas, including the invention of electric toasters, refrigerators, dishwashers etc. Thus, their ingenuity enriches our lives (Siropolis, 1994: 8 and Marx *et al*, 1998: 730). However, the risks associated with SME's, develop the typical entrepreneurial characteristic of accepting those risks (Marx *et al*, 1998: 731).

The economy depends on small business for much more than invention and innovation. Small businesses employ a large number of people. They also sell most of the products made by big manufacturers to consumers. Small businesses also provide big businesses with many of the services, supplies, and raw materials they require (Siropolis, 1994: 9 and Marx *et al*, 1998: 731).

SME's are major creators of new jobs. Small business plays a very crucial role in the creation of new and often well-paid jobs in the economy. The secondary importance of this role is the contribution to GDP, as new employees will want to buy output with their salaries; this also means the Revenue Services will have more people to tax. It is important though to note, that as much as the small business is a creator of jobs, it is also the largest contributor to job losses, because their hiring reflects the state of the economy. Small businesses are the first to hire in times of economic recovery and the first to fire in times of economic downturn (Siropolis, 1994:10).

The SME can be found in all sectors of the economy, as entrepreneurs are opportunity seekers. Partly because of the low capital requirements, service businesses are the largest and fastest growing segment of the small business sector, mostly because the return relative to the inputs are higher in services. Also many young professionals have found that because of the so-called brain drain, their skills are increasingly in demand and they opt to form service consultancies and

companies instead of seeking employment and therefore are able to serve a wider market and further enhance their knowledge (Fry *et al*, 2001: 296).

A retail business sells products manufactured by other firms directly to consumers. In this sector small businesses favour specialty shops that let them focus their limited resources on a narrow market segment. Although manufacturing enterprises are usually large with access to the large amounts of capital required for equipment, energy and raw materials, small enterprises are also involved in this sector. They usually manufacture components, needed by big enterprises in their production and in some instances manufacture their own products that they sell directly to the consumer (Fry *et al*, 2001: 290). Therefore, SME's will predominate in these sectors.

Cited in Marx *et al* (1998: 732), is research conducted in the United States of America, on failure of the SME. Research shows that economic factors are responsible for 45% of failures and identifies inadequate sales, low profitability and weak growth prospects as being responsible. Financial factors such as insufficient capital and high operating costs account for 37.2% of failures. Lack of experience accounted for 10, 5% of failures and includes lack of managerial skills and business expertise.

Due to the high failure rate of SME's, Cronje *et al*, (2000: 497), suggest that governments in developing, strategies to promote the SME sector should include the following:

- The creation of an environment conducive to entrepreneurship and development of SME's.
- Mobilisation of financial resources to promote SME's through financial aid programmes.
- Provision of low-cost, affordable premises that may be leased or bought by SME's in areas where there are none at present.
- The upgrading of SME management skills and knowledge (training), and
- The establishment of appropriate professional support programmes.

## **2.7 Conclusion**

This chapter looked at the entrepreneur, the entrepreneurial process and the definitions of the SME and the nature thereof. It was found that the entrepreneur is an individual who is an opportunity seeker and a venture creator. He / she undertakes the creation of the venture following a logical process and accepts the risks and rewards thereof. The venture created undergoes different stages and at each stage resource requirements and the management role of the entrepreneur changes. The construct 'small business' was defined in terms of this study. The history and nature of the SME was briefly explained and finally a strategy to promote and combat the failure of SME's was provided. The following chapter analyses the SME sector in South Africa.

## CHAPTER THREE

### THE SME SECTOR IN SOUTH AFRICA

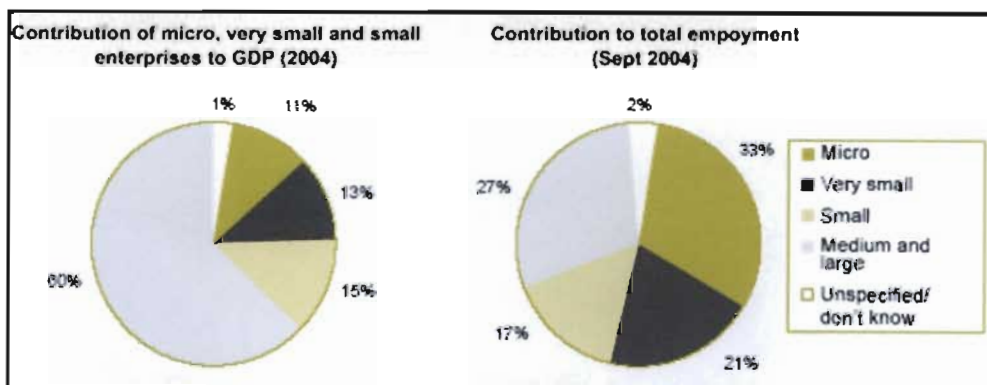
#### 3.1 Introduction

Given South Africa's legacy of big business domination, constrained competition and unequal distribution of income and wealth, the small business sector is seen as an important force to generate employment and more equitable income distribution, to activate competition, exploit niche markets (both internally and internationally), enhance productivity and technical change, and through all of this to stimulate economic development.

The aim of this chapter is to evaluate the SMME sector in South Africa with a view of determining the factors that constrain the growth thereof. This is achieved by reviewing various studies that have been conducted in South Africa. The chapter begins by looking at the contribution made by the SMME sector to employment and the Gross Domestic Product (GDP). Secondly, it highlights the main findings of the Global Entrepreneurship Monitor (GEM) reports on the state of entrepreneurship in South Africa, the salient findings of the Investment Climate Survey (ICS) and the findings of the Small Business Project's (SBP): Counting the Cost of Red Tape. Finally, the chapter will look at the economic climate of Pietermaritzburg, the site for this study.

#### 3.2 The Contributions of the SME Sector

Figure 3.1: Contribution of SMME's



Source: (Small Enterprise Development Agency, 2004: 66)

From the pie charts presented above, the importance of the SME sector cannot be disputed. The small business sector contributed 15% to the South African GDP and 17% to total employment in 2004. The importance of developing such a sector to facilitate economic development and the alleviation of high unemployment should definitely be a priority for the South African government. Therefore, policies and regulations should be focused at this sector in order to nurture, sustain and expand it.

### **3.3 The Global Entrepreneurship Monitor Studies**

The Global Entrepreneurship Monitor (GEM) is an international assessment of entrepreneurial activity. There is participation from 37 countries, including South Africa. The studies examined the South African entrepreneurial environment and the results represent an important source for any study of the entrepreneurial environment (Foxcroft *et al*, 2002: 4). The GEM surveys provide a critical background to the discussion of business growth and an enabling business environment within the context of this study.

South Africa has been fortunate enough to participate in this annual global entrepreneurial study, for the last five years. The GEM survey is an international, long-term, multi-country survey that measures the level of entrepreneurial activity within the participating countries. The survey provides information on the total entrepreneurial activity (TEA) in the country, the association between entrepreneurial activity and economic growth and the factors associated with entrepreneurial behaviour in comparison with other developed and developing countries (Foxcroft *et al*, 2002: 10).

The summarised findings of the last five GEM surveys and the problems confronting South African entrepreneurs are presented below:

#### **3.3.1 The Findings of GEM 2001**

South Africa, as a new democratic country with new opportunities available to its entire people, has an average of (6.5%) total entrepreneurial activity (TEA). However, it scores the lowest of the developing countries surveyed. It was found that South Africans, are starting new ventures but unfortunately, are finding it difficult to turn their start-up ventures into sustainable businesses.

The survey further reveals that South African entrepreneurs have a low survival rate. GEM 2001 indicated that South Africans, although they are able to identify the opportunities, do not believe that they have the skills to take advantage of these opportunities (Driver *et al*, 2001: 3). The low TEA rate and the shortage of skills can however be ascribed to an educational system that is lacking.

### **3.3.2 The Findings of GEM 2002**

South Africa's total entrepreneurial activity has deteriorated from the results obtained in 2001. Unfortunately, South Africa has the lowest (6.3%) score of entrepreneurial activity among the developing countries. South Africa has a larger than average number of necessity entrepreneurs (2.3%) and a lower than average number of opportunity entrepreneurs (3.2%). South Africans are starting businesses but are unable to turn them into sustainable businesses implying that South African entrepreneurial ventures have a low survival rate (Foxcroft *et al*, 2002: 14). These findings once again point to an education system that is lacking in providing the skills necessary for business success.

### **3.3.3 The findings of GEM 2003**

South Africa's total entrepreneurial activity (4.3%) has yet again declined and is still significantly the lowest of the participating developing countries. One of the reasons for the low entrepreneurial rating identified by the GEM 2003 is that South Africans believe they do not have the necessary skills and experience to start businesses. South Africa is in need of an entrepreneurial society and this can be achieved by increased entrepreneurial awareness in the school education system and increased training with existing entrepreneurs (Orford *et al*, 2003: 18).

### **3.3.4 The Findings of GEM 2004**

South Africa's total entrepreneurial activity is still low in comparison to the other countries in the study, i.e. 5, 4% compared to an average of 9, 4% in all 34 countries and 21% in the developing countries. South Africa's ranking has stayed the same since its inclusion in 2001. Cross-national data suggests that South Africa has lower than expected TEA rates, given its per capita income. The reasons cited for this are structural and related to human capital constraints. GEM estimates



and government statistics; suggest that approximately 5.0% - 7.5% of South Africans aged between 15 and 65 are self-employed and estimates that the owner managed enterprise sector employs about 2.1 million people. Average employment per firm increases with the stage of the firm, rising from less than one person per start up to about 2.5 people per new firm and about 4.3 per established firm (Orford *et al*, 2004: 3-4).

International evidence suggests that the regulatory environment has a major influence on the survival and growth of small and new business. According to the World Bank, regulatory reforms in developing countries could add as much as 1.4% to average annual GDP growth in these countries. South Africa was found to have a relatively favourable regulatory environment, however there are, areas where improvements could be made. These areas are VAT tax and reductions in compliance costs (Orford *et al*, 2004: 3-4).

GEM acknowledges that the South African government has invested considerable resources into supporting small enterprises, however the reach of these programmes is very limited and most businesses are either unaware of or have not used any of the government's programmes and structures. Furthermore, small enterprises are largely unimpressed with the direct support offered by government (Orford *et al*, 2004: 3-4).

### **3.3.5 The Findings of GEM 2005**

South Africa's TEA rate (5.1%) has declined yet again and remains the lowest among the developing countries surveyed. The survey has found that the more educated a person, the more likely they are to start a business and the more people they are likely to employ. The potential of tertiary educated adults to create employment is 2.5 times greater than for adults who have only completed secondary education and it may be concluded that the level of educational attainment of the entrepreneur is by far the best predictor of the job creation potential of a firm (Von Broembsen *et al*, 2005: 7).

GEM estimates suggest that the job creation potential of men is 2.3 times that of women. Men are also more likely than women to become a new (less than 42 months) or established (more than 42 months) firm owner / manager. The data also reveals that Indian and White owned, new and

established businesses, tend to employ more staff on average, by comparison with businesses managed by their black and coloured counterparts (Von Broembsen *et al*, 2005: 26).

Innovative businesses constitute a tiny percentage of new and established firms. In this respect South Africa is no different to other GEM countries. Fewer firms offer products or services that are differentiated from their competitors. Whereas in 2003, 11.3% of owner-managers operated in markets where they had no competitors, this declined to 1.8% of owner-managers in 2005. The majority of businesses innovate on a relatively small scale and only a small fraction of owner-managers claim that what they offer is new to all customers. Owner-managers who offer products that are new to all customers have increased from 9% in 2003 to 15% in 2005 (Von Broembsen *et al*, 2005: 31).

The growth potential of South African enterprises is enormous if they are able to apply the very latest technologies to their products, services and technologies. However, skills will also need to be transferred in the process. Fewer firms use the latest technology for products or services. In 2003, 28% of South African owner-managers indicated that they used the very latest technologies (developed less than one year ago). In 2005, 0% of the sample reported that their firms used the latest technology. Education in South Africa is responsible to some extent for the country's low rates of entrepreneurial activity. The failure lies with the schooling system rather than with the tertiary education system (Von Broembsen *et al*, 2005: 33).

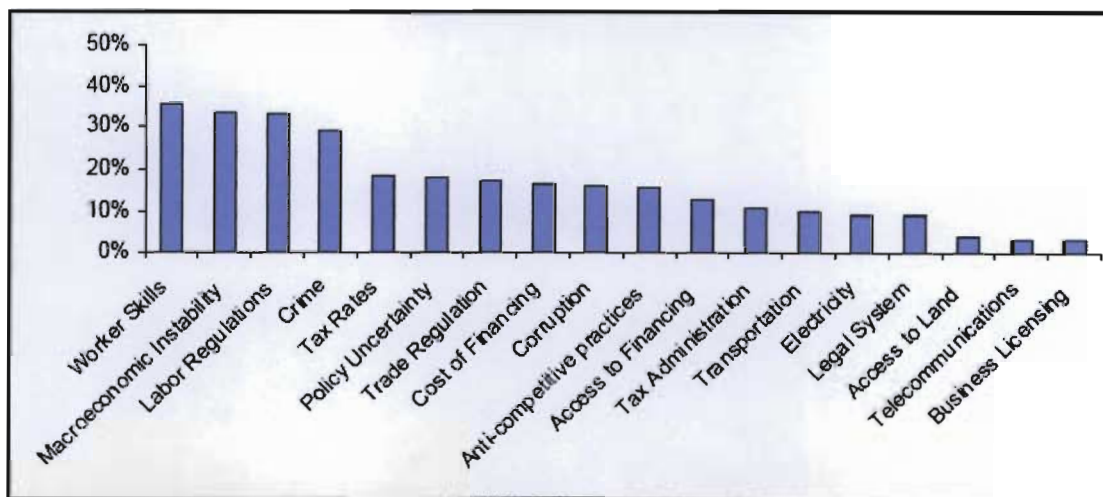
From the above discussion, it is evident that the lack of a sound education system has a rippling effect on the business sector. The products of such a system have a shortage of skills, lack innovativeness, under-utilise technology and as a result a poor entrepreneurial environment is created. The regulatory environment was also shown to constrain the growth and survival of the small business and it was established that the efforts of the South African government to lend support to the small business sector is failing. These findings indicate that small business entrepreneurs will face difficulties in recruiting skilled labour and in growing and expanding their ventures.

### 3.4 THE INVESTMENT CLIMATE SURVEY

The Investment Climate Survey (ICS) is a joint Department of Trade and Industry and World Bank initiative. The survey is undertaken by Cape Town based Citizen Surveys, a private South African firm. The survey of 800 businesses examined the location specific factors that shaped opportunities and incentives for firms to invest productively, create jobs and grow. The surveyed firms consisted of manufacturing, construction, wholesale and retail trade from Gauteng, Western Cape, KwaZulu-Natal, and the Eastern Cape (Investment Climate Survey, 2004: 5). The ICS provides us with a detailed cross-sectional snapshot of the South African private sector. Its main advantage is that it enables benchmarking of the South African private sector by comparing it to countries around the world (Investment Climate Survey, 2004: 16).

The data generated by this study enables us to analyze several things, including firm performance as measured by firm-level productivity, characteristics of markets such as labor and finance, and the impact of the business environment including infrastructure, regulation, and crime and security. Thus, we can see how South African firms perform relative to their counterparts around the world, and what their constraints are in a comparative context (Investment Climate Survey, 2004: 17).

Figure: 3.2: Major Obstacles to Growth



Source: (Investment Climate Survey, 2004: 9)

Figure 3.2 above, shows the response of surveyed businesses to factors that constrain growth. Worker skills, macroeconomic instability, labour regulations, crime and tax rates were the top five constraints to growth. Although the other factors also inhibit growth, the top five factors will be discussed in detail.

### **3.4.1 Worker Skills**

Jobs are the main source of income for people—and the main pathway out of poverty for the poor. A sound investment climate contributes to the creation of employment opportunities, investment in the workforce, increases in wages, and, ultimately, a more productive and prosperous society. A well-functioning labor market is vital to the success of the government's policies to redress historical inequalities and to establish a vibrant and globally competitive economy. However, surveyed respondents indicated that worker skills were a serious impediment to firm productivity and growth. One notable piece of evidence is the high premium that firms appear to pay for skilled and educated workers. Econometric analysis of individual workers' wages suggests that returns from schooling are very high. An additional year of education is associated with an 11-12 percent increase in wages. In comparison, returns for an additional year of education tend to be on the order of 5 to 7 percent in developed economies (Investment Climate Survey, 2004: 69).

Another piece of evidence is that wages appear to be relatively higher for managers and skilled workers in South Africa than wages for unskilled workers are. The returns to training are very high. A worker that has received some training earns about 30% more. This suggests positive returns to training. Training in South Africa is low compared to other countries and it is suggested that South African firms need to undertake rigorous and continuous training in order to maintain a competitive advantage (Investment Climate Survey, 2004: 72). Therefore the shortage of worker skills and the high premium required by skilled workers places a serious constraint on growth, productivity and recruitment.

### **3.4.2 Macroeconomic Instability**

Macroeconomic instability was rated as a serious obstacle to enterprise operations and growth by about 33 percent of South African firms—making it the second greatest constraint asked about in

the Investment Climate Survey. One possible explanation for the concerns about macroeconomic instability is that exchange rates have been relatively unstable—especially against the U.S. dollar. It was found that 28 percent of non-exporters rated macroeconomic instability as a major or very severe problem, while 44 percent of exporters did the same. This indicates that it is not only exporters who bear the brunt of macroeconomic stability. Since many South African manufacturing firms appear to be price takers on international markets, changes in the exchange rate can have a serious impact of enterprise revenues (Investment Climate Survey, 2004: 97). The economic environment therefore, can be a serious inhibitor of facilitator of growth.

### **3.4.3 Labour Regulations**

Managers in the Investment Climate Survey were concerned about the impact of labor regulation on their enterprise's operations and growth. Previous work has also stressed the potential impact of these regulations. For example, a paper published by the World Bank Southern Africa Group on constraints to growth and employment, reveals that 10-15% of a sample of SME's reduced employment as a result of the four major labor regulations. A study on the regulatory environment in South Africa noted that it took 2.7 months on average to retrench an entry-level employee. It cost R9,000 to hire and R2,160 - 2,900 to fire a least skilled worker. Partly as a result, 40% of firms hired fewer workers, used more machinery, hired temporary staff, or subcontracted (Investment Climate Survey, 2004: 66).

The ICS survey cites the 2003 South Africa Human Development Report, in which the authors discuss a policy bias, during apartheid, toward capital intensity. These included corporate tax incentives, depreciation allowances, tariff rebates, debt financing, subsidised interest rates and provision of utilities and infrastructure. Since 1994, it has been found that, policies continue to promote capital intensity at the expense of employment (Investment Climate Survey, 2004: 67). Therefore, labour regulations are a definite constraint to growth.

### **3.4.4 Crime**

About 30 percent of enterprises in the Investment Climate Survey rated crime as a major or very severe problem. Although there were a few differences, complaints regarding crime were common among most types of enterprises and in most regions. About 30% of South African

firms cited security issues as a major or severe obstacle to doing business. This compares favorably with the more volatile Latin American countries, where between 50 and 80% of firms rated crime as a severe obstacle, but is considerably higher than most other middle-income countries (between 10 and 20% of enterprises). Objective measures of the cost of security are consistent with the perception based data. The direct costs associated with the security situation in South Africa are large and significant for many firms: 1.1 percent of sales revenue.

Table 3.1: Cost of Crime and Security relative to Labour costs and Value Added

<i>Sector</i>	Losses to crime, mill. Rand	Cost of Security, mill. Rand	Net value-added, mill. Rand	Total labor costs, mill. Rand	Total cost of crime and security (% of labor costs)	Total cost of crime and security (% of net value-added)
<i>Retail &amp; wholesale</i>	83	203	5,151	3,574	8.0	5.6
<i>Manufacturing</i>	1,962	1,368	55,168	17,270	19.2	6.0
<i>Construction</i>	227	192	6,724	5,668	7.3	6.2
<i>All</i>	2,272	1,764	67,045	26,511	15.2	6.0

Source: (Investment Climate Survey, 2004: 96)

Table 3.2: Cost of Crime and Security in Millions of Rands.

<i>Sector</i>	Losses to Crime, mill. Rand	Cost of Security	Sample, estimated % of total sector	Extrapolated cost of crime, mill. Rand	Extrapolated cost of security, mill. Rand
<i>Retail &amp; wholesale</i>	83	203	2.3	3,544	8,717
<i>Manufacturing</i>	1,962	1,368	23.1	8,495	5,925
<i>Construction</i>	227	192	23.2	978	827
<i>All</i>	2,272	1,764		13,017	15,470

Source: (Investment Climate Survey, 2004: 96)

From the tables (3.1 and 3.2) presented above, the total cost of crime and security is about 6% of the net value-added and losses due to crime across all sectors amount to 2,272 million of rands. The cost of crime therefore is a serious constraint to the growth of the business.

In summary, the Investment Climate Survey reveals that firm productivity is relatively high, the investment climate is mostly favourable, the burden of regulation is not excessive, corruption is low, access to finance does not seem to be a problem, but investment and growth has still been low over the past decade (Investment Climate Survey, 2004: 14). A possible explanation is that

although most areas of the investment climate are favourable, some are not. The cost of labour is high for skilled workers, labour regulation is burdensome and the cost of crime is high. These factors discourage investment, and definitely constrain the growth of SME's.

### **3.5 THE SMALL BUSINESS PROJECT'S: Counting the Cost of Red Tape**

The Small Business Project (SBP) is an independent, non-profit, private sector development and research organization, promoting strategic partnerships and a better policy, regulatory and operational environment for business growth in Africa. Their work combines research, advocacy, and practical business development programmes. In June 2005, SBP published a comprehensive report on the cost of regulation that was made available to the South African public sector (Small Business Project, 2005: 5).

#### **3.5.1 The Findings of SBP 2005**

Regulation cost South African firms R79-billion in 2004. This is the bottom-line result of SBP's pioneering study of regulatory compliance costs to the South African private sector, from large corporations through small and medium enterprises (SMEs) to the informal sector. No comprehensive survey of this kind has previously been undertaken in this country and therefore it is the largest general regulatory cost survey ever carried out anywhere (Small Business Project, 2005: 6).

Organised business and the South African government agree that it is necessary to create an enabling environment that spurs economic growth and job creation. The rewards of an improved regulatory environment are extensive. A 2002 study of 10 developing countries, including South Africa, by SBP and Bannock Consulting concluded that an appropriate regulatory environment was the single most important element in an economic growth strategy. Although South Africa has a better regulatory system than many developing countries, improving the regulatory environment could have a significant impact on economic prospects (Small Business Project, 2005: 18).

Results from the SBP study suggest that red tape is not only of significant financial cost to the SA economy, but what may be of even more significance than the approximately R79-billion which

firms and individuals spend on regulatory compliance, is the extent to which the regulatory environment is acting as a brake on economic development.

The report is based on a survey of the costs of regulation to the South African private sector. Between February and June 2004, a total of 1 794 businesses throughout the country were interviewed in depth. Respondents ranged from corporations on the top-200 list to enterprises in the informal sector. The survey covered all the sectors of the economy, including manufacturing, mining, construction, trade, agri-business and services (Small Business Project, 2005: 5).

Regulations are vital to the fair and sustainable working of market economies, but even the most socially necessary regulations create costs as well as benefits, and some of these costs may be unnecessarily high. It is important to distinguish between a regulation and the costs created by complying with it. For example, health and safety regulations are unarguably essential. This does not mean, however, that we should accept the current level of associated regulatory costs as fixed. It may well be possible to reduce the costs of complying with regulations without reducing their benefits (Small Business Project, 2005: 18).

Reducing regulatory costs can be very beneficial, studies by the World Bank, covering 145 countries, have demonstrated that countries with higher regulatory costs have larger informal sectors, more unemployment and slower growth (Small Business Project, 2005: 17). Counting the cost of red tape, examined in detail two kinds of regulatory costs faced by the private sector: efficiency costs and compliance costs.

### **3.5.2 Efficiency costs**

Efficiency costs arise because regulation may distort market outcomes. If employment is discouraged by inappropriate labour market regulation, for example, then the costs of the resulting unemployment in terms of lost output and incomes is an efficiency cost. Other examples of efficiency costs of regulation would be a business's decision to restrict output to keep sales below the value added tax (VAT) threshold, or an inability to compete in an export market because the costs of complying with regulations have made a product too expensive (Small Business Project, 2005: 14).



### 3.5.3 Compliance costs

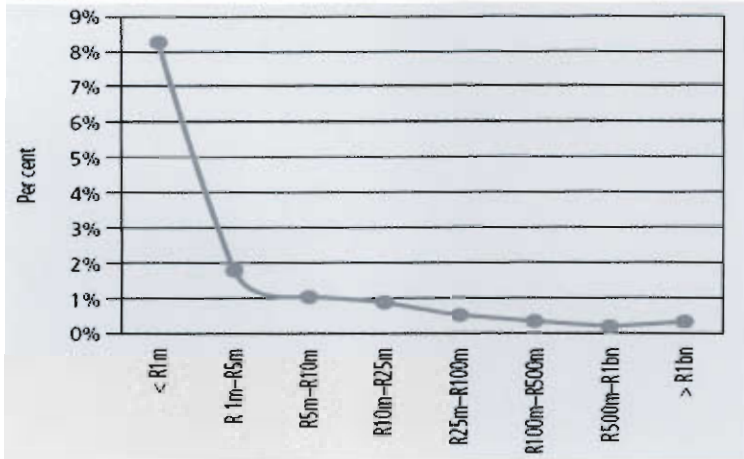
Compliance costs are pure red-tape costs: that is, they are the incremental costs incurred by business in the course of complying with regulations. They include the value of time spent by business managers and staff on understanding the rules and applying them; interacting with the authorities to clarify matters arising; and the payments made for the expertise of professional advisers such as consultants, lawyers and accountants. For instance, the costs of tax paperwork are compliance costs, whilst tax payments themselves are not (Small Business Project, 2005: 14). What makes the Small Business Project (SBP) study valuable is that it provides hard data on compliance costs and provides quantitative information for businesses on how much red tape actually costs them. It is important to note that the study has not attempted to measure the benefits of regulation. It is clear from the results that regulation costs are fairly prohibitive to firms and consumers or tax payers in the South African economy.

There is strong evidence, echoed by many other studies (Orford *et al*, 2004 and Investment Climate Survey, 2004), to show that features of the regulatory environment discourage business growth and job creation in the formal economy. This research has also shown that, even though regulations may not be enforced in the informal sector, the regulatory environment acts as a barrier to development by keeping a large, energetic and entrepreneurial group of black South Africans out of the formal economy (Small Business Project, 2005: 72).

The SBP survey has shown that regulatory compliance costs are substantial in South Africa. Based on the average recurring compliance cost per firm of R105174, and conservative estimates of 750 000 as the number of firms affected, the estimated aggregate recurring compliance costs for the formal sector amounted to R78.9-billion in 2004, an amount equivalent to 6.52% of the gross domestic product (Small Business Project, 2005: 89).

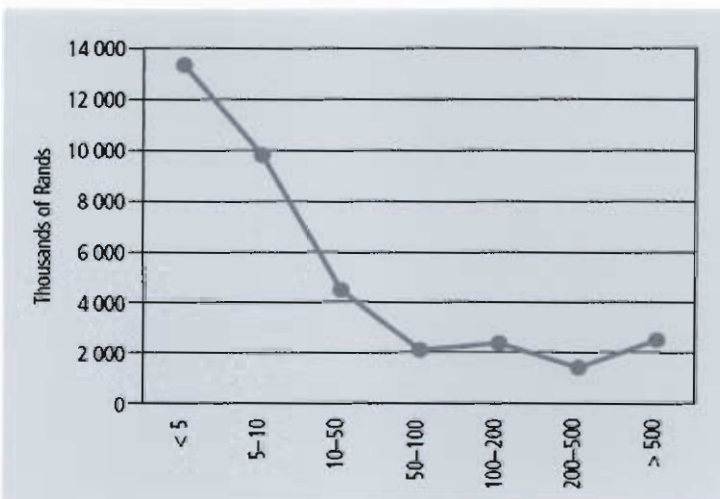
Figures 3.3 and 3.4 (below) indicate that for very small firms, more than 8% of turnover and more than R13 000 per employee is spent on annual regulatory compliance. Although these costs fall relatively quickly as we move up the firm-size continuum, they nonetheless remain significant. This result indicates that regulatory compliance costs are regressive, as small firms bear the heaviest burden in relation to firm size (Small Business Project, 2005: 45)

Figure 3.3 Annual regulatory compliance costs as a percentage of turnover.



Source: (Small Business Project, 2005: 45)

Figure 3.4 Annual regulatory compliance costs per employee by number of employees



Source: (Small Business Project, 2005: 45)

These costs represent real resources, which can have alternative uses. Businesses could employ the resources used in complying with regulation for innovation and expansion, or improving their local and international competitiveness. The government could use some of the cost savings to improve public services or to reduce taxation. Moreover, countries that reduce their regulatory compliance costs increase their attractiveness to foreign direct investment.

## **3.6 THE PIETERMARITZBURG PERSPECTIVE**

### **3.6.1 Introduction**

KwaZulu-Natal was the second-highest contributor to the South African economy during 2003, at 16.5% of GDP. The key strength of this province's economy is its trade and transport infrastructure. The province's unemployment rate of 31, 7% is the second-highest of the provinces after Limpopo (Labour Force Survey, 2005: 1). Information for the Pietermaritzburg region was sourced from the Quarterly Economic and Business Report prepared by Clive Coetzee of the University of Kwazulu Natal.

### **3.6.2 The Quarterly Economic and Business Report**

Important to note is that the analyses presented makes use of the Kernel Smoothing Technique.

#### **3.6.2.1 Provincial Government Expenditure in Kwazulu Natal**

According to Clive Coetzee, current expenditure (remuneration of employees, spending on other goods and services, interest, subsidies and current transfer to households) increased from a quarterly average of R7.3 bn in 2003 to a quarterly average of R8.9 bn in 2004 and to a quarterly average of R10 bn in 2005. This represents an average monthly increase of 4.12% from January 2003 to December 2005. The increasing level of current expenditure is expected to positively contribute to business turnover and the overall performance of the local economy in 2006. Capital expenditure however represents, on average, a mere 8.83% of current expenditure and has been decreasing steadily from 11.2% in 2003 to 7.5% in 2005. This is well below the recommended 30% target level. This is a point of concern because capital expenditure is crucial for sustainable development and future levels of economic growth (Coetzee, 2006: 4).

#### **3.6.2.2 Turnover and Remuneration**

Average quarterly turnover increased from R8 bn in 2003 to R9.5 bn in 2004 before decreasing modestly to R9.1 bn in 2005. More significantly, the upward trend has continued, although at a slower pace than from 2002 to 2004. The increase in turnover is mostly due to the low inflation and interest rate environment and increased levels of current government and consumer expenditure. It is very possible that the local economy has experienced an increase in the number

of businesses and thus an increase in the range of products and services available. Businesses that target the consumer directly have indeed experienced an increase in profitability since 2003. Pietermaritzburg has become a lucrative market and this fact in itself should attract and encourage investment into the local and surrounding economies (Coetzee, 2006: 5).

### **3.6.2.3 Business Investments**

Research indicates that loans to businesses and the value per loan application for purposes of new ventures and/or expansion increased robustly since the beginning of 2005. The increase in demand for investment finance can directly be attributed to the performance of the local economy and the increase in profitability expectations (Coetzee, 2006: 7).

### **3.6.2.4 Labour Market**

The number of claims for unemployment benefits decreased significantly during the last two quarters of 2005. Whereas the number of unemployment claims increased in 2004 by 23%, there was only an increase of 1% in 2005. This is significant for two reasons, i.e., it signals a decrease in the unemployment rate in the local economy and it is evidence that the economic performance of the local economy during the past three years created and is still creating sustainable employment and opportunities for SMME's .

It is encouraging to note that the economy is still creating employment and in fact the pace of job creation accelerated during 2005. The average job creation index value for 2003, 2004 and 2005 was 109, 132 and 150, respectively. The number of job placements during 2004 and 2005 increased by 21% and 23%, respectively, representing a cumulative increase of between 1000 and 1500 private sector jobs created between 2003 and 2005. The trend also suggests that further job creation is likely (Coetzee, 2006: 9).

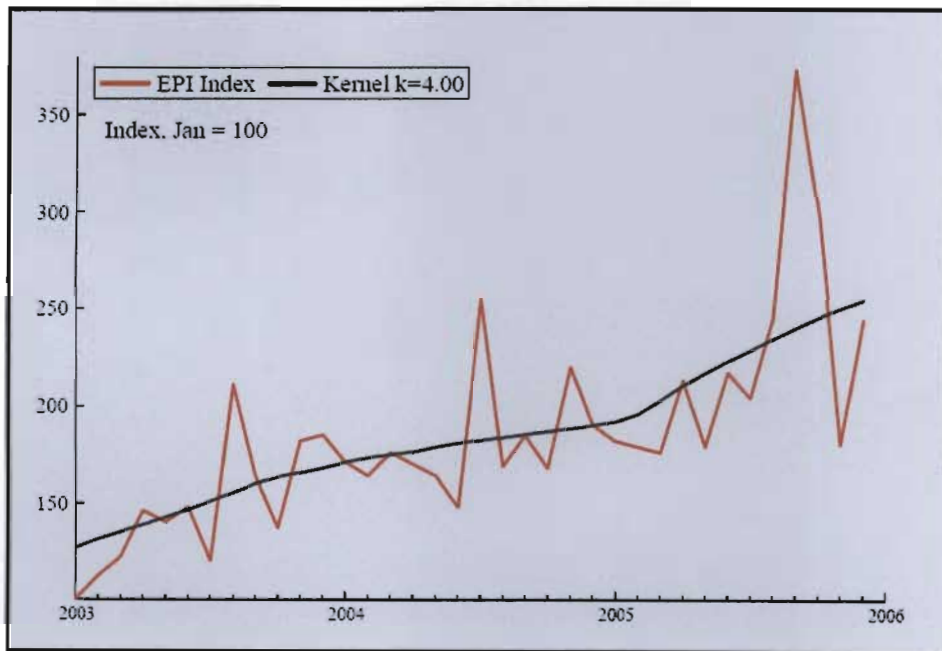
### **3.6.2.5 The Economic Performance Indicator for Pietermaritzburg (PMB)**

The Economic Performance Indicator (EPI) is a time series and is formed by aggregating a variety of component indicators. The EPI for PMB is designed to provide qualitative and quantitative information on short-term economic movements, especially at the turning points, and long-term trend movements in the local economy. The EPI comprises a set of component series

selected from a wide range of key short-term economic indicators (most of the individual economic indicators are included). These key short-term economic indicators are weighted in terms of their relative importance in influencing the economic activity of the district economy. The EPI is thus a weighted economic performance indicator (Coetzee, 2006: 33).

The graph (figure 3.5) presented below demonstrates the robust increase in the level of economic activity in the local economy. The cause for optimism is that the long term trend of the EPI is still in an upward direction. Most of the individual indicators (variables) also suggest further growth in the local economy.

Figure 3.5 Level of Economic Activity



Source: (Coetzee, 2006: 34).

The Business Confidence Index (BCI) for PMB for the second quarter of 2006 is 85 (86 for South Africa). The BCI with a value of 50 is indicative of neutrality, 100 indicates extreme confidence and 0 indicates extreme lack of confidence. It seems that businesses are very positive and confident about the current and future state of business in PMB and in the Umgungundlovu District (Coetzee, 2006: 40).

### **3.7 Conclusion**

The literature reviewed has shown that while South Africa's investment climate is favourable, growth has not been exceptional and this can be attributed to the education level and training of both entrepreneurs and workers, the regressive cost of compliance of regulations, crime and taxes. The economic climate of the site for this study looks promising. The BCI is on the rise in Pietermaritzburg. This should enable businesses in the region to flourish. However, whether ventures flourish or do not grow, depends mostly on the environmental factors. The following chapter examines both internal and external variables that constrain the growth of the SME.

## CHAPTER FOUR

### THE ENVIRONMENTAL CONTEXT OF ENTREPRENEURSHIP

#### 4.1 Introduction

Businesses are neither independent nor completely isolated as they are inextricably part of the environments (internal and external) within which they function. These environments are not static but dynamic in nature (Fry *et al*, 2001: 13). Changes in the environments can have positive or negative consequences for business growth. This chapter looks at the factors of the internal and external environments that will be examined in this study. The present study approaches the entrepreneur's environment as perceptions of the difficulties they encounter. This is similar to the approach used by various other studies (Global Entrepreneurship Monitor Studies, 2001-2005; Investment Climate Survey, 2004; Small Business Project's: Counting the Cost of Red Tape, 2005 and Kozan *et al*, 2006: 119).

#### 4.2 THE INTERNAL ENVIRONMENT

##### 4.2.1 Business Age and Industry Sector

Storey (1994: 85) provides an overview of the many factors considered by researchers prior to 1994 and concludes that among small businesses, the business age, industry sector and legal form are of significance for growth. Storey notes that empirical research showed that business age is inversely related to growth, that is, older businesses grew more slowly than young firms. Similar results were found by Davidsson *et al*, (2002: 344) and Almus and Nerlinger (1999: 152) in Sweden and Germany respectively. Age, then, is an important factor that affects business growth. Storey also found that growth rates vary by industrial sector and that certain sectors such as services, retail trade and manufacturing have been found to grow differently (Storey, 1994: 145). These findings were verified by Davidsson *et al*, (2002: 346); and Almus and Nerlinger, (1999: 154).

##### 4.2.2 Education, Experience and Training

The Global Entrepreneurship Monitor 2001, 2002, 2003 and 2004 surveys have identified education and training as one of the major problems facing South African entrepreneurs. The legacy of apartheid has left the vast majority of South Africans with a lack of basic skills. For

example, more than 50% of the population has not obtained a grade 12 qualification and only 6% of the population have some form of tertiary education (Driver *et al*, 2001: 39).

South Africa has consistently scored badly on international measures of human capital development. For example, in the 2004 World Competitiveness Yearbook South Africa ranks 49th out of 60 countries on the overall ranking. However, on the sub-index for education, South Africa ranks 55<sup>th</sup> (Orford *et al*, 2004: 27). According to Bukula, South Africa was placed 47<sup>th</sup> out of the 47 countries surveyed in an international study of skilled labour and education systems (Bukula, 2000: 65). The importance of education is highlighted by the tables below.

**Table 4.1: Entrepreneurial Level of South Africans according to their Education**

	Start-ups (%)	New firms (%)	Established firms (%)	Total business ownership* (%)
Without matric	3.1	0.9	0.8	4.0
With matric only	4.9	2.4	1.8	7.2
Tertiary qualification	6.9	4.3	5.2	10.4

Source: (Small Enterprise Development Agency, 2004: 62)

**Table 4.2: Educational Level of Entrepreneurs compared to South African Population**

	Population of working age		Economically active		Entrepreneurs	
	In '000	In %	In '000	In %	In '000	In %
Without matric	20,445	70	9,224	58	869	51
With matric only	6,082	21	4,223	27	484	28
Tertiary qualification	2,546	9	2,178	14	351	21
<b>TOTAL</b>	<b>29,305</b>	<b>100</b>	<b>15,778</b>	<b>100</b>	<b>1,704.3</b>	<b>100</b>

Source: (Small Enterprise Development Agency, 2004: 62)

Tables (4.1 and 4.2 above), show that entrepreneurship levels increase with education. From the table below it is evident that those in possession of a tertiary education have the highest chance of owning established firms (5.2%) or even starting-up in business (6.9%).



The Global Entrepreneurship Monitor 2002 study has also shown that entrepreneurs with matric employ, on average more workers than those without matric.

Qualitative studies undertaken by Watson *et al*, (2003) and Saprenza and Grimm (1997) cited by Barringer *et al* ( 2005: 667) lend support to Storey's finding that educated entrepreneurs are more likely to establish faster growing businesses (Storey, 1994: 127). These authors further state, that higher education provides founders with the skills necessary to launch ventures. In other cases the time spent in acquiring a higher education help embed an individual in a social network that is helpful in launching a business venture (Barringer *et al*, 2005: 678).

The expert informants who participated in the Global Entrepreneurship Monitor 2001 survey believe that South Africa could improve this situation by integrating business and management skills into the South African education system. Technical skills training in areas such as science, maths, engineering and technology should be drastically increased. Focusing on education and training to advance entrepreneurial performance is critically important (Driver *et al*, 2001: 41).

It is not important to develop technical and management skills only, as other studies highlight the importance of entrepreneurial education (Anderson and Jack, 1999: 2 and Van Vuuren, 2001: 2). Entrepreneurial education and training builds awareness, improves attitudes and creates a positive perception of entrepreneurship as a career option. Therefore the demand for entrepreneurial education and training arises from various sources, including government, learners and the broad business environment (Anderson and Jack, 1999: 3).

This view is supported by Bukula (2000: 67), who believes that the lack of entrepreneurial education in South African schools is one of the country's biggest failings. Kennedy and Drennan (2001: 165), in comparing the results of multiple studies relating to the influence of education and prior experience on the performance of entrepreneurs conclude that the level of education, previous entrepreneurial experience and business similarity experience definitely impact on the success and growth of new ventures. Finally, the Global Entrepreneurship Monitor 2005 study found that the more educated a person, the more likely they are to start a business and the more people they are likely to employ. The potential of tertiary educated adults to create employment

is 2.5 times greater than for adults who have only completed secondary education. The level of educational attainment of the entrepreneur is by far the best predictor of the job creation potential of a firm (Von Broembsen *et al*, 2005: 29).

#### **4.2.3 Access to Finance**

Small business managers often see access to and the cost of financing as serious obstacles to their business operations and growth. The lack of adequate financing is the most serious constraint during the formation of a new venture. Mahadea (1997: 72) conducted a study concerning the financial problems associated with the formation and growth of small businesses and the study revealed that 83% of respondents indicated that lack of capital was the most pronounced initial constraint. Similarly, Murphy (1996: 22) reports that insufficient funding was the most important barrier to overall growth amongst small businesses in the UK. Access and the cost of financing ranks among the top five constraints in Sub-Saharan Africa, according to the Investment Climate Survey (Investment Climate Survey, 2004: 12).

A possible reason for this constraint given by Rwigema and Venter (2004: 390) is that traditional financial institutions view informal SMMEs as high-risk areas that have poor collateral and high administrative costs. Traditional financial institutions often have stringent funding requirements for small businesses. These requirements often represent barriers for entrepreneurs which force them to approach alternative forms of financing (Rwigema and Venter, 2004: 394). In support of this, it was found that the majority of the financing of entrepreneurial ventures is self-funding or informal funding, including friends, family and colleagues (Orford *et al*, 2003: 36).

Global Entrepreneurship Monitor 2003 concluded that increased access alone was not the most important issue in terms of improving financial support to small businesses. Rather these businesses needed improvements in their internal financial management (Orford *et al*, 2003: 34).

#### **4.2.4 Financial management**

Financial management is one of the most important management skills. As explained in the entrepreneurial process and life cycle of the business venture (chapter two) financial information affects every aspect of the entrepreneurial venture. Financial management entails minimising the

costs, maximising the profit, and planning and controlling the finances of the venture (Bloom and Boessenkool, 2002: 244). The management of cash flow is vitally important as it entails the inflow and outflow of cash (Marx *et al*, 1998: 714). Hodgetts and Kuratko (1998: 255) believe that financial management links all of the functional areas of the business including marketing, distribution, manufacturing and general management.

Effective financial management will enable entrepreneurs to effectively manage their businesses. The production of certain financial documents and the proactive use of financial documents to manage cash, reduce the probability of cash flow problems. Given the centrality of cash flow to the survival of a business, it seems reasonable to deduce from this that proficiency in financial administration and management can be expected to reduce the probability of business failure and therefore becomes a pre-requisite for business growth and expansion (Orford *et al*, 2003: 46).

Inadequate bookkeeping leads to deficiencies in several other areas of financial management. Potgieter and Frank (1990: 3) mention that management incompetence is directly linked to inadequate information for decision making. It is therefore imperative that entrepreneurs equip themselves with the necessary financial skills to analyse and monitor financial activities.

#### **4.2.5 Management skills**

Oosthuizen (2002: 99) views general management skills as the basic functions conducted by all managers at any management level. These skills are essential for entrepreneurs because they assist with planning, organising, leading and controlling the relevant resources. De Villiers and Crous (1998: 353) agree that the general management function can be broken down into five distinct tasks. These are planning, organising, leading, co-ordinating and controlling. These tasks are found at all levels of management, regardless of the size of the business.

The skills required by managers and entrepreneurs can also be sub-divided into four skills types which include technical skills (specific knowledge and techniques), analytical skills (analysis of information), interpersonal skills (communication, motivation and relationship management) and conceptual skills (vision, creativity and long-term orientation). Hodgetts and Kuratko, quote a lack of these managerial skills and experience as the third common cause of business failure

(Hodgetts and Kuratko, 1995: 17). It is these skills that are required for environmental scanning (SWOT and PESTLE) that lead to the formulation of short term objectives to satisfy long term goals.

#### **4.2.6 Human resource management**

The human resource management process is, perhaps, one of the most critical functions for small business owners to deal with and is a vital concern for any new venture, as it can facilitate a competitive advantage for the organization (Hodgetts and Kuratko, 1995: 371). These assets must be nurtured and correctly managed to secure a maximum return (Rwigema and Venter 2004: 185). A new venture would not exist if it did not have a reliable and productive human input. It is the entrepreneur's responsibility to manage the personnel within the organisation. Entrepreneurs must recruit effectively, train their employees and motivate and lead their employees (Marx *et al*, 2002: 257). However, recruitment is a function of both internal and external factors. External factors affecting recruitment are legislation (Labour Relations, Employment Equity and Minimum Wage Regulations) and labour market conditions.

Internal factors affecting recruitment can stem from the business's recruitment policy, which advocates internal recruitment before external recruitment. (Hunter, 2002: 85). When there is a shortage of skilled people as revealed in the previous chapter, the recruitment process is usually more difficult, time consuming and expensive. The entrepreneur's tasks include managing the services to the organisation (recruiting, selection and training), controlling the human resource function (implementing human resource policy and administration), advising staff and management (disciplinary conduct, salaries and budgeting), formulating a human resource policy and adhering to the labour legislation (Marx *et al*, 1998: 473).

#### **4.2.7 Innovation and Technology**

Innovation is of great importance for economic growth and job creation. All businesses, regardless of their size, need to innovate to satisfy the changing needs of their markets, both local and global. In the literature, innovation is often considered to be an integral part of entrepreneurship (Hisrich and Peters, 2002: 39, Hodgetts and Kuratko, 1998: 44, and Timmons, 1999: 6). Outcomes of innovation include: introducing new products or services; competing in

new ways; and using technology in new and creative ways to create value for customers. It is important to remember that innovation is context-specific and that what is seen as innovative in one country may not necessarily be seen as innovative in another (Von Broembsen *et al*, 2005: 32). The utilization of technology such as computers in the operation of the business can also be a source of competitive advantage.

Computer based functions are not limited to routine record-keeping activities, but include a wide range of diverse applications. Tasks such as desktop publishing, communicating electronically with vendors and customers, and electronic banking are but a few of the applications that the small business utilizes to contain costs and improve services (Longernecker *et al*, 1994: 593). The areas of the small business where computer technology can be utilised are : tracking financial transactions such as order entries, accounts receivable, accounts payable, payroll, inventory management; Electronic Data Interchange (EDI), the exchange of data between businesses through computers that make manual purchase orders and sales invoices obsolete; Local Area Networks (LAN), that makes communication and coordination of employees easier; and the application of Computer Aided Design, (CAD) and Computer Aided Manufacturing (CAM) that has revolutionised the manufacturing process (Longernecker *et al*, 1994: 594)

It becomes evident that the small business can benefit greatly from the use of technology such as computers and innovativeness. However the cost of such technology is often viewed by managers as extremely high and many still prefer the conventional way of doing business. Such a myopic view ultimately constrains the growth of the business. In order for the small business to be innovative the organizational structure and climate must also be conducive to encourage innovation and risk taking.

#### **4.3 EXTERNAL ENVIRONMENT**

The macro-environment contains economic, socio-demographic, political, physical, international and technological factors over which management cannot exert full control. There is considerable evidence to suggest that improving the regulatory environment can have a positive influence on the growth and survival of new and small enterprises. Gnyawali and Fogel (1994: 46) argued that the environment is actually more important for small businesses as large businesses have a better

chance of influencing it. Among environmental factors, Gnyawali and Fogel included governmental policies, socio-economic conditions, availability of business skills, and financial and non-financial assistance as factors of importance. Evidently, their classification of environmental factors includes both internal and external variables.

Dana (1998) cited in Kozan *et al* (2006: 118), found that keeping regulations at a minimum, offering tax and other incentives, and providing training and counseling services increased the likelihood of new venture startups and stimulated growth. Young and Welch (1993) cited in Kozan *et al* (2006: 118), further found that entrepreneurs face many obstacles such as lack of financial assistance, lack of business information, unnecessary taxation and a soaring inflation rate. These findings have been consistent with those of the Global Entrepreneurship Monitor studies, the Investment Climate Survey and the Small Business Project's: Counting the Cost of Red Tape Report.

#### **4.3.1 The Economy**

Economic forces impact heavily on business. As these forces are beyond the control of the business, managers therefore need to anticipate and react to changes as quickly and efficiently as possible. The macroeconomic forces include interest rates, inflation, unemployment and economic growth (Gross Domestic Product) (Fry *et al*, 2000: 165).

A growth in the economy results in an increase of the Gross Domestic Product (GDP). This implies that consumer expenditures are increasing and bodes well (increase in sales) for businesses. Since the transition to democracy, South Africa's macroeconomic performance has been positive. The Gross domestic Product (GDP) growth has averaged 2.9% between 1994 and 2003, and increased to over 3% in 2004 and 2005. In this respect, South Africa appears locked into a path of sustained but moderate growth (Investment Climate Survey, 2004: 6).

Inflation refers to a general increase in prices or an increase in the prices of most goods and services. The most popular measure of inflation is the Consumer Price Index (CPI). The impact of inflation on businesses can be severe. As inflation increases, more money is required for consumers to purchase the same amount of goods, resulting in a decline of consumer spending,

which affects the sales of a business (Fry *et al*, 2000: 168). High inflation also results in higher costs of doing business, which translates into higher prices of goods sold to the public.

Interest is the price paid by individuals or businesses to borrow money. The interest rate expresses that price as a percentage per rands of funds borrowed. Interest rates affect businesses in three significant ways. Firstly, rising interest rates increase the total price customers pay who use credit for products and services. Therefore an increase in interest rates reduces the demand for products and services. Second, most businesses borrow money to run their daily business. Higher interest rates mean higher cost of doing business. Managers must either raise the prices of their products to cover this cost of doing business or accept lower profits. The third effect of interest rates is on the expansion of the business. Lower interest rates mean that it is a good time to expand as the cost of borrowing is low (Fry *et al*, 2000: 172).

Therefore the business manager/entrepreneur must at all times know what is happening to the macroeconomic factors of growth, inflation and interest rates. This is only possible through constant scanning of the environment by using the management analysis tools, SWOT and PESTLE. These analyses enable the entrepreneur to take advantage of favourable changes in the economic environment and protect the business against adverse changes.

#### **4.3.2 Taxation**

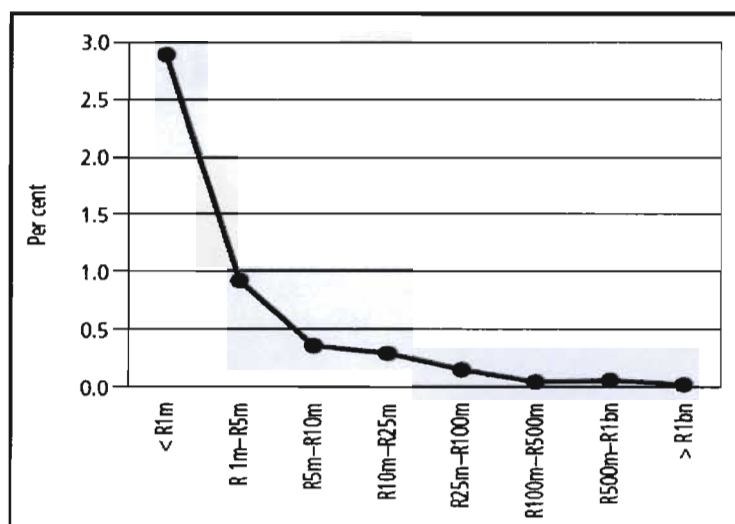
“Nothing is for certain except death and taxes.” This widely quoted phrase expresses the mood of most taxpayers and businesses. High tax rates and complex tax administration is a significant constraint for small and medium enterprises and can lead them to the informal sector if tax burdens become excessive (Longenecker *et al*, 1994: 685). A large informal economy can mean lower government revenues and higher taxes for firms in the formal economy, creating more incentives for informal operation. A complicated tax system discourages the development of entrepreneurs and investment in SMMEs. The principle taxes imposed in South Africa are direct and indirect taxes:

- Direct Taxes include income tax, secondary tax on companies (STC), capital gains tax (CGT) and donations tax.

- Indirect Taxes include value added tax (VAT), estate duty, stamp duties, transfer duties on real estate, customs & excise duties, marketable security taxes, skills development levies, municipal

The current tax rules according to the 2006 budget speech is the expansion of Graduated Tax on Small Business Companies, which means that small businesses can pay up to about R61 000 less tax on their first R300 000 profits per year than large companies. The major change is that businesses with an annual turnover of less than R14 million can also now qualify (up from last year's R6 million). If businesses qualify, they will pay no tax on the first R40 000 annual profit, and only 10% on annual profit of between R40 000 and R300 000. On any profit more than R300 000, the business will pay the normal company tax of 29% (Small Enterprise Development Agency, 2006: 3).

Figure: 4.1: Annual Cost of Tax Compliance as a percentage of Turnover



Source: (Small Business Project, 2005: 46)

From figure 4.1, it is clear that the cost of tax compliance is regressive and that the small business pays the most amount of tax (almost 3% of turnover). In comparison larger firms, that have the resources to engage tax consultants pay between 0.1 to 0.5 % of turnover. Clearly such a situation forces small businesses to remain small and employ fewer workers.



### **4.3.3 Regulation and Laws**

Broadly defined, regulations are rules and standards imposed by public authorities to control human behaviour. Regulations include parliamentary legislation, rules, standards, orders and codes of practice issued by different spheres of government. Economic regulation is designed to alter the ways in which markets work. It does this by creating rules about what prices can be charged, influencing the number of firms in an industry, or trying to influence the way in which firms function. Social regulation is intended to protect public interests such as health, safety, the environment, public order, and social cohesion. A crucial social justification for regulation is the need to make the distribution of goods, services, income, and wealth fairer (Small Business Project, 2005: 10)

International evidence suggests that the regulatory environment has a major influence on the survival and growth of small and new businesses. According to the World Bank, regulatory reforms, as mentioned earlier, in developing countries could add as much as 1.4% to average annual GDP growth in these countries (Orford *et al*, 2004: 51).

Although South Africa's regulatory environment compares favourably with that in other developing countries, by further reducing and simplifying regulations and compliances, entrepreneurs will be encouraged to formalize and expand existing businesses and to start new businesses. Firms state that if they want to avoid regulatory compliance costs they could reduce employment, limit their growth, try to pay less tax, casualise their staff, and become more capital-intensive. In other words, red tape compliance costs have the potential to make firms behave in ways that damage South Africa's overall social and economic prospects (Small Business Project, 2005: 33)

### **4.3.4 Crime**

Crime is one of the cardinal problems affecting South Africa and its citizens. The effects of crime are a declining economy, unemployment, broken families and stress associated with a life of fear. Business, being the economic engine of society, is affected both directly and indirectly by crime. Directly regarding the theft of property and money, and indirectly through reduced business

confidence, loss of investment, emigration and the steady erosion of the foundations upon which the economy is built (BAC, 2006: 1)

About 30% of the respondents in the Investment Climate Survey rated crime as a major or very severe problem. Complaints were found to be common among most types of businesses and in most regions surveyed. The evidence from the Investment Climate Survey suggests that crime is also a serious concern for business. The median firm reported that the direct losses due to crime and the cost of security were equal to about 1.1% of sales. This is higher than in many middle-income countries—median costs were less than 1% of sales in China, Poland, Brazil and even Russia. But it is lower than in the very worst countries—median costs were equal to about 2% of sales in Honduras and Guatemala, about 4% of sales in Nicaragua and about 5% of sales in Ecuador (Investment Climate Survey, 2004: 12).

Security costs account for about two-thirds of the cost of crime, while direct losses account for the additional third. The burden of crime is not evenly distributed across firms. In general, manufacturing firms faced fewer losses than firms involved in retail and wholesale trade or construction. Large firms also tended to face higher losses than smaller firms. Firms in Durban faced the heaviest losses, while firms in Johannesburg faced relatively modest losses (Investment Climate Survey, 2004: 12). It is therefore evident that crime is a costly burden to the SME sector and would impact negatively on the growth of the business.

#### **4.3.5 Business Support**

Since 1994 the government has devoted considerable resources to supporting small enterprises. The form of support ranges from the establishment of state-initiated projects to supportive legislation, a variety of funding institutions and government incentives through the Department of Trade and Industry (DTI). The National Small Business Act, passed in 1996, helped to establish many of the supportive structures now in place. Some of these are:

##### **4.3.5.1 Khula**

Khula offers financial support mechanisms to the SMME sector. The financial products include loans, the national credit guarantee system, grants and institutional capacity building. Khula has

also launched its own micro-lending scheme, KhulaStart, an entry-level programme that provides loans to first-time borrowers in the survivalist sub-component of the SMME sector. The organisation has recently launched the Khula Technology Transfer Fund to facilitate access to local and international technology (South African Business Guidebook, 2002/2003: 35).

#### **4.3.5.2 Brain**

The DTI has launched a comprehensive online initiative known as BRAIN (Business Referral and Information Network), offering basic information and essential service links to entrepreneurs. The BRAIN website includes information about the government's incentives and SMME support agencies, as well as links to business centres throughout the country (South African Business Guidebook, 2002/2003: 35).

#### **4.3 5.3 Frain**

The Franchise Advice and Information Network (FRAIN) strives to supply high quality information and support services to individuals and small business (SMMEs) to ensure growth and improvement of new and existing franchise businesses in South Africa (South African Business Guidebook, 2002/2003: 36).

#### **4.3.5.4 Business Partners Limited**

In 1998, the Small Business Development Corporation (SBDC) was transformed into Business Partners Limited. The organisation shifted its focus onto small and medium enterprises, increasing its project involvement to a R150 000 minimum and a R15-million maximum. Business Partners set aside R277.7-million for investment in SMMEs last year. The organisation has invested R4.6-billion in emerging businesses in the past 20 years, directly influencing the creation of 500 000 jobs (South African Business Guidebook, 2002/2003: 36).

#### **4.3.5.4 Small Enterprise Development Agency (SEDA)**

In 2004, the National Small Business Act, 1996 (Act 102 of 1996), was amended to provide for the merging of the Ntsika Enterprise Development Agency and the National Manufacturing

Advisory Centre and the birth of the integrated, single SEDA on 13 December 2004. SEDA aims to: improve geographic outreach, achieve the desired impact on small enterprises, provide a single access point for small enterprises, be inclusive of all relevant stakeholders, leverage resources in service delivery and optimise resource utilization (Small Enterprise Development Agency, 2006: 2).

However, the Global Entrepreneurship Monitor studies and independent surveys have been critical of the quality and reach of this support. A 2004 national survey of small enterprises provides, for the first time, overwhelming confirmation that the government is failing to reach most small enterprises (Small Enterprise Development Agency, 2004: 65). According to the survey, small enterprises are either unaware of or do not use the services offered by the government. Where they do use government support, small enterprises are skeptical about the quality of this support. It is clear that government efforts to promote small enterprises are not well regarded by the firms responding to the survey (Small Enterprise Development Agency, 2004: 66). One reason for this might simply be that small enterprises are unaware of government initiatives to support them or, even if they are aware of them, have not used them. Support to small business entrepreneurs throughout the life-cycle of the business, is imperative for growth and development.

#### **4.4 Conclusion**

The earlier section presented some of the major environmental factors that affect business development. This sets the background for examining the internal and external factors that would be examined in this study. Specifically, the educational level and training of the entrepreneur/business owner, the economy, access to finance, taxation, regulation and laws, human resource practices, technology and innovation, managerial skills and crime will be examined. The following chapter focuses on the formulation of the hypotheses and the research methodology.

## CHAPTER FIVE

### RESEARCH METHODOLOGY

#### **5.1 Introduction**

Knowledge of the relative role of personal and environmental factors in bringing about growth and expansion is important for the field of entrepreneurship. It has been shown that the majority of entrepreneurs can be found in the SME sector. The importance of this sector and its contribution to the Gross Domestic Product and employment cannot be over emphasised. This knowledge would be beneficial in providing insights for government policy. Research on entrepreneurship, thus far, has focused solely on the internal qualities of the entrepreneur.

Multivariate and quantitative studies are studies that relate elements within the entrepreneur, the business operation (internal) and the external environment to the growth of the small business. Such studies illustrate the effects of a large number of factors examined in the relationship between the small business environment (both internal and external) and growth. Due to the complex relationships between factors, more than one factor has to be held constant, thus justifying the use of multivariate analyses. Unfortunately, such studies are few, and results from univariate and qualitative studies had to be taken into consideration in the literature review.

#### **5.2 Statement of the Problem**

The definition of the research problem is of great importance since it guides all subsequent actions. Knowledge of the relative role of personal and environmental factors of this study in bringing about growth and expansion is expected to provide insights for government policy. This study provides evidence on the links between the external and internal environments and the entrepreneur's perceptions of them, with respect to growth. The problem of this study is the effect of internal and external environmental factors on the growth of the small business in the Pietermaritzburg area. The research question can be stated as follows: "What are the perceptions of Pietermaritzburg small business owners/ entrepreneurs of the internal and external business environments with respect to the growth of their ventures."

### **5.3 Research Objectives**

To achieve the above the researcher formulated the following primary objectives.

#### **5.3.1 Primary Objectives:**

- To evaluate the internal environmental conditions that favour or constrain entrepreneurship and small business development in the Pietermaritzburg region.
- To evaluate the external environmental conditions that favour or constrain entrepreneurship and small business development in the Pietermaritzburg region.
- To investigate whether the internal or external set of factors constitute the greater burden on business growth.
- To examine whether policy on small business / entrepreneurship should focus more on the internal conditions or external factors.

#### **5.3.2 Secondary Objectives:**

1. To determine by means of regression analysis the Determinants of Growth (in terms of the number of employees).
2. To determine using factor analysis, the factors (classification) that contribute to the growth of the business.
3. To determine if growth varies with:
  - 3.1 Gender
  - 3.2 Activity
  - 3.3 Ethnicity
  - 3.4 Legal Status
  - 3.5 Educational Level
  - 3.6 Exposure to training
  - 3.7 Source of Start-Up Capital.

## 5.4 Hypotheses

The following hypotheses were set to guide the research in order to achieve the stated objectives.

1.  $H_0$ : Internal Factors do not prevent growth in the Pietermaritzburg region.  
 $H_1$ : Internal Factors prevent growth in the Pietermaritzburg region.
2.  $H_0$ : External Factors do not prevent growth in the Pietermaritzburg region.  
 $H_1$ : External Factors prevent growth in the Pietermaritzburg region.
3.  $H_0$ : There is no difference in the average growth between males and females.  
 $H_1$ : There is a difference in the average growth between males and females.
4.  $H_0$ : There is no difference in the average growth between ethnic groups.  
 $H_1$ : There is a difference in the average growth between ethnic groups.
5.  $H_0$ : there is no difference in the average growth between activities of business.  
 $H_1$ : there is a difference in the average growth between activities of business.
6.  $H_0$ : there is no difference in the average growth between legal statuses of business.  
 $H_1$ : there is a difference in the average growth between legal statuses of business.
7.  $H_0$ : there is no difference in the average growth between education level groups.  
 $H_1$ : there is a difference in the average growth between education level groups.
8.  $H_0$ : Sources of start-up capital do not account for a difference in average labour growth.  
 $H_1$ : Sources of start-up capital do account for a difference in average labour growth.
9.  $H_0$ : there is no difference in the average growth between business managers/entrepreneurs who have been exposed to training and to those who have not been exposed to training.  
 $H_1$ : there is a difference in the average growth between business managers/entrepreneurs who have been exposed to training and to those who have not been exposed to training.

## **5.5 Research Design**

This study is a cross-sectional, quantitative formal study, using the survey method to attempt to establish a relationship between small business owner's / entrepreneur's perception of the business environment (internal and external) with respect to growth in Pietermaritzburg.

### **5.5.1 Sampling Design**

A population is the total collection of elements about which inferences are to be made. The objective of sampling is that by selecting some of the elements in a population, conclusions about the entire population can be made. The ultimate test of a sample design is how well it represents the characteristics of the population it supposedly represents (Wegner, 2002: 168).

The reasons for sampling in this study include:

- Lower Cost,
- Greater speed of data collection, and
- Time constraints.

For the purposes of this study the population is defined as: Small, Medium and Micro Enterprises in Pietermaritzburg. It is possible to construct a so-called sampling frame, by drawing a sample from the total population. Due to the fact that no complete list exists for SMME's in Pietermaritzburg, a database of VAT registered SMME's, obtained from the Pietermaritzburg Chamber of Commerce, was used to draw the sample.

Since the aim of the study is to make probability-based confidence estimates of certain parameters, systematic random sampling was utilised. The sample size was influenced by the research hypotheses as theory dictates that there must be sufficient number of cases to examine research hypotheses properly. Generally the literature considers 100 cases in a sample as the bare minimum (Spiegel, 1992: 175). Taking the above factors in account it was decided to distribute 250 questionnaires.



### **5.5.2 The Measuring Instrument / Questionnaire (Refer to Appendix B)**

There is no simple answer to which of the available methods of data collection the researcher should use when collecting data. Cooper and Schindler (2001: 210) cite three major criteria for evaluating a measuring tool. These are:

- Validity refers to the extent to which the test measures what we actually wish to measure.
- Reliability has to do with the accuracy and precision of a measurement procedure, and
- Practicality is concerned with a wide range of factors of economy, convenience and interpretability.

An attempt was made to achieve content validity by ensuring that the instrument provided adequate coverage of the investigative questions guiding the study. This was possible as an extensive search of the literature covering problems and constraints facing small businesses were made.

In terms of improving the reliability of the questionnaire, four principles outlined by Newman, (1997: 183) were followed to increase the reliability:

- The researcher clearly conceptualised the constructs,
- Precise measurements were used( i.e., the Likert- based scale and the dichotomous strategy),
- Multiple indicators were included (i.e., open-ended and closed-ended questions), and
- Pilot tests were employed.

The primary method used to gather data was the survey method. This method was developed in the form of a self-administered questionnaire. The questionnaire consisted of open- and close-ended questions designed in accordance with the research objectives with the intention of extracting the most relevant information. The close-ended questions used in this study offer the participant a selection of possible alternative responses allowing the researcher to gather

quantitative data. Open-ended questions are described as free response questions in which the participants express their views openly (Oppenheim, 1992: 112).

Ten pilot questionnaires were initially distributed. The pilot participants were well-established business owners. The pilot questionnaire had many functions; namely, to test the questions for content and understanding, to assess how long it would take to complete the questionnaire and, finally, to ensure that the instructions were clear and easy to follow. Pilot samples in academic studies are widely used and recommended. The pilot questionnaire assists in identifying any problems in the questionnaire. In addition, it assists the researcher to perfect the questions prior to distribution (White, 2000: 31-52, and Riley *et al*, 2000: 98).

The pilot participants responded to the questionnaire as follows: the questions were found to be simple and understandable, the test took the pilot sample approximately 10 minutes to complete and the instructions were clear and easy to follow. The questionnaire was designed to extract as much information as possible, and in accordance with the research objectives. The questionnaire was divided into the following two sections:

#### **5.5.2.1 Section A: Demographics (Refer to Appendix B)**

The following variables were selected for the purposes of this study:

- Gender
  
- Ethnic Grouping
  
- Level of Education: Research has consistently shown that higher levels of education result in profitable and expanding businesses. It was hypothesised that higher levels of education will result in higher growth.
  
- Business Activity: It was hypothesised that certain sectors would show more growth than others as found in the literature review.

- Legal Status of Business: Literature states that the close corporation is the choice as it offers advantages of limited liability and access to finance.
- Source of Start up Capital: Depending on the age of the business, it is hypothesised that most businesses would have used personal funds as the cost of finance was high and access to credit difficult.
- Exposure to Training: Research has shown that those that have undergone some form of training will be better equipped in growing and developing a business.

#### **5.5.2.2 Section B: Firm Specific Data (Refer to Appendix B)**

This section makes use of the Likert based scale where a score of:

- 1 = Strongly Disagree
- 2 = Disagree
- 3 = Neither agree nor disagree
- 4 = Agree
- 5 = Strongly Agree

Q11 and Q12 asked respondents to indicate the ways in which they would like to expand their business, while Q12 provided alternatives needed for the expansion process. The researcher felt that those that indicated moving into new markets and introducing new products and services displayed innovativeness and risk taking. Those that merely wanted to increase turnover with the same products were not really determined to grow as the small business operates in a saturated market. From the alternatives provided those that indicated expansion of premises and investment in more capital equipment show their willingness to grow.

Q13 asked respondents how they would fund their growth. The choices given were internal, external or a combination of both. The researcher hopes to gauge from this question the availability of external finance for small business owners.

Q14 provided a list of internal and external factors that constrain or retard growth, which the respondents had to rate. The researcher will, using the responses received determine whether these internal or external factors prevent growth in the Pietermaritzburg region.

Q15 list different taxes that impact on the small business owner. The respondent is required to rate these different types of tax in terms growth retardation.

Q16, linked to Q15 asks the respondents to show how burdensome taxation is to the small business owner, by rating the alternatives provided.

Q17 provides a list of other regulations that the respondents have to rate as an obstacle to the growth of their business.

Q18, 19, 20, 21, & Q22 all relate to crime. The respondents are initially asked to rate crime as a very big problem, a fairly big problem, not a very big problem or not a problem at all. Using the responses received the researcher can determine if crime is a problem in the Pietermaritzburg area. The respondents were then asked if they were victims of crime within the last twelve months and to indicate the frequency of such crimes. They were also asked to state the types of crimes they suffered and lastly they had to indicate the cost of the crimes they suffered. From this the researcher will determine the impact of crime on the growth of the small business.

Q22 and Q23 dealt with staff training and development. Respondents were asked if they provided training and development for their staff within the last twelve months and to indicate the nature of such training. Staff training and development is well documented in research papers and texts and leads to growing and profitable businesses. Using the responses received the researcher can determine the extent to which Pietermaritzburg business owners are willing to train staff and expand their businesses.

Q25, 26 & 27 all deal with technology and the use of computers. Respondents are asked if they utilize computers and to indicate the use thereof. They are finally asked to indicate if the use of such technology is helping them to grow the business. The value of technology such as computers can then be determined in terms of business growth.

Q28 & 29 asked respondents to indicate if, with regards to innovation and the conduct of their business, they are doing something different that competitors cannot replicate. This determines the level of innovation of the small business community in Pietermaritzburg.

Q30 & 31 was based on business support. Respondents were asked if there was sufficient business support in the Pietermaritzburg area and to indicate from the alternatives provided the support organizations they knew. From this the researcher can determine if business support is helping small business in Pietermaritzburg. The awareness of the different support organizations can also be gauged.

Q32 asked respondents to provide data on their sales and the number of people employed, on the basis of which average growth in labour was calculated.

### **5.6 Data Collection**

After obtaining ethical clearance from the University of Kwa-Zulu Natal (Appendix A), the questionnaires were hand-delivered to the 250 respondents during the 20<sup>th</sup> – 31<sup>st</sup> July 2006. Some respondents answered the questionnaires immediately while others preferred the researcher to collect the completed questionnaires after a period of two days. Before administering the questionnaire, the respondents were briefed about the study and the consent form (Appendix C) was completed and the confidentiality clause explained. On receiving the completed questionnaires, the researcher checked them for completeness. A total of 160 completed questionnaires were finally collected representing a 64% response rate.

### **5.7 Data Processing**

The completed questionnaires were coded and the responses were captured in the SPSS statistical software programme. The analyses of the data were done using SPSS.

### **5.8 Descriptive Statistics**

An important aspect of the description of a variable is the shape of its distribution, which tells the frequency of values from different ranges of the variable. Simple descriptive statistics can

provide some information about this issue (Spiegel, 1992: 58). The mean, the mode, the median, the sample variance and the sample standard deviation was considered in this study. The mean or the arithmetic mean is the sum of all the values divided by the sample size, the mode is the most frequent response given by the respondents and the median is the middle most value when the data (per variable / question) is arranged from highest to lowest. The sample variance is the degree or quantity by which each observation varies one from another. The sample standard deviation is the square root of the sample variance (Spiegel, 1992: 87).

### **5.9 Factor Analysis**

Factor analysis evaluates all variables simultaneously with the objective to group variables that belong together and have overlapping measurement characteristics together. The main applications of factor analytic techniques are:

- to reduce the number of variables, and
- to detect structure in the relationships between variables, that is to classify variables.

Factor analysis was conducted to determine whether the internal or external factors contribute more to the growth of the business. The results of this analysis were also used to determine whether policies and support programmes should concentrate more on the internal or external environments.

### **5.10 Variance Analysis**

The statistical method for testing the null hypothesis that the means of several populations are equal is analysis of variance (ANOVA). This data analysis technique examines the significance of the factors (= independent variable) in a multi-factor model (Wegner, 2002: 214). This method of analyses was used to test for differences between average growth and gender, activity and ethnicity.

### **5.11 Chi Square Test**

Wegner (2002: 248) states that there are three areas in inferential statistics where the Chi Square test for significance is commonly applied. These are:

- Tests for independence of association,
- tests for equality of proportions in more than two populations, and
- goodness of fit tests

The Chi-Square test for independence of association was used to determine whether internal and external factors constrain growth of the business in the Pietermaritzburg region.

### **5.12 Regression Analysis**

Regression analysis is a statistical method that is used to quantify and describe possible relationships between variables (Wegner, 2002: 303). Multiple regression analysis was utilised to discover the relationship of internal and external factors on the dependent variable, average growth. Different models were fitted to check the variation and influence of the independent variables, which are different groupings of questions measuring a certain trait against the dependent variable, average growth in the number of employees.

### **5.13 Reliability Testing**

Reliability testing was done in order to determine whether the questionnaire and the results obtained were reliable and that the results obtained were true and realistic findings. Cronbach's alpha was also calculated as part of the reliability test to assess how valid the results were and whether we will get similar results to generalise if we increased the sample size. A value of 0.7 or higher is a very good value that can lead us to conclude that we will get the same results if we carried out this survey with a larger sample of respondents (Burns and Bush, 2000: 329). The Cronbach's alpha was calculated using questions 11, 12, 13, 14, 15, 16, 17 and 22 because they have the same scales.

### **5.14 Conclusion**

This chapter provided an in depth analysis of the research methodology that was used to achieve the research objectives. The following chapter presents the results of the analyses.

## CHAPTER SIX

### RESULTS

#### 6.1 Introduction

This chapter presents the results of the analyses of the data obtained from the questionnaires. These results were obtained using the statistical methods explained in the previous chapter. The results are presented as per the questions of the questionnaire and as per the objectives and hypotheses of the previous chapter. The chapter is structured in this manner so that conclusions can be made in terms of the hypotheses formulated.

#### 6.2 Descriptive Statistics

This section provides a profile of the businesses and of their entrepreneurs surveyed for this study. The sample comprised of 160 business persons: 96 males and 64 females.

#### Q1 Number of years your business is in operation.

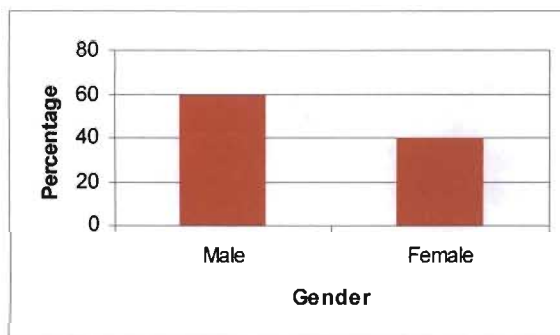
Table: 6.1: Age of Business

	N		Mean	Median	Mode	Std. Deviation	Variance	Range	Minimum	Maximum
	Valid	Missing								
Q1	160	0	9.2219	8.0000	5.00	5.91628	35.00235	37.00	2.00	39.00

The age of the businesses ranged from 2 to 39 years (table: 6.1). The mean age of the businesses sampled is 9.22 years. The modal age of the sample is 5 years.

#### Q2 Gender

Figure: 6.1: Gender of Respondents



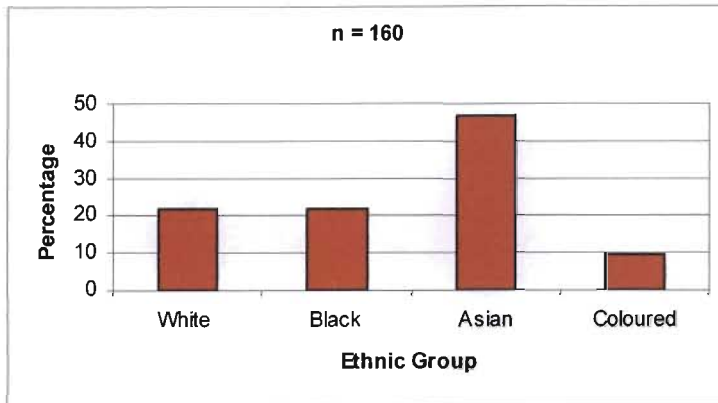
Of the sample, surveyed 96 were male and 64 were female. This translates to 60% males and



40 % females (figure 6.2).

### Q3 Ethnic Distribution

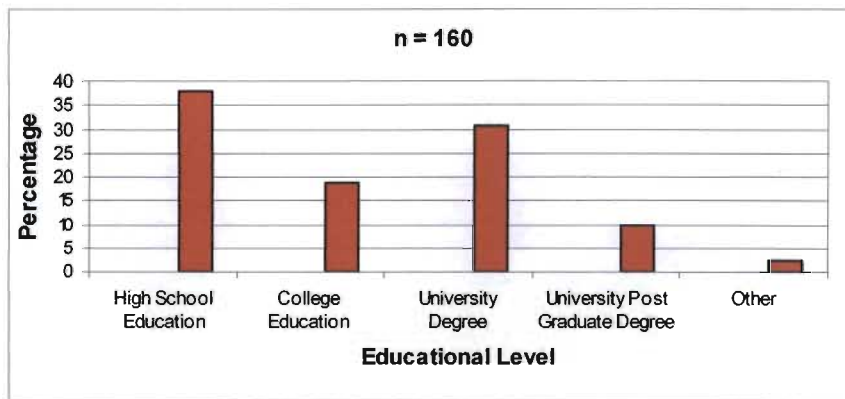
Figure: 6.2: Ethnic Distribution



The sample was representative in that it consisted of all ethnic groups. The modal ethnic group was the Indians (Asians) 46.9%, followed by the whites and blacks with 21.9% each. The representation of coloureds tallied 9.4%.

### Q4 Educational Level of Respondents

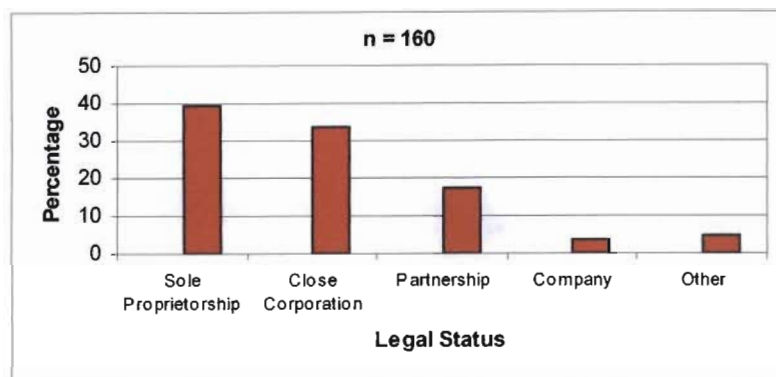
Figure: 6.3: Educational Level of Respondents



The above table shows the educational level of the sampled businesses. High school education was possessed by 38.1% of respondents, college education by 18.8%, University degrees by 30.6% and University postgraduate degrees by 10% of respondents.

## Q6 Legal Status of Business

Figure: 6.4: Legal Status



Most of the businesses surveyed were sole proprietorships (39.4%), and close corporations (33.8%). This result is similar to the findings of a study done in Pietermaritzburg in 2003. In that study 61% of businesses sampled were sole proprietors (Pather, 2003: 47).

## Q7 Source of Start-Up Capital

Table: 6.2: Source of Start-up Capital

	N		Mean	Median	Mode	Std. Deviation	Variance	Range	Minimum	Maximum
	Valid	Missing								
Q6	160	0	2.1698	2.0000	1.00	1.14851	1.31908	2.00	1.00	3.00

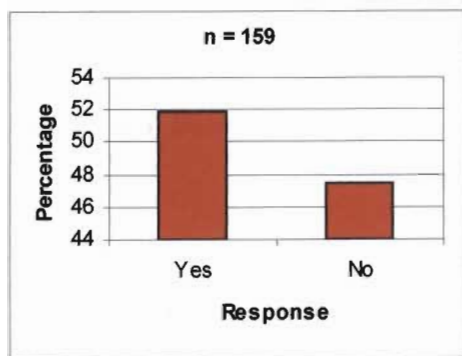
The questionnaire provided respondents with three alternatives to this question. These were internal (1: personal), external (2: banks, investors) and a combination (3) of both. From table 6.2 we see that the modal response is 1. This indicates that the common or most frequent source of start up capital is personal funds. A possible reason is that the cost of external borrowing is high and this forces entrepreneurs to make use of personal funds. Internal funding includes borrowing from friends and family members.

## Q8 Exposure to Training

Of the surveyed entrepreneurs, about 52% (figure 6.5 below) were exposed to some form of training while 47.5% of business owners had no training at all. The researcher is of the opinion

that those owners that underwent some form of training or have prior work related experience will show a higher growth rate compared to those that have none.

Figure: 6.5: Exposure to Training



### Average Growth of the Business

The following formula was used to calculate the average growth in the number of employees.

$$averageGrowth = \frac{L_1 - L_0}{L_0 \times n}, \text{ where: } L_1 = \text{Number of Employees as at 2005.}$$

$L_0$  = Number of Employees at Inception.

$n$  = Number of Years the Business is in Operation.

The results are presented in table (6.3).

Table: 6.3: Average Growth

Mean	12.5010
Median	4.8000
Mode	.00
Std. Deviation	32.37614
Variance	1048.21418
Range	324.00
Minimum	.00
Maximum	324.00

The sample average growth in employees is 12.5010. This implies that of the sampled businesses, the average growth in the number of employees is 12.5010 per year. Such a value indicates that the small business sector in Pietermaritzburg, is a good contributor to employment. This is also indicative of the potential that the small business has to reduce unemployment in South Africa as a whole.

### Q5 Distribution by Sector

The questionnaire provided nine different sectors to the respondents. For the purposes of analysis the number of sectors was scaled down to five as indicated in (figure 6.6) below. The other (major) category represents a combination of transport, construction, travel and tourism, agriculture and financial sectors. The 'other' category represents the franchise businesses.

Figure: 6.6: Distribution by Sector

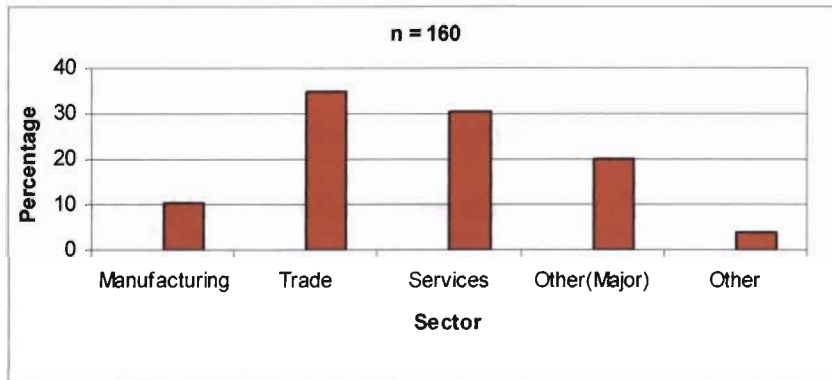
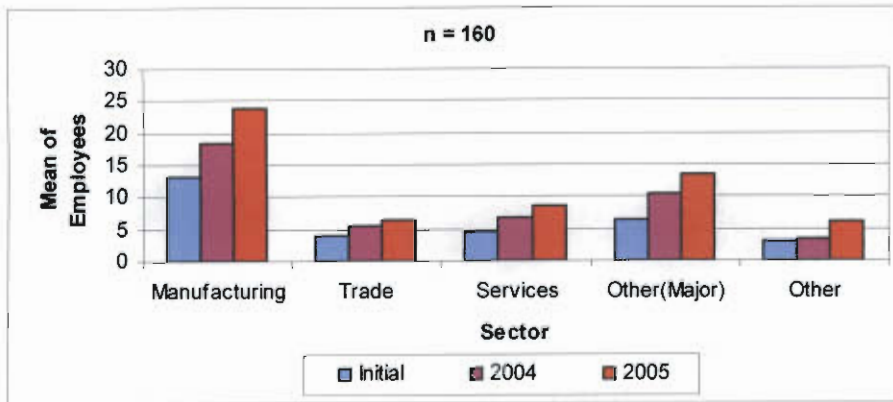


Figure 6.6 shows the distribution of the sampled businesses across the different sectors. The majority of the sampled businesses (35%) belonged to the trade sector. The services sector was represented by 30.6% of surveyed businesses. Manufacturing consisted of 10.6% of surveyed businesses and 3.8% of franchised (other) outlets were surveyed. The major (other) category represented 20% of the surveyed sample.

### Q5 Distribution of the Number of Employees per Sector

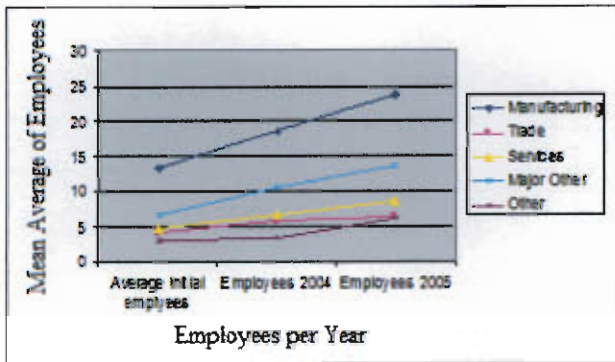
Figure 6.7 below, illustrates the number of employees hired by the surveyed firms at the founding stage and in the last 2 years. Although all sectors surveyed show an increase in the mean number of employees, manufacturing ventures were employing more labour throughout than the other types of business. At inception, the manufacturing sector had a mean employment of 13.24 units of labour and in 2005, the sector recorded a mean of 23.82 units. This indicates that in the Pietermaritzburg region, the manufacturing sector is by far the largest contributor to employment growth.

Figure: 6.7: Distribution of Employees per Sector



A means plot was generated to highlight these results more clearly.

Figure: 6.8: Means plot for Employees

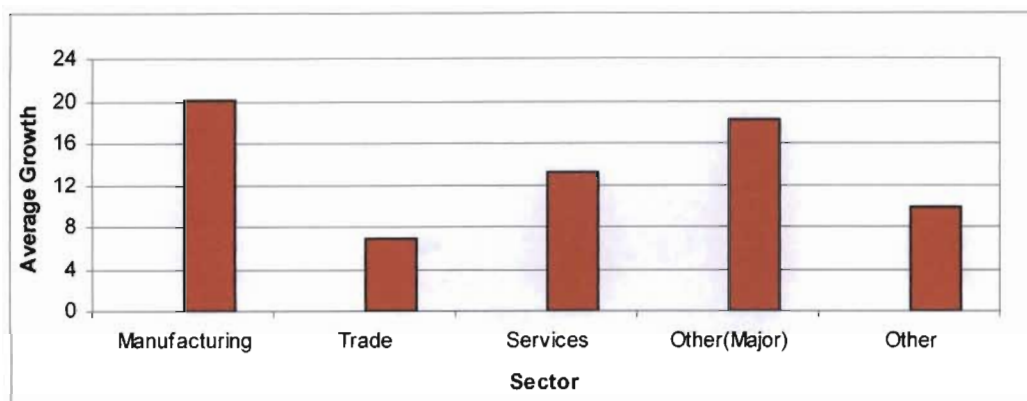


Clearly evident from these results is the fact that the number of employees per sector has been increasing over the life-span of the business (figure 6.8). The largest increase was recorded by the manufacturing sector, which had a mean labour employment value of 13 in the founding period and 23 units of labour in 2005. The trade sector shows the lowest mean labour employment, 4 units in the founding period and 6 units in 2005.

Figure 6.9 below shows the average growth in terms of labour employment for the different sectors. The average growth in labour employment of the surveyed businesses ranged from 20.0493 units for manufacturing to 6.7988 units for firms in the trade sector. The major other category (consisting of a combination of transport, construction, travel and tourism, agriculture and financial sectors) indicated an average growth of 18.2202 units while the services sector had an average growth of 13.2101 units. The 'other' category representing the franchised firms

recorded an average growth of 9.9333 units of labour. These results (figure 6.9 below) show that firms across all sectors surveyed have grown their businesses since inception. This bodes well for the Pietermaritzburg economy and serves to qualify a Business Confidence Index of 85 (page 30).

Figure: 6.9: Average Growth per Sector



## Factors Contributing to the Growth of Firms in Pietermaritzburg

### Educational Level

It is well documented that business growth and success are products of higher levels of education (Storey, 1994: 129; Small Enterprise Development Agency, 2004: 62; and Von Broembsen *et al*, 2005: 29). In most studies, education has served as a proxy for entrepreneurial skills and abilities. In addition, it has been shown that specific forms of knowledge-intensive education, such as engineering, computer science, and biochemistry, provide the recipients of such education an advantage if they start a firm that is related to their area of expertise (Barringer *et al*, 2005: 678).

Figure 6.10 below, illustrates the mean employment units in relation to the educational level of the entrepreneurs. Although an increase in the average number of employees is evident over the lifespan of all surveyed business, those in possession of University Post Graduate degrees experienced the highest growth in the average number of employees. The average growth should show similar results.

Figure: 6.10: Educational Level Vs Labour Employment

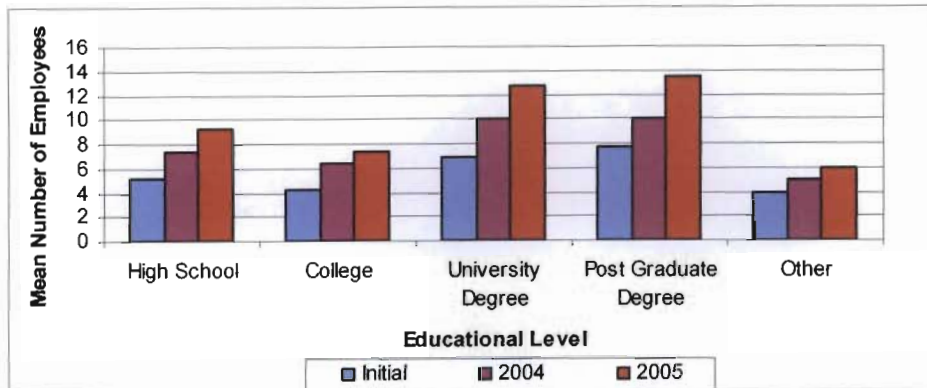
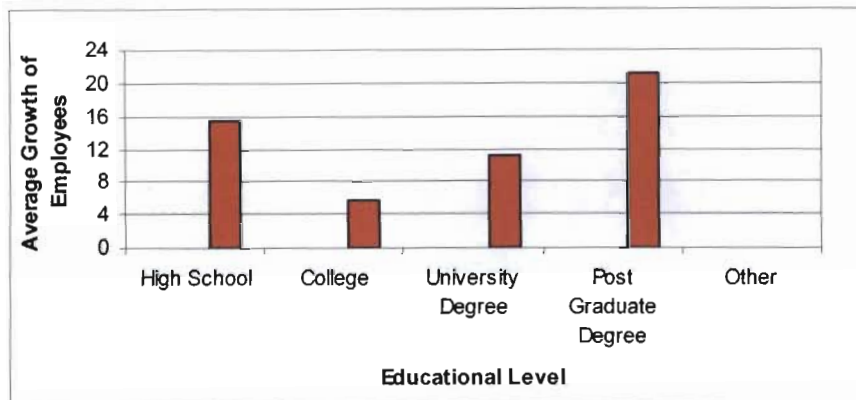


Figure: 6.11: Average Growth of Employees Vs Educational Level



One can see clearly that the respondents that had a University Post Graduate Degree had the highest average growth of 21.2214 followed by the High school education (15.5240) and then University degrees (11.0763). College education recorded an average growth of 5.7165 employees per year. This confirms the surveyed literature that higher educational levels of owners, result in the growth of the business, reflected in employment numbers for this study.

### Training

Business owners / managers / entrepreneurs that have undergone some form of training are better equipped at operating and making the venture successful. This training includes on the job training, learnerships, apprenticeships or prior work experience in the same field as the current business. Storey (1994: 133) strengthens this argument by reviewing two studies and concludes that individuals with business skills are more likely to form businesses that experience growth than individuals with other functional skills.

Table: 6.4: Training versus Average Growth

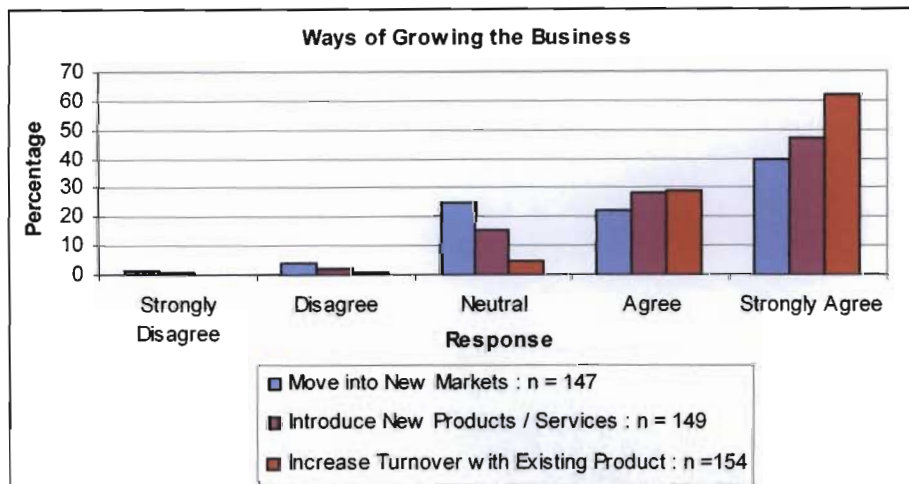
Exposure to Training	Average growth of employees
yes	15.9634
no	13.2594

From table 6.4 it is evident that those that were exposed to training recorded a higher average growth in employees than those that had no exposure to training. This result is in keeping with the literature reviewed.

### Q11 Ways of Looking to Grow the Business

Businesses can grow in different directions. Figure 6.12 below examines the perceptions of respondents with respect to growing their businesses.

Figure: 6.12: Methods of Growing the Business



Growth strategies are discussed briefly to illustrate the routes that business owners can employ. Some can take the route of growth through new markets by targeting the same product at new markets or by diversifying and targeting different products at different markets. Others could take the route of new products and services and target existing markets using a product development strategy. Some may try to increase turnover by driving down costs and penetrating existing markets through increased advertising (Mintzberg *et al*, 2005: 107). The growth orientations of the surveyed businesses are presented in figure 6.12 above, and the responses were based on a five point Likert scale.



The results indicate that almost 62% of respondents would like to expand their business by moving into new markets. This approach requires thorough market research in order to segment the population and position the products. A majority of 75% of respondents would like to expand their business by introducing new products or services. Such a strategy requires strong innovations. Another approach to business growth is to look at the existing product/market configuration more extensively. About 91% of the respondents indicated that they would increase their turnover by servicing the current market. This is the easiest route and requires driving down costs and aggressive marketing tactics, and seems to be the most preferred route of surveyed businesses.

### Q12 Requirements for Growing the Business

Growth of a business often entails the recruitment of more staff members, expansion of premises, investing in more capital equipment and obtaining finance to undertake the above plans. However, problems can be experienced in the pursuit of any one of the above choices. According to Storey (1994: 122) the willingness to grow and expand and grow is a function of the starting resources of the entrepreneur, the business itself and the strategy employed by the business. As expounded in chapter 2, the business undergoes different stages and each stage is characterised by changing management styles and organisational structures. These changes can be in the form of employing more staff, expanding existing premises, investing in more capital equipment and the borrowing of funds.

Figure: 6.13: Requirements for Growth

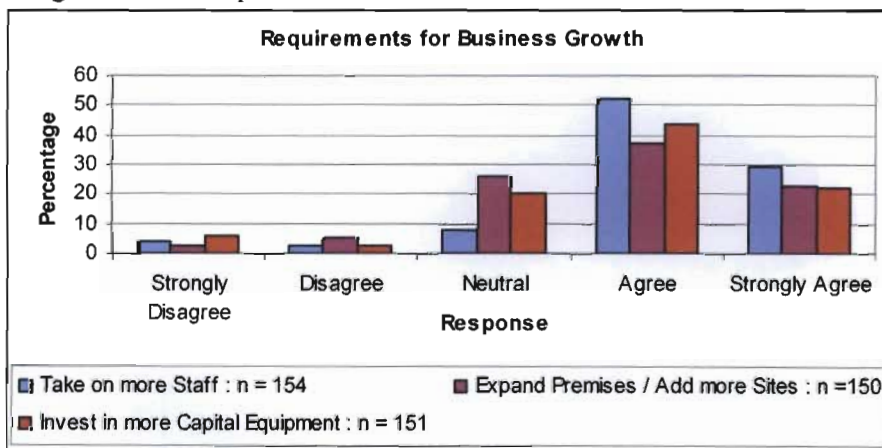


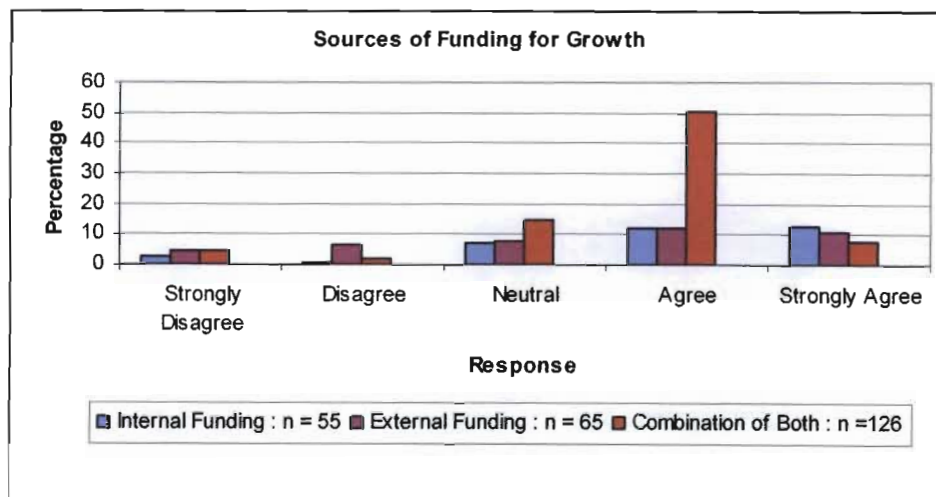
Figure 6.13 above, illustrates the surveyed responses to the requirements for growth. A majority (82%) of respondents in Pietermaritzburg would like to grow their businesses by employing more staff. If the existing physical infrastructure is inadequate or small, growth may also entail the expansion of the business premises or the acquisition of additional sites. This is aim of 60% of surveyed respondents. Business growth also entails the acquisition of more capital equipment as production increases due to increasing demands. Figure 6.13 illustrates that about 66% of the respondents would like to invest in more capital equipment in order to ensure the growth of their businesses.

In order to accomplish the above, funds are a pre-requisite. The following question determines the source of funding that is most commonly used.

#### Q12.4 Sources of Funding for Growth

There are two sources of finance that a small business can utilise. One is debt that is money borrowed from a bank at a certain cost. This type incurs costs in the form of interest. The second is equity or personal funds (internal) of the owner. A third option is to make use of both internal and external funding (Barrow, 1994: 66). Lack of finance can be a serious factor inhibiting the growth of a business. This is more so if the internal sources of funding are inadequate and the business entrepreneur experiences collateral problems in tapping into external funding. However, external funding is a commonly used source for many businesses.

Figure: 6.14: Sources of Funding for Growth



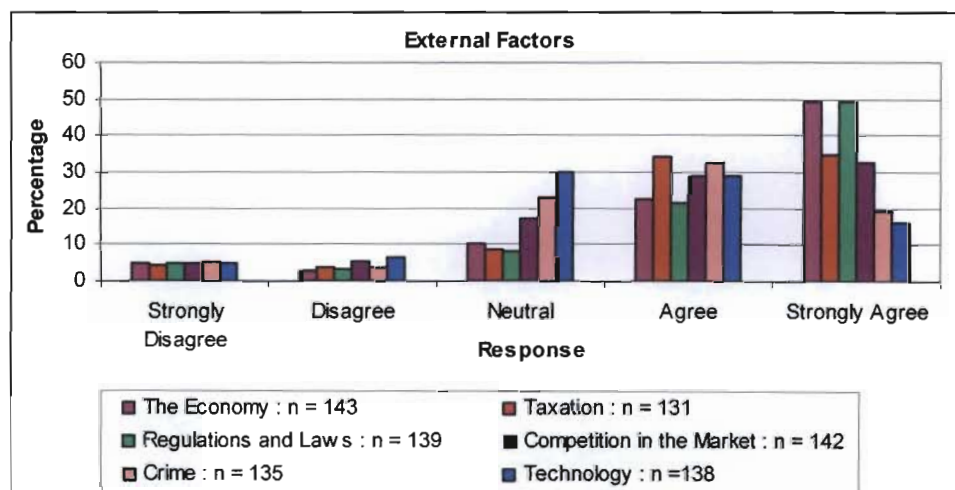
Analysis of the results, indicate that 24.4% of the respondents are willing to use external financing to grow their businesses while 22.5% of the respondents indicated that they are willing to use their own finance to grow their businesses as indicated in figure 6.14 above. However, seeking external funding may be a costly exercise, as high interest rates have to be paid over the duration of a loan. The risks of payment on time have to be borne. Businesses may take a more cautious route in funding their growth by using a mix of internal and external sources. This study reveals that 58% of the respondents were willing to use a combination of internal and external sources to fund the growth of their businesses.

### Q14 Internal and External Constraints to the Business

Thus far, the perceptions of the growth orientations of surveyed respondents have been determined together with their growth requirements and choice of funding. It is now appropriate to look at their perceptions of internal and external factors with respect to growth. For ease of presentation and interpretation, the variables are grouped into internal and external factors.

#### 14.1 External Factors

Figure: 6.15: External Environmental Factors



**The Economy:** A growing economy creates more ‘space’ for the growth of a business as with growth, income generation and expenditures are associated. Economic forces impact heavily on business. As these forces are beyond the control of the business, managers therefore need to anticipate changes and react timeously and efficiently. The macroeconomic forces include economic growth (Gross Domestic Product), interest rates, inflation and unemployment (Fry *et*

*al*, 2000: 165). About 71% of the surveyed businesses (Figure: 6.15 above), felt that the economy is an inhibitory growth factor.

**Taxation:** Tax is a financial contribution that is paid to the government for the provisions of educational facilities, health and social services, recreational facilities and defence and security. High tax rates and complex tax administration is a significant constraint for the small business (Longernecker *et al*, 1994: 685). Furthermore, the Small Business Project's: Counting the cost of Red Tape has shown that the cost of tax compliance is regressive and the small business pays almost 3% of annual turnover (Small Business Project, 2005: 46). A majority of 69% of the surveyed respondents felt that taxation was a constraint to the growth their business.

**Regulations and Laws:** These are vital to the fair and sustainable working of market economies, but even the most socially necessary regulations create costs as well as benefits, and some of these costs may be unnecessarily high, especially for the small business that has to understand and comply with these laws and regulations. International evidence suggests that the regulatory environment has a major influence on the survival and growth of the small business (Orford, 2004: 51). A massive 71% (figure 6.15) of respondents in Pietermaritzburg are of the opinion that regulation and laws are a constraint to the growth of their business.

**Technology:** The economic environment determines the direction of technological innovation. Entrepreneurial ability on the other hand determines how much of this technological innovation can be absorbed. According to Von Broembsen *et al* (2005: 33), the growth potential of South African enterprises is enormous if they are able to apply the latest technologies to their products and services. However, the small business may find new technology inaccessible owing to the cost involved or to a lack of knowledge and experience. Of the surveyed respondents (figure 6.15), 45% view technology as constraint while 30% remained neutral. Therefore, the growth potential of the small business sector in Pietermaritzburg, can be enhanced through the application of technology.

**Competition:** A business is faced with competition from three different sources. These are brand competition from marketers of directly similar products, substitute products that satisfy the same

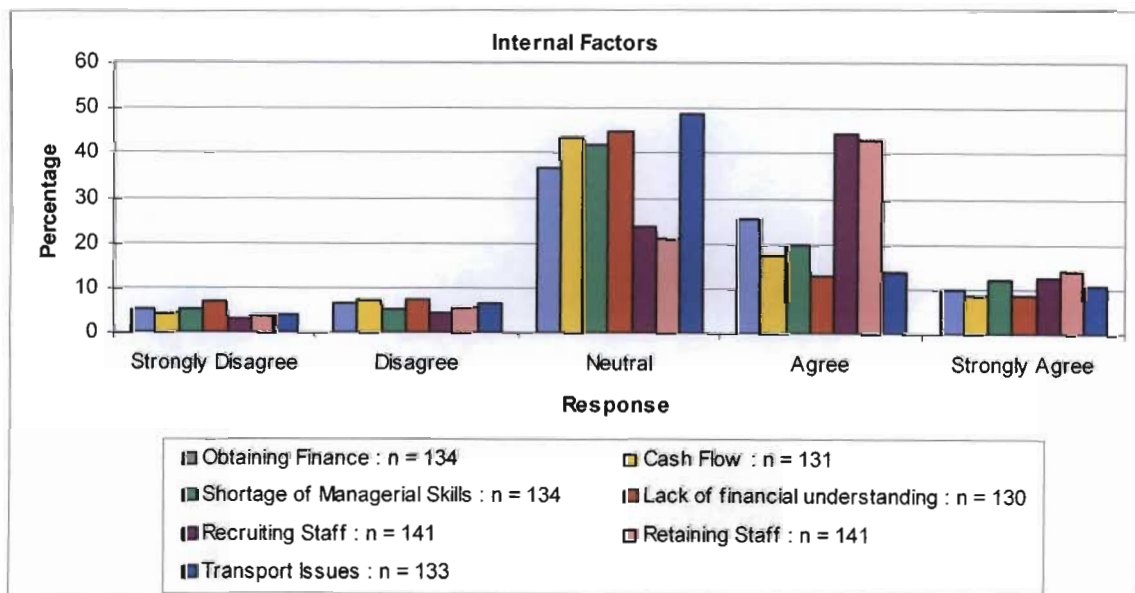
need and competition for the customer's limited buying power (Perreault and McCarthy, 2002: 99). Competition, then, can severely constrain the growth of a business. In Pietermaritzburg, 61% (figure 6.15) of the respondents perceive competition in the market to constrain business growth. Because the small business operates in saturated markets, strategic planning is of utmost importance in order to grow the business.

**Crime:** High crime rates and continuing violence are serious obstacles to small business growth as they increase the risks and often cause major losses of stock, damage to buildings or reduced turnover. The surveyed literature (Investment Climate Survey, 2004: 96), has shown that losses due to crime, across all sectors amounted to 2.272 million of Rands. Crime in Pietermaritzburg (52%) is seen as a constraint to the growth of the business.

### 14.2 Internal Factors

Internal factors are factors that originate from within the business. These factors may arise due to deficiencies in the organisational structure, human resources or business management skills. Figure 6.16 below, shows the recorded responses to internal factors as constraints.

Figure: 6.16: Internal factors



**Obtaining Finance:** Access to and the cost of finance can be a serious factor that constrains the growth of a business (Mahadea, 1997: 72 and Murphy, 1996: 22). In this study, about 11% of the

respondents felt that obtaining finance is not a problem. About 37% were neutral in their response. However, about 35% (figure 6.16 above) of the respondents felt that obtaining finance to grow their businesses is a constraint.

**Cash Flow:** Income and expenditure are activities of every business. The manager has to ensure that the amount of cash flowing into the business exceeds that flowing out. Although some businesses operate with a negative cash flow, the ideal is always a positive cash flow. Given the centrality of cash flow to the survival of a business, it seems reasonable to deduce from this that proficiency in financial administration and management can be expected to reduce the probability of business failure and therefore becomes a pre-requisite for business growth and expansion (Orford *et al*, 2003: 46). Although the modal response to the question on cash flow (43.8%) was neutral, 26% of respondents consider cash flow to be an obstacle to the growth of their businesses (figure: 6.16 above).

**Shortage of Managerial Skills/ Business Expertise:** Managerial skills of planning, organising, leading and controlling are imperative for venture start-up as well as growth and development of the business. Coupled with this is business expertise and strategic decision-making that is required to grow and develop the business. A lack of these skills often results in failure of the business or high costs involved in acquiring the services of consultants to perform these functions. Hodgetts and Kuratko (1995: 17) support this argument. Of the respondents surveyed, 41.9% remained neutral whilst 31.9% of respondents agreed that shortage of managerial skills / business expertise is a constraint to the growth of their business.

**Lack of financial Understanding:** Lack of financial understanding such as incorrect bookkeeping and financial records can seriously affect the general operation of the business. Such a lack of understanding has the ability to cause failure or hinder the growth of a business. An analysis of the data reveals that the modal response to the question was “neutral” (45%). From (figure 6.16), about 22% of respondents agree that a lack of financial understanding retards growth of the business.

**Recruiting Staff:** Every business uses resources (such as capital, machinery, buildings, human capital, etc.) in the pursuit of its objectives. As the business grows, recruitment of staff requires

more time and attention, as suitably qualified staff needs to be employed to perform specific functions. The Investment Climate Survey (2004: 66-69) has shown that a lack of worker skills and labour regulations make recruitment difficult and constrain the growth of the business. Of the surveyed businesses, 57 % felt that recruiting staff was a constraint to the growth of their businesses.

**Retaining Staff:** Once the staffing requirements of the business, have been determined, the onus is on the manager to retain the employees. This can be achieved through employee training and development, incentives and industry related salaries. Of the surveyed businesses, 58% (figure, 6.16) of the respondents felt that retaining staff was a constraint to the growth of the business.

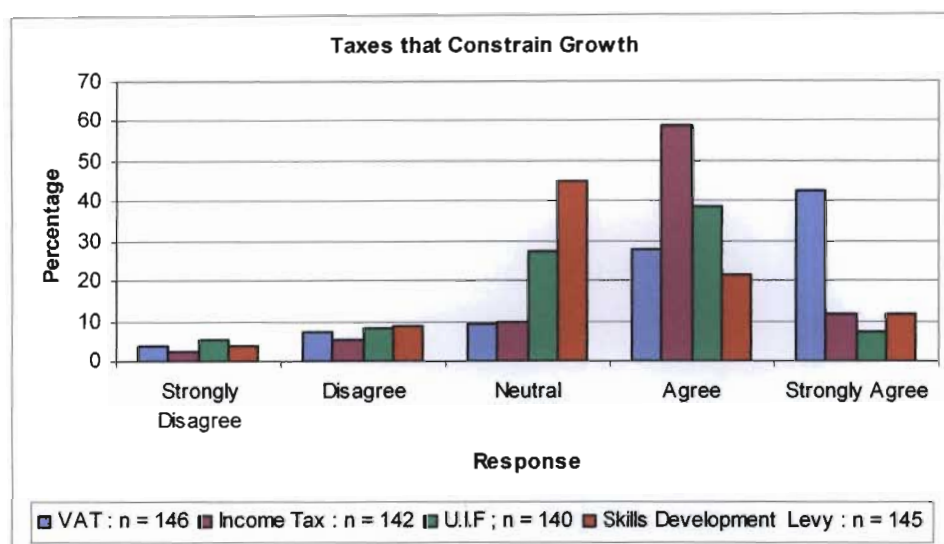
**Transport Issues:** Transport issues are important for any business as the cost of transport erodes profits. Although the choice of mode depends on the nature of the product, of significance is the reliability of delivery, from suppliers and to customers. Constantly rising fuel prices place a heavy cost burden on the small business. A 48.8% neutral response (figure 6.16) was obtained for this question. However, 24% of the respondents perceived transport issues to constrain business growth in Pietermaritzburg.

#### **Q15: Taxes that Constraint Growth**

The small business owner/entrepreneur has numerous taxes to comply with. These taxes place a severe burden on the owner in terms of money, administration and paperwork and time. The Small Business Project (2005: 46) has shown that the cost of tax compliance is regressive and costs the small business almost 3% of annual turnover. Such regulations severely constrain the growth of the business. The taxes reviewed in this study were Vat, income tax, Unemployment Insurance Fund (UIF) and the Skills Development Levy.

**VAT:** An invoice-based value-added tax (VAT) has been in force since 30 September 1991. Most transactions involving goods (including immovable property) and services attract VAT. The rate of VAT is 14% and the tax is levied on the value added in each transaction (Roux, 2002: 83). A majority (71%) of surveyed respondents, (figure 6.17 below) indicated VAT as a constraint to business growth.

Figure: 6.17: Taxes that constrain Growth



**Income Tax:** South Africa has a progressive tax system that places a burden on the economy. Small business corporations (namely corporations having an annual turnover of less than R5 million and which meet certain specified requirements), are taxed at the rate of 15% for the first R150 000 of taxable income, and at 30% for amounts in excess of R150 000, (exclusive of secondary tax on companies - the effective rate will increase in respect of profits distributed by way of dividend) (Small Enterprise Development Agency, 2006:8). Income tax severely constrains the growth of the small business. A tax annuity has been granted to small businesses with an annual turnover of less than R10 million (in 2006). An analysis of the responses received indicates clearly that 71% (figure 6. 17 above) of the respondents view income tax as a constraint to growth.

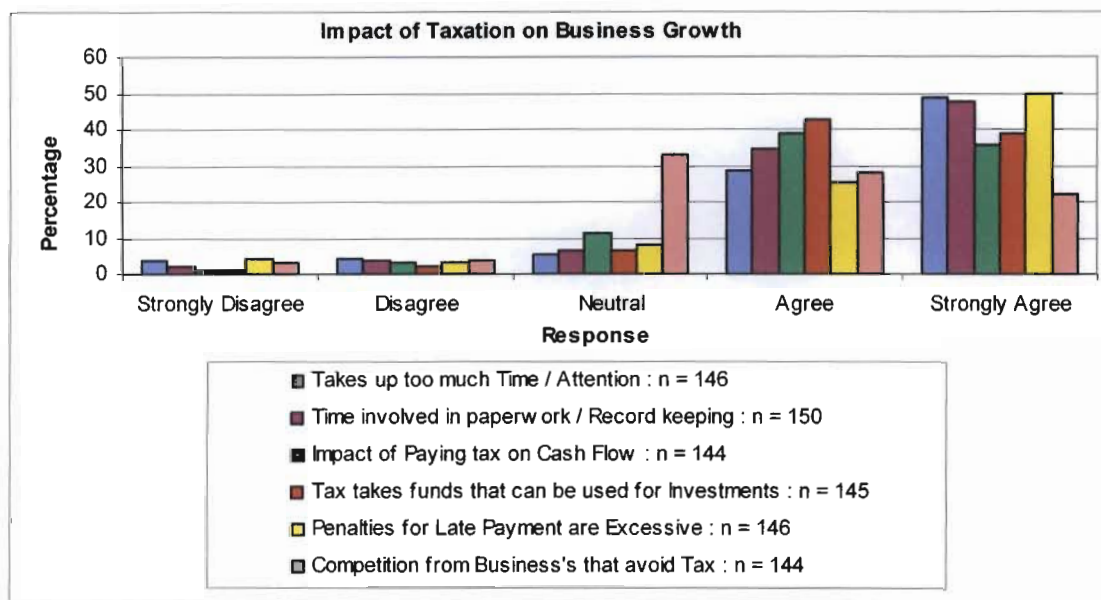
**Skills Development Levy:** The Skills Development Levies Act (9 of 1999) imposes levies for skills development. The aims of this act are *inter alia* to develop workforce skills, improve the quality of work life, improve productivity and improve the delivery of social services (Cronje *et al*, 2000: 470). Employers are liable to pay a skills development levy of 1% of remuneration. To the extent that there is appropriate training for the staff, some of this levy may be reclaimed. About a third of the respondents indicated that the skills development levy is a constraint on the growth of their business (figure: 6.17 above). However, (45%) of respondents remained neutral



### Q16: The Impact of Taxation on the Business

All formal businesses have to register with SARS and comply with the U.I.F., income tax and Vat regulations. These regulations may be time consuming and burdensome for the small business owner / entrepreneur. Furthermore, the Small Business Project's: Counting the cost of Red Tape has shown that the cost of tax compliance is regressive and the small business pays almost 3% of annual turnover (Small Business Project, 2005: 46).

Figure: 6.18: The Impact of taxation on Business Growth



**Takes up to much Managerial Time/Attention:** About 80% of the respondents indicated that taxation has an adverse impact on their business, in that it takes too much of their managerial time to sort out the tax affairs.

**Amount of time involved in keeping records, paperwork:** In addition, the majority of the respondents (over 80%) agree that the amount of time involved in keeping records and the paperwork involved in completing tax returns are excessive. This time can be profitably spent trying to grow the business venture.

**Impact on cash flow of paying tax:** Furthermore, the paying of taxes, at different times of the financial year impacts negatively on the cash flow of the small business. This money can be used

for other purposes. Over 55% of respondents agree that tax impacts on the cash flow of the business.

**Tax takes money out of the business that could be used for Investment:** The money that is used for taxation can be used profitably to grow the business. One such way is short-term investments. Of the surveyed respondents, almost 80% agree that tax takes money out of the business.

**Penalties for Late Payment are Excessive:** Another impact of taxation is the excessive penalties for late payment. Businesses that are late in submitting their tax returns are fined excessively. 75% of the surveyed respondents agree that penalties for late payments are excessive (figure: 6.18).

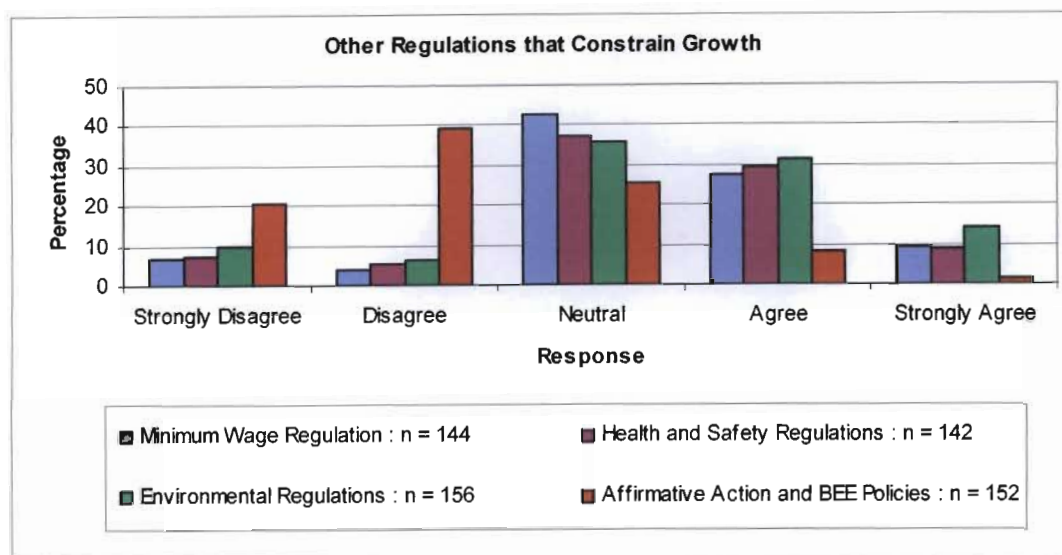
**Competition from businesses that perhaps avoids tax:** Businesses operate in a real world where there is competition among different firms. Competition is healthy as it keeps firms on their 'toes', but some firms may be operating informally and are not paying taxes. These firms then become a source of competition for tax-paying firms. A third of the respondents remained neutral while 50% agreed that competition from firms that do not pay tax affect them.

#### **Q17: Other Regulations that Constrain Growth**

There are various other regulations that affect the growth of the business. The most profound effect of these regulations is the cost of compliance. Some regulations pose a major problem to the small entrepreneur and the use of consultants is often required.

**Minimum Wage Regulation:** The minimum wage regulation ensures that employees of certain sectors are paid a minimum wage. This is to ensure that workers are paid a wage that enables them to live a comfortable lifestyle and that no exploitation of labour occurs. The act also stipulates the number of labour hours workable and conditions for U.I.F. registration. Analysis of the results indicates a neutral response of 42.5% while 37% of respondents agree that the minimum wage regulation hinders the growth of the business (figure: 6.19) below.

Figure: 6.19: Other Regulations that Constrain Growth



**Health and Safety Regulations:** It is the duty of the small business manager to care for their employees and to provide a healthy and safe workplace. The costs associated with such a regulation come from the policies, programmes and procedures that need to be in place to ensure the health and safety of workers. Only 38% of the respondents view the health and safety regulation as a constraint to growth. More than a third of respondents remained neutral.

**Environmental Regulations:** These types of regulations pertain to the extraction of resources and the disposal of waste and by products. These regulations ensure that the surrounding environment is not damaged in the course of conducting business. About a third of the respondents agreed that environmental regulations constrain growth. However, 35% of the respondents remained neutral (figure: 6.19) above.

**Affirmative Action and BEE Policies:** These are policies designed to address the inequalities of the previous government. These policies promote the empowerment of previously disadvantaged individuals. A majority of 60% of respondents disagreed while a mere 9% agreed. Therefore, these policies are perceived as not constraining growth in the Pietermaritzburg area.

**Q18: Crime and its Effects**

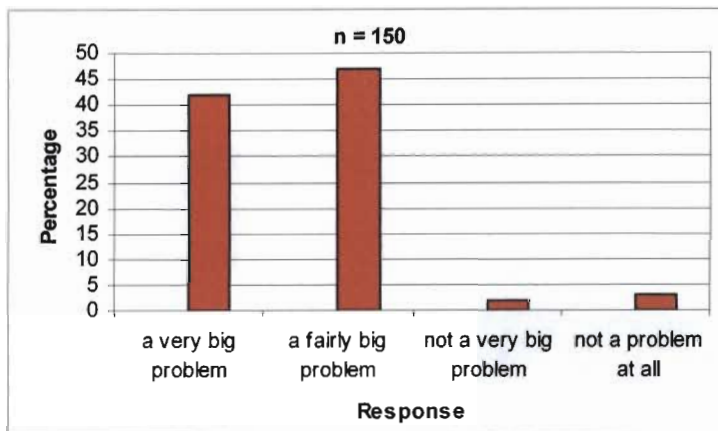
Crime is a social problem experienced in most countries. The effects of crime are a declining economy, unemployment, broken families and stress associated with a life of fear. Business,

being the economic engine of society, is affected both directly and indirectly by crime. Directly regarding the theft of property and money, and indirectly through reduced business confidence, loss of investment, emigration and the steady erosion of the foundations upon which the economy is built (BAC, 2006: 1)

As an introduction to this section, respondents were asked if they perceived crime to be a problem.

### Q18.1 Is Crime a problem?

Figure: 6.20: Is crime a Problem?

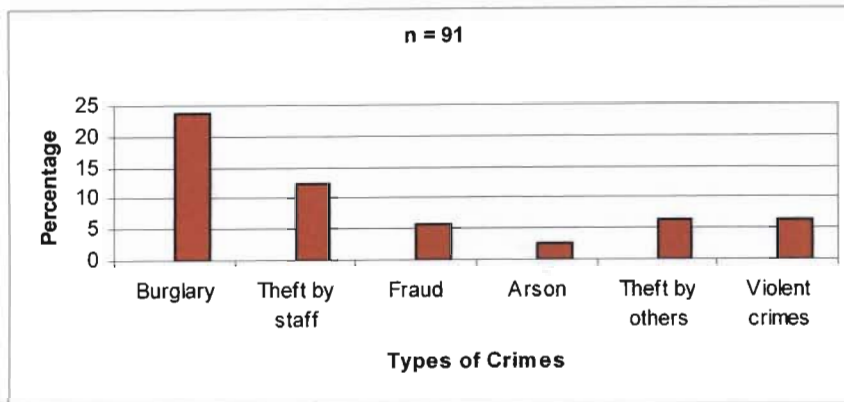


From (figure: 6.20) and it is evident that crime is a fairly big problem. Almost 89% of respondents indicated that crime is a fairly big problem. Only 5% of respondents indicated that crime was not a problem.

### Q21 Types of Crime

A number of crimes affect the small business. These include amongst others, theft by staff, burglary, armed robbery, hijackings, fraud, arson and violent crimes. The small business sector is often the target for criminals as they do not have sufficient funds to invest in sophisticated alarm and security systems as large firms do. Respondents were asked to indicate the types of crimes that they experienced. An analysis of the results reveals (figure: 6.21 below) that burglaries were most common followed by theft from staff. Arson was the least experienced type of crime

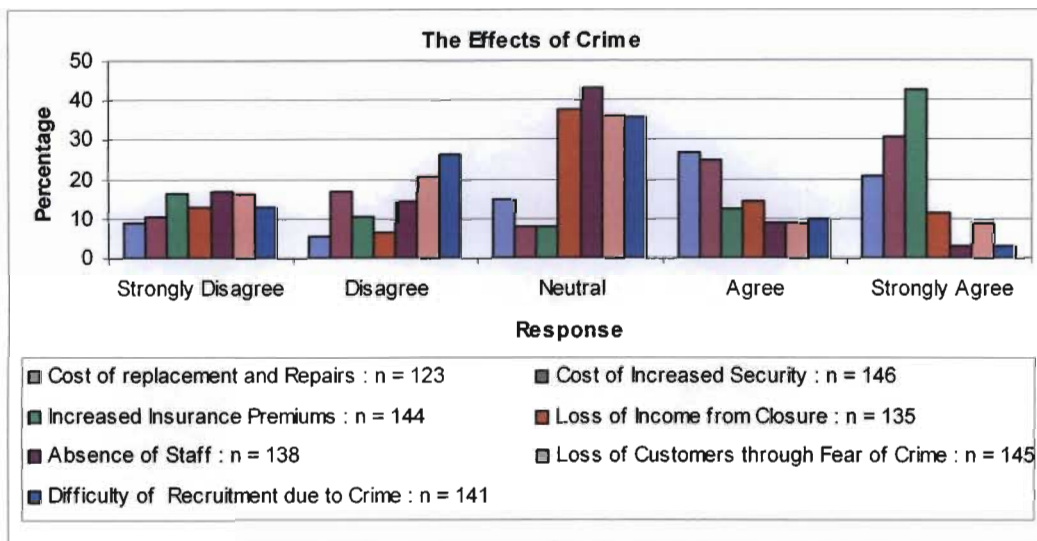
Figure: 6.21: Types of Crime



### Q22 The Effect of Crime on the Business

The surveyed literature (Investment Climate Survey, 2004: 96), has shown that losses due to crime, across all sectors amounted to 2.272 million of Rands. Therefore, crime is a constraint to business growth in a number of different ways.

Figure: 6.22: Effects of Crime on Business Growth



**Costs of replacements and repairs:** Replacement of stolen stock and equipment vital for the operation of the business, places an added financial burden on the small business. Repairs and replacements to damaged windows, doors and locks needs to be attended to promptly. Of the

surveyed respondents, 47.5% (figure 6.22) agreed that crime impacts on the growth of the business due to the costs incurred in replacements and repairs.

**Cost of Increased security:** Installing alarm systems and employing security guards as a preventative measure are some of the solutions undertaken by small firms to combat crime. These measures are costly and apart from retarding growth also affect the cash flow of the business. More than 50% of the respondents agreed that the cost of increased security was a hindrance to the growth of the business.

**Increased Insurance Premium:** Insuring the business against theft, burglaries, fire is another way of combating the cost of crime. The material losses suffered due to crimes can be claimed partially or wholly from the insurance company. Due to the number of fraudulent claims, received by insurance companies, claims are only paid after thorough investigations are conducted, thus affecting cash flow. Insurance premiums are determined by the location (risk profile) and by the number of claims made. A majority of 55% of surveyed respondents agree that the cost of increased insurance premiums constrain growth.

**Loss of Income from Closure:** It may occur that the business stay closed for long periods of time due to criminal acts of arson and vandalism. In such a situation the business will have to stay closed until renovations are done. Prolonged closure results in a loss of income. From (figure: 6.22 above), 38% remained neutral while 25% agreed that loss of income from closure inhibits growth.

**Absence of staff:** Violent crimes and armed robberies traumatise workers to such an extent that long periods of rest and counselling are needed to remedy the situation. This results in staff absenteeism and additional staff needs to be hired on a temporary basis. Such a situation affects productivity as well as cash flow. The modal response to the question was neutral (43%) while 31% disagreed. Only 11% of respondents agreed. Therefore, absence of staff due to crime does not affect the business adversely.

**Loss of customers through fear of crime:** Businesses that are located in areas that are constantly targeted by criminals will suffer not only declining sales but loss of customers as well.

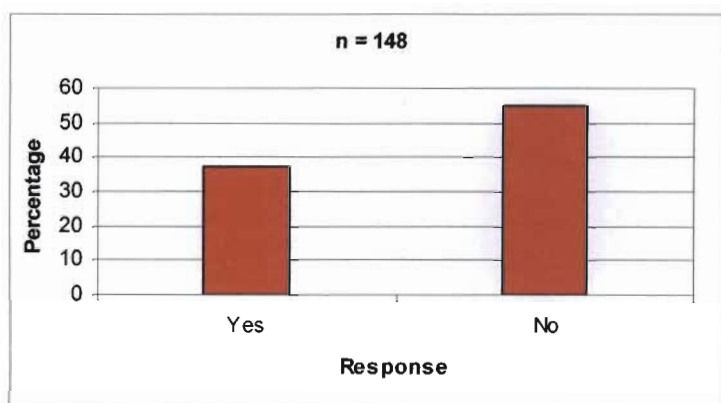
Customers will avoid such firms for fear of being mugged and robbed. Over a third of respondents remained neutral, 36% disagree and 17% agreed that loss of customers through fear of crime constrain growth (figure: 6.22) above.

**Difficulty in Recruitment:** If the business location is conducive to crime, the recruitment of workers becomes difficult. This can be attributed to workers fear of being mugged and robbed. Of the respondents surveyed 13% agreed while 35% remained neutral. Almost 40% of respondents disagreed (figure: 6.22).

### Q23 Staff Training

Staff training and development is important to both the individual and the business. The individuals benefit by improved skills, knowledge and attitudes while the business benefits from increased productivity, controlled costs and a positive climate for growth and communication is created.

Table: 6.23: Response to Training Provided for Staff

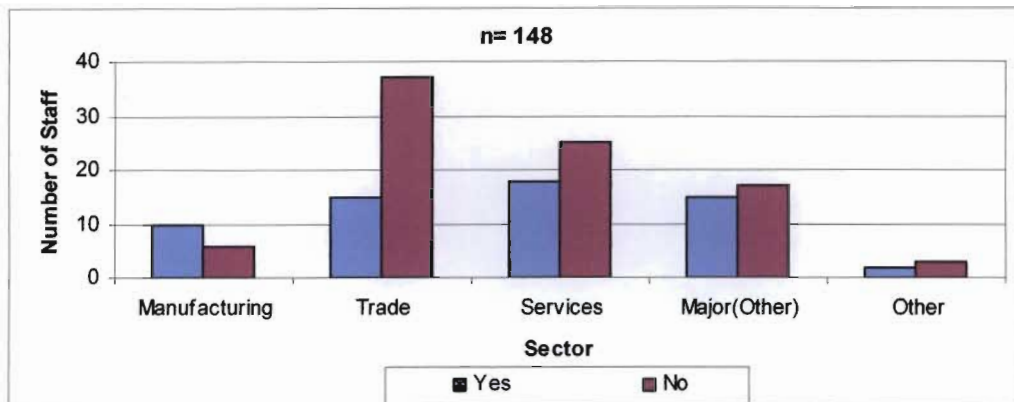


Of the surveyed respondents, 55% provide no training for their staff, while 37.5% of respondents do.

#### Q23.1 Training per sector

Figure 6.24 below, presents a distribution of staff training by the various sectors. The services sector seems to be the sector where most training has occurred.

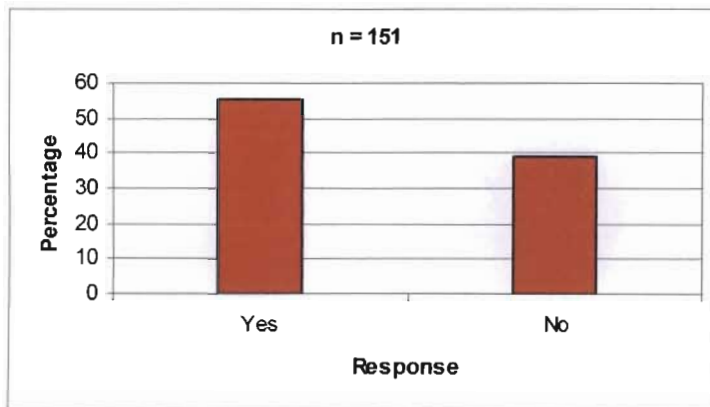
Figure: 6.24: Staff Training per Sector



### Q25 Use of technology such as computers

The use of technology, such as computers, can greatly enhance the operation and competitive advantage of the small business. With the latest computer technology, the entire business operation can be controlled and monitored. Of the surveyed respondents, a mere 55.6% make use of computers and 38.8% do not.

Figure: 6.25: Use of technology such as Computers



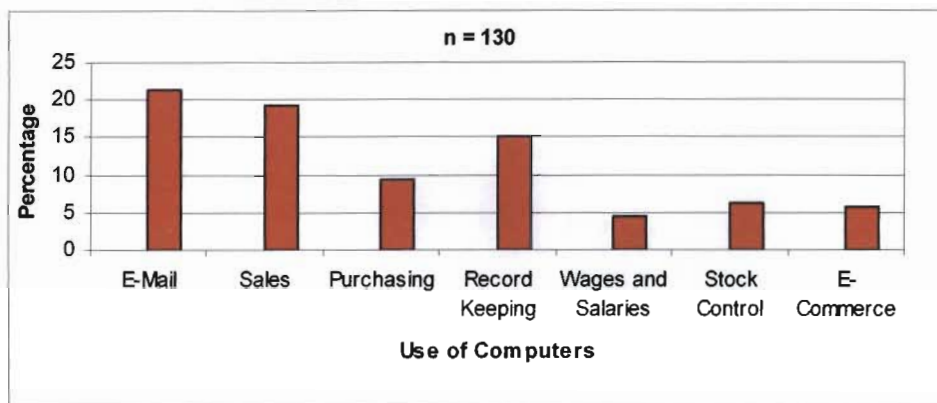
### Q26 Use of Computers

Computer based functions are not limited to routine record-keeping activities, but include a wide range of diverse applications. Tasks such as desktop publishing, communicating electronically



with vendors and customers, and electronic banking are but a few of the applications that the small business utilizes to contain costs and improve services (Longernecker *et al*, 1994: 593).

Figure: 6.26: Use of Computers

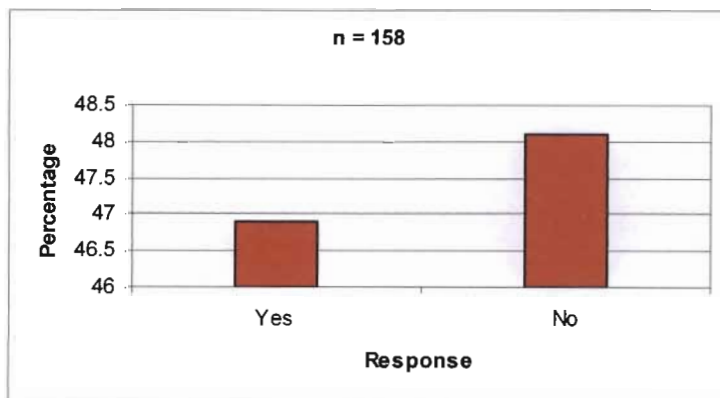


From (figure: 6.26), we see that E-mail, sales, wages and salaries are the most common uses of the computers. Therefore, the respondents are not leveraging technology to enhance the business and this is an area for concern.

**Q27 Do you think Technology is helping you to grow your business?**

Technology, although costly, can be used efficiently to create a competitive advantage for the small business by cutting costs, facilitating communication between employees and other businesses and as a decision-making support tool.

Figure: 6.27: Technology helping to grow the Business

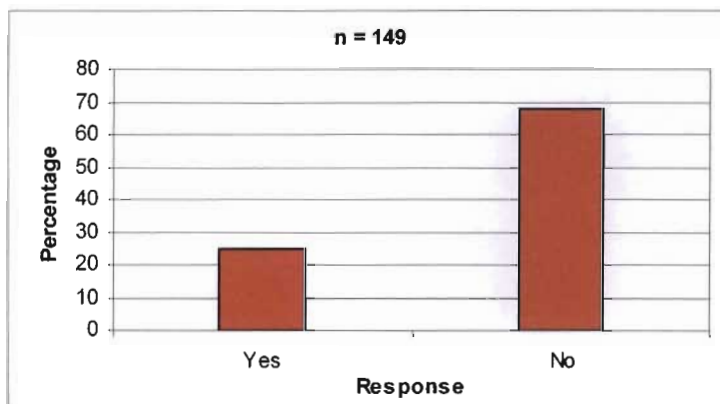


From the results obtained (figure 6.27 above), it was found that only 46.9% of the surveyed respondents felt that technology was helping them grow their business. This implies that 53% of the respondents are either under-utilising the use of their computers or do not use computers at all. Globalisation has changed the way business is conducted and the use of computers is an indispensable tool in the modern business world.

**Q28 Innovation and doing something unique that others cannot replicate.**

Firms that are innovative and do things differently from other firms have a distinct competitive advantage. This advantage enables them to capture a larger share of the market, and hence realise greater profits. This then leads to growth and development of the business. A 68% majority, of the respondents indicated that they were not innovative (figure 6.28).

Figure: 6.28: Response to being Innovative

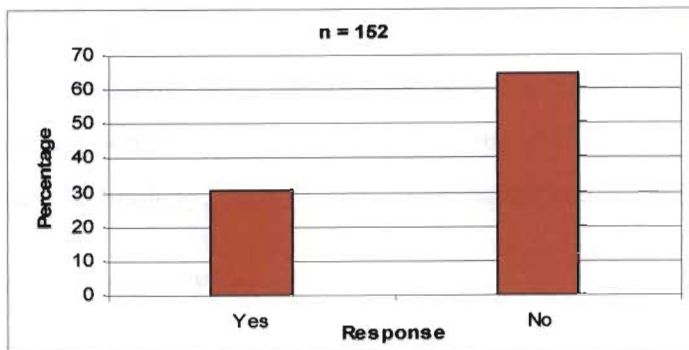


**Q30 Is there sufficient business support available in your local area?**

The importance and contributions made by the SME sector to employment and GDP cannot be over emphasised and the government therefore has a major role to play in supporting and growing such a sector.

From figure 6.29 below, an overwhelming majority of 64.4% of the surveyed respondents felt that there is not enough business support for small business ventures in Pietermaritzburg. This can have a negative effect on the growth of the business.

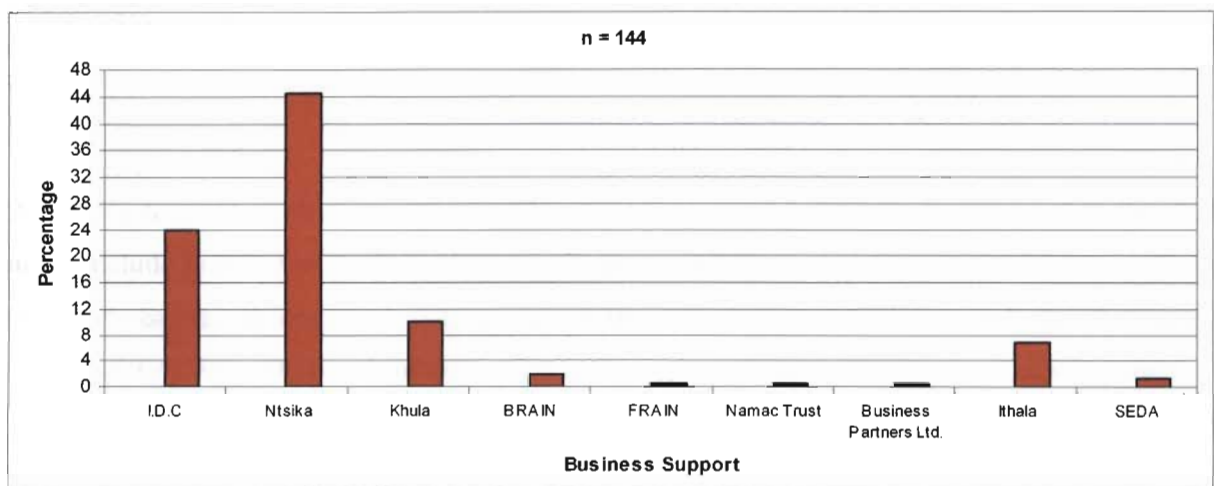
Figure: 6.29: Sufficient Business Support



**Q31 Have you heard of any of the following organisations that provide business support?**

To promote and help the SME sector there are currently many agencies available to service the small business sector. From (figure: 6.30), it is evident that such agencies are not well known as most of the surveyed businesses have heard of the Investment Development Corporation (23.8%) and Ntsika (44.4%).

Figure: 6.30: Percentage of Business Support Identification



**6.3 Hypotheses Testing**

The hypothesis test that was carried out was the Chi-Square test. The reason for using this test was to test for independence of association. The researcher carried out these tests to determine whether the internal factors ( obtaining finance, cash flow, recruitment and retaining staff,

transport issues, shortage of managerial skills / business expertise and lack of financial understanding) and external factors (economy, taxation, VAT, income tax, U.I.F, Skills Development Levy, Regulation and Laws, Minimum Wage Regulation, health and Safety Regulation, Environmental Regulations, Affirmative Action and BEE Policy, keeping up with new technology, competition in the market and crime) prevent growth of the business.

### 6.3.1 Internal Factors

**H<sub>0</sub>:** Internal factors do not prevent growth.

**H<sub>1</sub>:** Internal factors prevent growth.

Table: 6.5: Chi-Square test statistics for Internal Factors

Factor	$\chi^2$	d.f	p
Obtaining Finance	1162.575	4	.000
Cash Flow	1308.646	4	.000
Recruitment of Staff	1422.726	4	.000
Retaining Staff	1323.780	4	.000
Transport Issues	1519.101	4	.000
Shortage of managerial skills/Business Expertise	1270.857	4	.004
Lack of financial understanding	1307.379	4	.000

At the 5% level of significance we reject H<sub>0</sub> since the p-values of all the factors are less than 0.05 and conclude that factors such as obtaining finance, cash flow, recruiting and retaining staff, and transport issues, shortage of managerial skills / business expertise and lack of financial understanding prevent growth of the business. The relevant chi-square test statistics in support of this association between the above internal factors and business growth are summarised in (table: 6.5) above.

### 6.3 2 External Factors

**H<sub>0</sub>:** External factors do not prevent growth.

**H<sub>1</sub>:** External factors prevent growth.

Table: 6.6: Chi-Square test statistics for External factors

Factor	$\chi^2$	d.f	p
The Economy	1602.099	4	.000
Taxation	1337.441	4	.000
VAT	1363.411	4	.000
Income Tax	1989.798	4	.000
U.I.F	1218.051	4	.000
Skills Development Levy	1337.461	4	.000
Regulation and Laws	1604.206	4	.000
Minimum Wage Regulation	1366.142	4	.000
Health and Safety Regulation	1214.707	4	.000
Environmental Regulations	1136.761	4	.000
Affirmative Action and BEE policy	313.284	4	.000
Keeping up with new Technology	1046.327	4	.000
Competition in the Market	1110.744	4	.000
Crime	1060.134	4	.000

At the 5% level of significance, we reject  $H_0$  since the p-values of all the factors are less than 0.05 and conclude that these factors significantly prevent growth. The relevant chi-square test statistics in support of this association between the above external factors and business growth are summarised in (table: 6.6) above.

#### 6.4 Regression Analysis

The determinant of growth was done using multiple regression analysis. Different models were initially fitted to check the variation and influence of the independent variables, which are different groupings of questions measuring a certain trait against the dependent variable, AVERAGE GROWTH in employees. The model that is selected rests on 11 independent factors: Ethnic Grouping (q3), level of education of the entrepreneur (q4), activity of business (q5), legal status (q6), start-up capital (q7), entrepreneur's exposure to training (q8), access to finance (q13), staff training and development (q23), use of technology (q25), technology growing the business

(q27) and business support (30). The models were fitted in different orders with different results, but the optimal model that explains the most variation is given below:

**Average Growth** =  $\beta_0 + \beta_1 q4 + \beta_2 q6 + \beta_3 q7 + \beta_4 q8 + \beta_7 q30 + \varepsilon$ : where  $\beta_0$  = constant term and  $\varepsilon$  = error term. The R-square value for this parsimonious model is 45%, meaning that the independent variables are accounting for 45% of the variation with respect to the dependent variable.

Table: 6.7: Test Statistics for Regression Model

Factor	$\beta$	t	p
Level of Education	1.027	3.05	.016
Legal Status	3.131	10.1	.007
Start-Up Capital	8.493	4.40	.002
Exposure to Training	7.219	14.61	.003
Business Support	9.088	2.72	.008

The above table reflects that at the 5% significance level, the level of education, legal status of the business, source of start-up capital, exposure to training and business support are significant and positively related to average growth.

Diagnostic tests were carried out on the above model to check the validity of the model. This was done by examining the residuals. Firstly, a histogram of the residuals was looked at, to check the normality assumption of the residuals. The plot (figure 6.31 below), is a good plot indicating a normal curve about the histogram of residuals.

Secondly, the Normal P-P plot was looked at. These residuals also appear to be normally distributed (figure 6.32 below) and the assumptions of normality in this regression model are therefore not violated. This implies that the regression model is valid.

Figure: 6.31: Histogram of Residuals

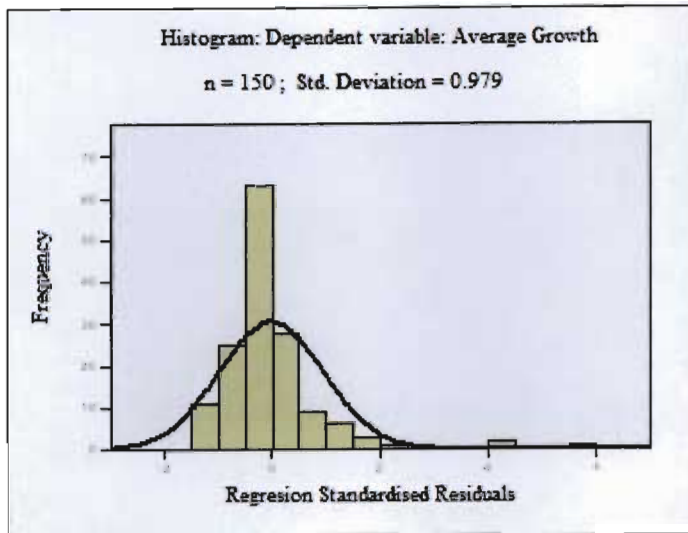
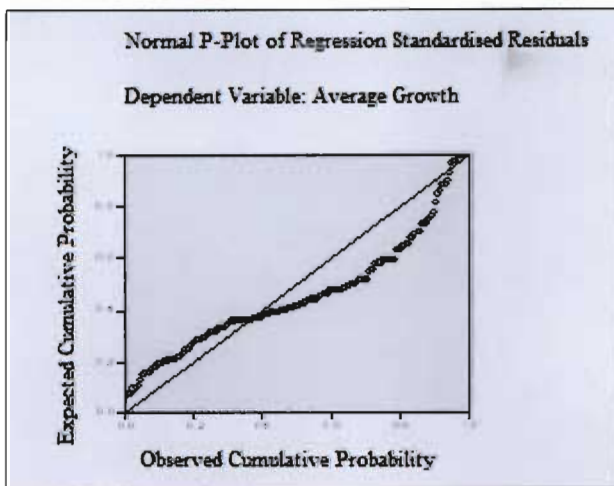


Figure: 6.32: Normal P Plot of Regression Standardised Residuals



## 6.5 ANOVA Tests

ANOVA tests were conducted to determine whether growth varies with Gender, Ethnicity, Activity, Legal Status, Educational level and Exposure to Training and within the different sectors surveyed in Pietermaritzburg. The independent sample t-test was used for the following hypotheses:

**6.5.1.  $H_0$ :** There is no difference in the average growth between males and females.

**$H_1$ :** There is a difference in the average growth between males and females.

Table: 6.8: Test Statistics of Av. Growth Vs Gender

		t-test for Equality of Means						
		t	df	Sig. (2-tailed)	Mean Difference	Std. Error Difference	95% Confidence Interval of the Difference	
							Lower	Upper
Average Growth	Equal variances assumed	1.946	155	.043	10.2648	5.27466	-.15472	20.68428
	Equal variances not assumed	2.388	100.492	.019	10.2648	4.29842	1.73735	18.79221

At the 5% significance level, we will reject  $H_0$  since the p-values are less than 0.05 and conclude that there is a difference in the average growth between males (16.77) and females (6.09). These results demonstrate that the average, job creation potential of males is almost three times that of females.

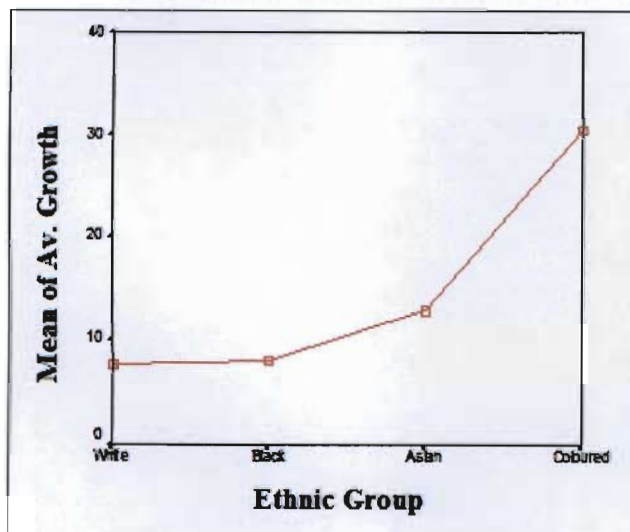
**6.5.2  $H_0$ :** There is no difference in the average growth between ethnic groups.

**$H_1$ :** There is a difference in the average growth between ethnic groups.

Table: 6.9: Test Statistic of Av. Growth Vs Ethnic Groups

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	6312.052	3	2104.017	2.032	.112
Within Groups	159492.731	154	1035.667		
Total	165804.783	157			

Figure: 6.33: Means Plot of Av. Growth Vs Ethnic Groups





At the 5% significance level, we will accept  $H_0$  since the p-values are greater than 0.05 and conclude that statistically there seems to be no difference in the average growth between ethnic groups sampled. However, within ethnic groups there appears to be a difference. The means plot is presented in figure (6.33) above.

**6.5.3.  $H_0$ :** There is no difference in the average growth between activities of business.

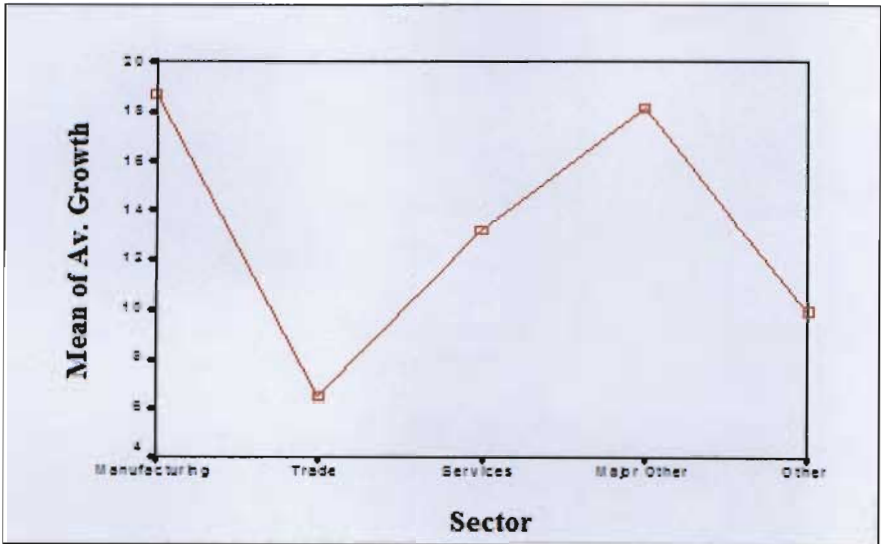
**$H_1$ :** There is a difference in the average growth between activities of business.

Table: 6.10: Test Statistic for Av. Growth Vs Activities of Business

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	13730.242	4	3432.56	3.222	.008
Within Groups	161925.138	152	1065.297		
Total	175655.38	156			

At the 5% significance level, we will reject  $H_0$  since the p-values are less than 0.05 and conclude that there is a difference in the average growth between activities of business. The manufacturing (18.5) and the major (other) sector (18) appear to experience, on average, more growth than the other sectors. The means plot is as follows:

Figure: 6.34: Means plot of Av. Growth Vs Activities of Business



**6.5.4 H<sub>0</sub>:** There is no difference in the average growth between legal statuses of business.

**H<sub>1</sub>:** There is a difference in the average growth between legal statuses of business.

Table: 6.11: Test Statistic for Av. Growth Vs Legal Status

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	11803.236	4	2950.809	2.736	.005
Within Groups	163888.806	152	1078.216		
Total	175692.042	156			

At the 5% significance level, we will reject H<sub>0</sub> since the p-values are less than 0.05 and conclude that there is a difference in the average growth between legal status groups. It appears that sole proprietorships and partnerships are, on average, registering more growth in labour/employment than other businesses with different legal status. The means plot is as follows:

Figure: 6.35: Means plot of Av. Growth Vs Legal Status



**6.5.5. H<sub>0</sub>:** There is no difference in the average growth between education level groups.

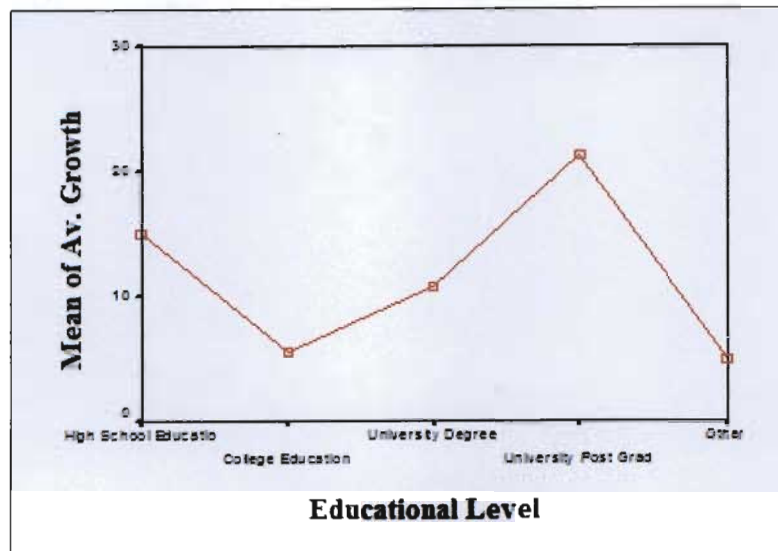
**H<sub>1</sub>:** There is a difference in the average growth between education level groups.

Table: 6.12: Test Statistics for Av. Growth Vs Educational Level

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	13114.614	4	3278.654	3.045	.007
Within Groups	162559.830	151	1076.555		
Total	175674.444	155			

At the 5% significance level, we will reject  $H_0$  since the p-values are less than 0.05 and conclude that there is a difference in the average growth between education level groups. Those entrepreneurs that possess university postgraduate degrees (21.22) appear to, on average, employ more people than those with high school education (15.52). The means plot is provided below:

Figure: 6.36: Means plot of Av. Growth Vs Educational Level



**6.5 6.  $H_0$ :** Sources of start-up capital do not account for a difference in average labour growth.

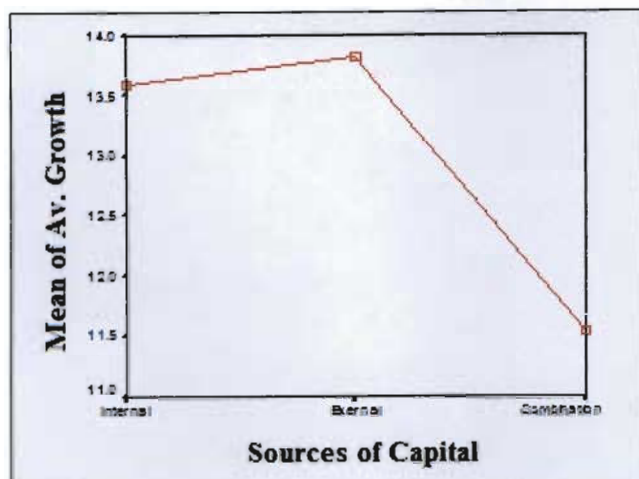
**$H_1$ :** Sources of start-up capital do account for a difference in average labour growth.

Table: 6.13: Test Statistic for Av. Growth Vs Sources of Start-Up Capital

	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	22161.087	2	11080.544	10.127	.029
Within Groups	165214.719	151	1094.137		
Total	187375.806	153			

At the 5% significance level we will reject  $H_0$  and conclude that there is a difference in the average growth between sources of start-up capital group. Business persons who have used external funding (13.8) tend, on average, to register more growth than those using internal sources of finance (13.6). The means plot is provided below.

Figure: 6.37: Means plot of Av. Growth Vs Source of Capital



6.5.7.  $H_0$ : there is no difference in the average growth between those who have been exposed to training and to those who have not been exposed to training.

$H_1$ : there is a difference in the average growth between those who have been exposed to training and to those who have not been exposed to training.

Table: 6.14: Test Statistics for Av. Growth Vs Exposure to Training

		t-test for Equality of Means						
		t	df	Sig. (2-tailed)	Mean Difference	Std. Error Difference	95% Confidence Interval of the Difference	
							Lower	Upper
Average Growth	Equal variances assumed	9.235	155	.014	-1.2292	5.22619	-11.55296	9.09453
	Equal variances not assumed	9.230	122.207	.019	-1.2292	5.35214	-11.82413	9.36570

At the 5% significance level, we will reject  $H_0$  since the p-values are less than 0.05 and conclude that there is a difference in the average growth between those who have been exposed to training (15.96) and to those who have not been exposed to training (13.35).

From the above results it can be concluded that in the Pietermaritzburg region there is a significant difference in, average growth between males and females, between legal statuses of

businesses, between activities of business and between sources of start-up capital with respect to the number of people employed. It also highlights the fact that higher educational levels and exposure to training affect the average growth potential of businesses positively.

## 6.6 Factor Analysis

Factor analyses was carried out in this study as an exploratory tool in order to reduce the initial set of internal and external factors to a smaller set that adequately explains the growth constraints and could account for being a set of sub constructs. The Principal Components method was used with varimax rotation.

Table: 6.15: Total Variance Explained

Component	Initial Eigenvalues			Extraction Sums of Squared Loadings			Rotation Sums of Squared Loadings		
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	4.701	36.159	36.159	4.701	36.159	36.159	3.170	24.382	24.382
2	1.663	12.794	48.953	1.663	12.794	48.953	2.681	20.623	45.005
3	1.333	10.257	59.210	1.333	10.257	59.210	1.847	14.205	59.210
4	.996	7.659	66.869						
5	.911	7.005	73.874						
6	.724	5.565	79.439						
7	.605	4.657	84.096						
8	.514	3.953	88.049						
9	.480	3.692	91.741						
10	.393	3.022	94.763						
11	.301	2.316	97.079						
12	.215	1.654	98.733						
13	.165	1.267	100.000						

Extraction Method: Principal Component Analysis

From the above table, the cumulative variance shows that 3 clusters are jointly explaining 59.210 % of the total variance in growth. Furthermore, all of these 3 clusters have eigenvalues over 1. The first cluster accounts for 36.159% of the variation. This is normally the case in factor analysis. The variables were derived from question 14 of the questionnaire, where the respondents were asked to rate the variables as constraints to growth. These included the economy, obtaining finance, cash flow, taxation, recruiting staff, retaining staff, transport issues, regulations and laws, keeping up with technology, competition in the market, shortage of

managerial skills, lack of financial understanding and crime. Table (6.16) presented below shows the formation of clusters.

Table: 6.16: Rotated Component Matrix

Variables	Cluster		
	1	2	3
Retaining staff	.816	.142	.135
Recruiting staff	.810	.011	.047
Shortage of managerial skills	.653	.510	-.206
Keeping up with new technology	.626	.209	.169
Transport issues	.605	.423	.143
Cash flow	.169	.800	-.160
Obtaining finance	.296	.780	.075
Crime	-.005	.658	.257
Lack of financial understanding	.354	.574	.144
The economy	-.010	-.042	.813
Taxation	.322	.022	.602
Regulations and laws	.561	.158	.597
Competition in the market	-.037	.374	.486

We now look at the rotated loadings table to find out which questions are not loading at all on the factors and could hence be eliminated from the data set and then re-run the factor analysis. All of the questions or variables (13), ranging from retaining staff to competition in the market, are loaded so we can now look at the classification of the different sets of clusters.

The first set of factors in cluster is labelled as “management” factors and it consists of 5 items which had loadings ranging from 0.605 to 0.816. These factors are: Retaining Staff, Recruiting Staff, Shortage of Managerial Skills, Keeping up with new Technology and Transport Issues. These factors being internal to the business are labelled as Management and accounts for 36.159% of the variance. Cronbach’s alpha calculated for factor 1 yielded a value of 0.7278. This is a good value and concludes that the result is reliable. A summary of this first group of factors is presented in table (6.17).

Table: 6.17: Factor 1: **MANAGEMENT**

QUESTION	INTEPRETATION	
q14ret	Retaining staff	Internal
q14rec	Recruiting staff	Internal
q14sho	Shortage of managerial skills	Internal
q14k	Keeping up with new technology	External
q14tr	Transport issues	Internal

The second cluster presented in (table: 6.18) and is labeled “Finance” consists of 4 factors, with loadings ranging from 0.574 to 0.800. Factor 2 consisted of Cash Flow, Obtaining Finance, Crime and Lack of Financial Understanding. These factors also are internal factors with the exception of crime. Crime no doubt is an external factor, however the negative impacts of crime such as increased costs of security, replacement and repair costs impact internally on the finances of the business. Using the above explanation factor 2 is classified as Finance and accounts for 12.794% of the total variance. Cronbach’s alpha calculated for factor 2 equaled 0.8251 and this certifies the reliability of the second factor. The table below shows factor 2.

Table: 6.18: Factor 2: **FINANCE**

QUESTION	INTEPRETATION	
q14c	Cash flow	Internal
q14o	Obtaining finance	Internal
q14crime	Crime	External
q14lack	Lack of financial understanding	Internal

The third cluster, consisting of 4 factors, and is labeled “External Factors”, has loadings ranging from 0.486 to 0.813. This consisted of the Economy, Taxation, Regulation and Laws and Competition in the Market. Being external in nature, the third factor is therefore classified as External and accounts for 10.257% of variation. Factor three is reliable as it has a Cronbach’s alpha of 0.8841. A summary of the third factor is presented in table (6.19) below.

Table: 6.19: Factor 3: **EXTERNAL**

QUESTION	INTEPRETATION	
q14t	The economy	External
q14ta	Taxation	External
q14ral	Regulations and laws	External
q14com	Competition in the market	External

From the above analysis, it is evident that the internal constraints (Factor1) accounts for 36.159% variance in growth. Factor 2 accounts for 12.7945 of variance in growth and factor 3 accounts for 10.257% of the total variance in growth. Collectively these three factors account for 59.210% of the variance in growth. It is therefore concluded that internal constraints impact more on average growth of labour than external factors and that the focus of policy on small business/entrepreneurship growth should be more on the internal conditions than the external conditions.

### 6.7 Reliability Analysis

Cronbach's alpha was also calculated as part of the reliability test to assess how valid the results were and whether we can get similar results to generalize if we increased the sample size. A value of 0.7 or higher is a very good value that can lead us to say that we will get nearly the same results if we carried out this survey with a larger sample of respondents. The Cronbach's alpha was calculated for questions 11, 12, 13, 14, 15, 16, 17 and 22 as they have the same scales.

The results are as follows:

#### Reliability Coefficients

N of Cases = 15.0

N of Items = 41

Alpha = 0.8687

The alpha value obtained is 0.8687 and as this value is greater than 0.7 we can conclude that the questionnaire and results that had been established were reliable and that the results have given true and realistic findings.

### 6.8 Conclusion

This chapter has presented the results of the data analyses in a logical sequence, starting with the descriptive statistics and then presenting the results of the various tests carried out according to the set objectives. The following chapter presents an in depth analysis of these results.



## CHAPTER SEVEN

### DISCUSSION OF RESULTS

#### 7.1 Descriptive

Relevant data was gathered from a sample of 160 (64% response rate) small business entrepreneurs in the (central) Pietermaritzburg region, with the aid of questionnaires. The sample consisted of 96 (60%) male and 64 (40%) female small business owners. The analysis of these questionnaires reveals the following:

The sample was representative as it consisted of all ethnic groups. The modal race group were the Indians (Asians) 46.9%, followed by the whites and blacks with 21.9% each. The representation of coloured business owners was 9.4%. The average age of the businesses sampled was 9.22 years and the modal age of businesses was 5 years.

The educational level of the surveyed owners ranged from high school to university postgraduate qualifications. High school education accounted for 38.1 %, College education for 18.8 %, University degrees for 30.6 % and Post Graduate degrees for 10% of the sample.

The preferred legal status of the businesses is the sole proprietorship (39.4%), followed by the close corporation with 33.8%. This result is similar to the findings of a study done in Pietermaritzburg in 2003. In this study, 61% of business owners sampled were also sole proprietors (Pather, 2003: 47). The possible reasons for such a status are that the owner/manager owns the entire business and all profits belong to him/her. Another advantage of proprietorship is the lack of restrictions in how the business is run, and the personal satisfaction that is derived. The disadvantages of such a legal status are the unlimited liability, the limited size and life of the business.

A majority of respondents (60%) indicated that personal funds were used to start the business. This is probably due to the high cost of capital. It is well documented that access to finance is a constraint not only in starting a venture but in growing the venture also.

The questionnaire provided nine different business sectors to the respondents. For the purposes of analysis the number of sectors was scaled down to five. The other (major) category represents a combination of transport, construction, travel and tourism, agriculture and financial sectors. Therefore the sectors analysed were manufacturing, trade, services, other (major) and the 'other' category represents franchised firms.

Over half, (51.9%) of the sampled respondents underwent training while 47.5% did not. The types of training listed included specific degrees such B.Com.; Mechanical Engineering degrees; M.B.A. degrees; F.E.T. college diplomas in plumbing, electrical trade, building and construction, beauty and hairdressing and short courses in management such as project management, financial management and strategic management. Therefore, the majority of business owners sampled in Pietermaritzburg have undergone some form of training.

## 7.2 GROWTH OF THE BUSINESS

The following formula was used to calculate the average growth in the number of employees.

$$\text{averageGrowth} = \frac{L_1 - L_0}{L_0 \times n}, \text{ where: } L_1 = \text{Number of Employees as at 2005.}$$

$L_0$  = Number of Employees at Inception.

$n$  = Number of Years the Business is in Operation.

Growth of the business was examined in terms of average employment growth (over time), as it was anticipated that many respondents would not want to divulge their true earnings. Average growth was also examined between the different sectors of the sample, between gender, ethnic groups, sources of start-up capital as well with the educational level and training of the owners.

The average growth recorded for surveyed businesses in Pietermaritzburg, in terms of the number of employees was 12.5010. The median value was 4.8. This implies that on average a business grows by 12.5010 employees per year. This indicates that the businesses sampled are growing and labour employment in small businesses is experiencing growth in PMB. The reasons for such a result could be numerous, and could stem from personal traits of owners, the internal environment and the external environment.

Evident from the results is the fact that the number of employees per sector has been increasing over the life span of the business. The largest increase of 20.0493 employees was recorded by the manufacturing sector followed by 18.2202 employees of the major (other) category. This included the combination of transport, construction, travel and tourism, agriculture and financial sectors. The services sector recorded an average growth of 13.2101 employees and the 'other' category representing the franchised firms recorded a growth of 9.9333 employees. The lowest average growth rate of 6.7988 employees was recorded by the trade sector. These results strengthen the conclusion that small firms are important job creators in PMB.

Examining labour growth in relation to the entrepreneur's educational level, clearly illustrates the fact that the higher the level of education the higher the growth of the business. Those in possession of a university postgraduate degree recorded an average mean growth of 21.2214 employees as opposed to those that possessed a high school education who recorded an average growth of 15.5240 employees per year. It is a well-documented fact that educational level and business growth are positively correlated (Barringer *et al*, 2005: 667; Storey, 1994: 129; Von Broembsen *et al*, 2005:28). Entrepreneurs with tertiary education employ, on average, three times as many people as entrepreneurs who have not completed secondary education (Von Broembsen *et al*, 2005: 28).

Average growth versus training, clearly illustrates that business growth is increased by training. Such training can take the form of prior work experience or specific commerce and management qualifications undertaken prior to business start up. The results found in this study show that those respondents that underwent some form of training have an average growth of 15.9634 employees as opposed to the average growth of 13.2594 employees for those respondents that had no training.

### **7.3 CONSTRAINTS**

The constraints or problems affecting business growth were broken down into internal and external categories. The internal constraints deal with the management processes (financial management, access to finance, innovation and technology, human resource practices, training

and development of staff, and lack of managerial skills) involved in running the business. The external constraints deal with the economy, taxation, regulation and laws, business support and crime. The internal constraints will be discussed first.

### **7.3.1 INTERNAL CONSTRAINTS**

#### **7.3.1.1 Finance**

Lack of access to finance and the skills to manage finance is a crucial field within the internal environment of the enterprise that yields potential obstacles to business success. The results of this study reveal that 35.6% of the respondents felt that obtaining finance to fund their growth plans was a problem. This is probably due to the high cost of external finance or the bank's reluctance to fund small businesses that have not yet proved themselves with a satisfactory record of accomplishment. Smorfitt (2002: 12) asserts that a major problem in stimulating SMME growth is constrained access to finance. Small and medium businesses often do not meet the criteria financiers have traditionally used in evaluating loan applications. Government subsidies are available for the small business sector, but the difficulty in accessing this finance is slowing small business growth.

The results also show that the majority of respondents did not find cash flow to be a problem and only 21% of respondents indicated that lack of financial understanding was a constraint to their business. Most of the respondents (45%) remained neutral and it is possible that they were reluctant to disclose their lack of financial understanding to the researcher. Inadequate financial understanding leads to deficiencies in several other areas of financial management. Potgieter and Frank (1990: 3) mention that management incompetence is directly linked inadequate information for decision making. It is therefore imperative that owners / managers equip themselves with the necessary financial skills to analyse and monitor financial activities.

#### **7.3.1.2 Staff Development and Training**

Only 37.5% of respondents indicated that they have provided staff training and development within the last twelve months. From the different sectors analysed, the services sector was most involved in training their employees. The importance of training to the small business sector cannot be over emphasised. Human resource development (HRD) can be defined as a set of

systematic and planned activities designed by the business to provide workers with the opportunities to learn necessary skills to meet current and future job demands (Desimone *et al*, 2002: 3). HRD efforts begin when the employee joins the business and continues throughout the employee's career.

Training improves skills and knowledge and in view of the constant change in products, technology, policies and procedures in the world of business, it becomes a necessity for the growth of the business. Well-educated, trained and skilled staff is a source of competitive advantage for any business venture as costs are reduced, productivity increases and a climate or culture conducive to growth is created.

#### **7.3.1.3 Managerial Skills**

Of the respondents surveyed, only 31.9% indicated that their shortage of managerial skills was a constraint to their growth plans. Those that remained neutral represented 42% of the sample. Here again it is assumed that the respondents were reluctant to disclose their lack of managerial skills to the researcher. Managerial skill is paramount to growth. Transport issues were not seen as a major problem as only 24% viewed it as a problem. With regard to management of the human resources, in particular the recruiting and retaining of staff were both seen to be a major constraint to business owners in Pietermaritzburg.

#### **7.3.1.4 Recruiting and Retaining Staff**

A total of 57% of the respondents felt that recruiting the 'right' staff was a problem and 58% felt that retaining staff was a problem. Such a result is not surprising if one considers the factors affecting recruitment. These factors are internal and external in nature. External factors affecting recruitment are legislation (Labour Relations, Employment Equity and Minimum Wage Regulation) and labour market conditions. When there is a shortage of people as there is in South Africa for skilled jobs, the recruitment process is usually more difficult, time consuming and expensive (Hunter, 2002: 85).

The internal factors that affect recruitment can stem from the business's recruitment policy, which advocates internal recruitment before external recruitment. It can also be that the cost of

recruitment is too great for the small business. However, the recruitment of employees with the necessary skills and knowledge is a problem that is well documented. The Investment Climate Survey (2004: 9) reveals that 35% of South African firms view worker skills as the biggest constraint to operations and growth. The Small Business Project (SBP) report- Counting the cost of Red Tape (2005: 27), reveals lack of skilled workers are cited as the fourth constraint to increased employment.

It was also found that skilled and educated workers demand a premium wage. An additional year of education is associated with an 11 – 12 % increase in wages (Investment Climate Survey, 2004: 10). Once recruited, employees must be trained to perform their jobs productively. The investment in the training and development, as mentioned earlier, is vital to the growth of the small business. Unfair wages and salaries result in employees leaving to join larger businesses as the benefits offered by larger companies far outstrip those of the small business. Other factors that compel the small business to offer low salaries are the economy and competition from other businesses, that impact on profits.

The association of the above factors (7.3.1.1 - 7.3.1.4) to the growth of the business was examined using the Chi Square test and the following hypothesis:

$H_0$ : Internal factors do not prevent growth.

$H_1$ : Internal factors prevent growth.

At the 5% level of significance we reject  $H_0$  since the p-values of all the factors are less than 0.05 and conclude that factors such as obtaining finance, cash flow, recruiting and retaining staff, and transport issues, shortage of managerial skills / business expertise and lack of financial understanding prevent growth of the business. The relevant chi-square test statistics in support of this association between the above internal factors and business growth are summarised in (table: 6.5: 85).

### **7.3.2. EXTERNAL CONSTRAINTS**

**7.3.2.1 The Economy:** The economy was seen as a major constraint to business growth. This is indicated by a 72% response rate. This result is in keeping with the findings of the Investment

Climate Survey where macro-economic instability was rated as a serious obstacle to growth by 33% of South African firms (Investment Climate Survey, 2004: 11).

**7.3.2.2 Regulations and Laws:** A majority of 71% of respondents indicated that regulations and laws were a constraint to the growth of their business. Environmental laws were seen to constrain growth while minimum wage regulations, health and safety regulations and affirmative action and BEE policies were not rated as major constraints. The Small Business Project (2005: 35) reveals that respondents see regulatory compliance as an impediment to growth and an expensive burden; compliance costs are also not evenly distributed amongst size classes of enterprises. The SBP research shows that regulatory compliance costs are regressive: small firms bear the heaviest burden in relation to firm size. For very small firms, more than 8% of turnover and more than R13, 000 per employee is spent on annual regulatory compliance. Although these costs fall relatively quickly as we move up the firm-size continuum, they nonetheless remain significant. The SBP study estimates that total recurring compliance costs for the formal sector amounted to nearly R79bn in 2004, equivalent to about 6.5% of SA's GDP in 2003 ( Small Business Project, 2005: 95).

**7.3.2.3 Taxation:** The respondents in Pietermaritzburg view taxation as a serious hindrance to the growth of their businesses. The majority of respondents cited Vat (71%), income tax (71%) and UIF (46%) as impediments to growth. The Skills Development Levy (33%) was not seen as a major constraint to growth. Taxation was seen as a constraint as it takes up too much of managerial time in keeping records (77%); the paying of tax impacts on the cash flow of the business (74%); tax takes money out of the business that can be used for investments (81%) and penalties for late payments are excessive (75%). These findings are in keeping with those of the ICS where tax rates were rated as the fourth constraint to growth (Investment Climate Survey, 2004: 9).

**7.3.2.4 Technology and Innovation:** The use of technology such as computers can greatly enhance the operation and competitive advantage of the small business. Computers are utilised by 55.6% of the surveyed businesses. E-mail and sales were the two most common uses of computers. A total of 48% of respondents indicated that technology was not helping them to

grow their business. Such a result raises concerns as advances in computer technology, coupled with lower prices, have made what was once available only to large businesses accessible to small businesses. The present day computer is capable of running the entire business, provided that the necessary software, research and installation have been professionally done. With regards to innovation, only a quarter of respondents indicated that they were innovative.

**7.3.2.5 Crime:** The survey results indicate clearly that crime is a serious problem among the business firms in Pietermaritzburg. About 42% of the respondents indicated that crime is ‘a very big problem’ and 46% stated that it is ‘a fairly big problem’. The percentage of businesses that were affected by crime in the last twelve months amounted to 28%. The most common types of crimes were burglaries and theft by staff. Crime is viewed as a problem as the costs of repairs and replacements, costs of increased security and the costs of increased insurance premiums are high. Therefore the cost of crime in the Pietermaritzburg region is high. The result of crime as a constraint to growth in Pietermaritzburg is similar to that found by the Investment Climate Survey. The survey found that crime was rated as the fourth factor inhibiting growth in South Africa (Investment Climate Survey, 2004: 9). The report goes on to say that the direct losses due to crime and the cost of security were equal to 1.1% of sales revenue. Security costs account for two thirds of the cost of crime and direct losses account for the additional third (Investment Climate Survey, 2004: 12).

**7.3.2.6 Business Support:** The majority of business owners (64.4%) felt that there was insufficient business support available in Pietermaritzburg. From the comprehensive list provided by the researcher, only the Industrial Development Corporation and Ntiska have been used. Although there are many government initiatives and support programmes available for small businesses, such support is unknown to the large majority of businesses in Pietermaritzburg. According to the survey conducted by the, (Orford, 2004: 46) it was found that, awareness and use of business support was low. The report found that less than 12% of the businesses surveyed had made use of business support. The overall effectiveness of business support was rated negatively (Orford, 2004: 46). This study’s results are similar to the findings of the Global Entrepreneurship Monitor studies.



The association of these external factors (7.3.2.1 -7.3.2.6) to the growth of the business was examined using the Chi Square test and the following hypothesis:

$H_0$ : External factors do not prevent growth.

$H_1$ : External factors prevent growth.

At the 5% level of significance, we reject  $H_0$  since the p-values of all the factors are less than 0.05 and conclude that these factors significantly prevent growth. The chi-square test statistics associated these variables are summarised in (table: 6.6: 86).

#### **7.4 Conclusion**

This chapter has provided an in depth discussion of the findings of the results presented in the previous chapter. These findings reveal the perceptions of the surveyed respondents with respect to the internal and external environments for business growth in the Pietermaritzburg region. The following chapter highlights the salient conclusions that can be drawn from these analyses with respect to the formulated objectives and hypotheses.

## CHAPTER EIGHT

### CONCLUSIONS

#### **8.1 Introduction**

Earlier chapters have shown that the relative role of personal and environmental factors have either an enabling or constraining effect on the growth of the business. Knowledge of such factors is of importance to the field of entrepreneurship as well as to policy makers interested in Small Medium Enterprise (SME) development. With a view to achieving the aims of this study, objectives were developed to guide the research process and achieve the aims of the study. This chapter highlights the salient conclusions that can be drawn from the analyses in relation to the main objectives that the researcher had set out to achieve and investigate.

#### **8.2 To evaluate the internal environmental conditions that favour or constrain entrepreneurship and small business development in the Pietermaritzburg region.**

The following hypothesis was formulated to achieve the above objective:

H<sub>0</sub>: Internal Factors do not prevent growth in the Pietermaritzburg region.

H<sub>1</sub>: Internal Factors prevent growth in the Pietermaritzburg region.

Reviewed literature has shown that internal factors such as access to finance, financial management, recruiting and retaining staff, shortage of managerial skills and a lack of financial skills can seriously dampen the growth of the business. Orford (2003: 46) has shown that proficiency in financial administration and management reduces the probability of business failure. Hodgetts and Kuratko (1995: 17), cite a lack of managerial skills as the third most common cause of business failure. These authors further state that the human resource management process, is one of the most critical functions for small business owners, as it can facilitate a competitive advantage for the firm. The Investment Climate Survey has shown that a shortage of skilled workers and high wage demands have made recruitment difficult.

The analysis of the results of this study has shown that obtaining finance and managing cash flow was perceived to constrain the growth of the business. Furthermore, recruiting and retaining staff was indicated as a constraint. However, staff turnover can be attributed to the lack of training and development as indicated by respondents. Furthermore, factor analysis of this study, has shown that internal constraints account for 48.9% of variance with growth. Therefore, using the data

obtained and the utilisation of the Chi Square test, at the 5% significance level, the above hypothesis was tested. It was found that: obtaining finance ( $\chi^2 = 1162.575$ ;  $df = 4$ ;  $p = .000$ ); cash flow ( $\chi^2 = 1308.646$ ;  $df = 4$ ;  $p = .000$ ); recruitment of staff ( $\chi^2 = 1422.726$ ;  $df = 4$ ;  $p = .000$ ); retaining staff ( $\chi^2 = 1323.780$ ;  $df = 4$ ;  $p = .000$ ); transport issues ( $\chi^2 = 1519.101$ ;  $df = 4$ ;  $p = .000$ ); shortage of managerial skills ( $\chi^2 = 1270.857$ ;  $df = 4$ ;  $p = .000$ ) and lack of financial understanding ( $\chi^2 = 1307.379$ ;  $df = 4$ ;  $p = .000$ ) were perceived by the sampled businesses to constrain growth. The researcher therefore concludes that by identifying the above factors the objective has been satisfied.

### **8.3 To evaluate the external environmental conditions that favour or constrain entrepreneurship and small business development in the Pietermaritzburg region**

The following hypothesis was formulated to meet the above objective:

H<sub>0</sub>: External Factors do not prevent growth in the Pietermaritzburg region.

H<sub>1</sub>: External Factors prevent growth in the Pietermaritzburg region.

The business manager has little control over external factors. However, constant environmental scanning can ensure rapid responses to both favourable and adverse external conditions. The literature reviewed has shown that the small business sector endures most of the laws and regulations. The small business project's (2005: 45), findings clearly indicate that the small business spends more than 8% of turnover on regulatory compliance. The Investment Climate Survey (2004: 96) has shown that cost of crime amounted to 2.272 millions of rands across all sectors. Crime in PMB was found to be a big problem and most firms suffered burglaries. Crime is viewed as a problem as the costs of repairs and replacements, costs of increased security and the costs of increased insurance premiums are high and this is seen to constrain growth.

Technology is one of the generic building blocks of competitive advantage. A competitive advantage is necessary to grow the business successfully (Hill and Jones, 1995: 114). Results of this study revealed that the business sector in Pietermaritzburg under utilise computers and the majority of respondents felt that technology was not helping them to grow the business. The most common use of computers was cited as e-mail. Taxation was seen as a major constraint to growth and specific taxes such as Vat, income tax, U.I.F, and the Skills Development Levy were

identified as constraints. The minimum wage, health and safety, and environmental regulations were identified as constraints. The respondents perceived taxation as a constraint as it takes up too much of managerial time in keeping records (77%); the paying of tax impacts on the cash flow of the business (74%); tax takes money out of the business that can be used for investments (81%) and penalties for late payments are excessive (75%). Factor analysis has revealed that external factors such as the economy, taxation, regulation and laws and competition account for 10.25% of variation with growth. Therefore, the external factors discussed, are perceived by the respondents, as constraints to business growth. These results are similar to those found in the literature. The association of these factors to business growth was tested using the Chi-Square test at the 5% significance level.

Analysis of the results, found that factors such as the economy ( $\chi^2 = 1602.099$ ;  $df = 4$ ;  $p = .000$ ); taxation ( $\chi^2 = 1337.441$ ;  $df = 4$ ;  $p = .000$ ) such as Vat ( $\chi^2 = 1363.411$ ;  $df = 4$ ;  $p = .000$ ), income tax ( $\chi^2 = 1989.798$ ;  $df = 4$ ;  $p = .000$ ), U.I.F ( $\chi^2 = 1218.051$ ;  $df = 4$ ;  $p = .000$ ), skills development levy ( $\chi^2 = 1337.461$ ;  $df = 4$ ;  $p = .000$ ); regulation and laws ( $\chi^2 = 1604.206$ ;  $df = 4$ ;  $p = .000$ ) such as minimum wage regulation ( $\chi^2 = 1366.142$ ;  $df = 4$ ;  $p = .000$ ), health and safety regulations ( $\chi^2 = 1214.707$ ;  $df = 4$ ;  $p = .000$ ), environmental regulations ( $\chi^2 = 1136.761$ ;  $df = 4$ ;  $p = .000$ ), affirmative action and BEE policies ( $\chi^2 = 313.284$ ;  $df = 4$ ;  $p = .000$ ); technology ( $\chi^2 = 1046.327$ ;  $df = 4$ ;  $p = .000$ ); competition in the market ( $\chi^2 = 1110.744$ ;  $df = 4$ ;  $p = .000$ ) and crime ( $\chi^2 = 1060.134$ ;  $df = 4$ ;  $p = .000$ ) were found to constrain the growth of the business. Thus, objective number two has been met.

#### **8.4 To investigate whether the internal or external set of factors constitutes the greater burden on business growth.**

To meet this objective factor analysis was carried out in this study as an exploratory tool in order to reduce the initial set of internal and external factors to a smaller set that adequately explains the growth constraints and could account for being a set of sub constructs. The Principal Components method was used with varimax rotation. The clusters that emerged were classified as factors 1, 2 and 3. Factor 1 consisted of Retaining Staff, Recruiting Staff, Shortage of

Managerial Skills, Keeping up with new Technology and Transport Issues. These factors being internal to the business, labelled as Management, accounted for 36.159% of the variance.

Factor 2 consisted of Cash Flow, Obtaining Finance, Crime and Lack of Financial Understanding. These factors also are internal factors with the exception of crime. Crime no doubt is an external factor. However, the negative impacts of crime such as increased costs of security, replacement and repair costs impact on the internal finances (cash flow) of the business. Using the above explanation factor 2, was classified as Finance, and accounted for 12.794% of the total variance.

The third factor to emerge from the analysis consisted of, The Economy, Taxation, Regulation and Laws and Competition in the Market. Being external in nature, the third factor was therefore classified as external and accounts for 10.257% of variation. From the above results, one can draw the firm conclusion that the management factor has the greatest variance (36.159%) followed by finance (12.794%) and then the external factor accounting for 10.257% of the variation. Factors one and two, both being internal can be said to collectively explain 48,953% of the total variance of the model. Therefore, the conclusion arising from these results is that the internal set of factors constitutes a greater burden (48,953%) than the external factors (10.257%) on the growth of the business. Objective three has therefore been met.

#### **8.5 To examine whether policy on small business / entrepreneurship should focus, more on the internal conditions or external factors.**

With a view to satisfying objective four, that examines whether policy on small business / entrepreneurship should focus more on the internal conditions or external factors, use is again made of the results from the factor analysis. As shown above, the internal factors account for the majority (48,953%), of the total variance (59,210%), explained in the model and the researcher therefore concludes that policy on small business should focus more on the internal conditions than external factors.

## **8.6 Variation in Average Growth and Gender.**

H<sub>0</sub>: There is no difference in the average growth between males and females.

H<sub>1</sub>: There is a difference in the average growth between males and females.

In the study, there were 96 male and 64 female entrepreneurs. Their employment creation potential, on average, seems to differ. The males had a mean employment of 16.7 while females had an average employment of 6.09. Therefore, on average, the males have almost three times the job creation potential than females. These results indicate that in order to reduce unemployment, one of the routes would be to provide more assistance and support for female entrepreneurs.

## **8.7 Variation in Average Growth and Activity**

H<sub>0</sub>: there is no difference in the average growth between activities of business.

H<sub>1</sub>: there is a difference in the average growth between activities of business.

Of the different sectors, researched growth was recorded across all. However, the average growth ranged from (18.6 employees) for the manufacturing sector to (6.7988 employees) for the trade sector. Anova testing at the 5% level of significance ( $F = 3.22$ ;  $df = 4$ ;  $p = 0.008$ ), indicates that there is a difference in the average growth between the groups. It is therefore concluded that certain sectors have a greater employment potential than others. In the Pietermaritzburg region, the manufacturing sector has the greatest potential. These results indicate the sectors (trade, services and other) that need support and development in order to improve their employment creation potential.

## **8.8 Variation in Average Growth and Ethnic Groups**

H<sub>0</sub>: There is no difference in the average growth between ethnic groups.

H<sub>1</sub>: There is a difference in the average growth between ethnic groups.

Analysis reveals that there is no difference in the average growth between ethnic groups ( $F = 2.032$ ;  $df = 3$ ;  $p = .112$ ). However, within ethnic groups there appears to be a difference.

### **8.9 Variation in Average Growth and Legal Status**

$H_0$ : there is no difference in the average growth between legal statuses of business.  
 $H_1$ : there is a difference in the average growth between legal statuses of business.

However, it was found using Anova, ( $F = 2.736$ ;  $df = 4$ ;  $p = .005$ ), that a difference exists between the average growth and the legal status of the business. Partnerships (15 employees) have a higher mean growth of employees than sole proprietors (14.2 employees), Close corporations (10.3 employees), companies (1.0 employee) and other (franchises: 2.1 employees). The conclusion is that the partnership has the highest job creation potential in terms of legal statuses in the Pietermaritzburg region.

### **8.10 Variation in Average Growth and Educational Level**

$H_0$ : there is no difference in the average growth between education level groups.  
 $H_1$ : there is a difference in the average growth between education level groups.

Educational level is well documented in the literature review. Numerous studies have shown that higher levels of education, more especially tertiary education, produces more growth than secondary education (Storey, 1994: 129; Small Enterprise Development Agency, 2004: 62; and Von Broembsen *et al*, 2005: 29). This research has highlighted the fact that the educational level of the entrepreneur / manager has a positive effect on growth. The potential of tertiary educated (postgraduate degrees) entrepreneurs to create employment (22.2214 employees) is greater than their counterparts who have only completed secondary education (15.5240). Using Anova, at the 5% risk level it was found ( $F=3.045$ ;  $df = 4$ ;  $p = .007$ ) that there is a difference between average growth and the educational levels. It is therefore concluded that the job creation potential (growth of the business) of educated business individuals, increases with tertiary education.

### **8.11 Variation in Average Growth and Exposure to Training**

H<sub>0</sub>: there is no difference in the average growth between business managers/entrepreneurs who have been exposed to training and to those who have not been exposed to training.

H<sub>1</sub>: there is a difference in the average growth between business managers/entrepreneurs who have been exposed to training and to those who have not been exposed to training.

The exposure to training and prior business experience of entrepreneurs / managers has been found to enhance growth. The importance of training to the small business sector cannot be over emphasised. Human resource development (HRD) can be defined as a set of systematic and planned activities designed by the business to provide workers with the opportunities to learn necessary skills to meet current and future job demands (Desimone *et al*, 2002: 3). Well-educated, trained and skilled staff is a source of competitive advantage for any business venture as costs are reduced, productivity increases and a climate or culture conducive to growth is created.

These results show that individuals who had been exposed to some form of training recorded a higher mean growth rate (15.9634 employees) compared to those that had no exposure (13.2594 employees). Making use of the independent sample t-test, it was found at the 95% confidence level that ( $t = 9.235$ ;  $df = 155$ ;  $p = .014$ ) there is a difference in the average growth between those who have been exposed to training and to those who have not. The conclusion that can be drawn from the results is that the job creation potential of those entrepreneurs / managers who have been exposed to some form of training is much greater than those who have had no exposure to training. Therefore, it is necessary for would be entrepreneurs, to undergo some form of business training prior to venture creation.

### **8.12 Variation in Average Growth and Sources of Start-Up Capital**

H<sub>0</sub>: Sources of start-up capital do not account for a difference in average labour growth.

H<sub>1</sub>: Sources of start-up capital do account for a difference in average labour growth.



Access and the cost of financing ranks among the top five constraints in Sub-Saharan Africa, according to the Investment Climate Survey (Investment Climate Survey, 2004: 12). The lack of adequate financing is the most serious constraint during the formation of a new venture (Mahadea, 1997: 72). This study has revealed that the most common form of start-up capital was internal funds. With respect to sources of start-up capital, it was found that the use of external funding has greater employment potential (13.85 employees) than internal (13.6 employees) or a combination of internal and external funding (11.5 employees). The test results ( $F = 10.127$ ;  $df = 2$ ;  $p = .029$ ) confirms that at the 5% significance level there is a difference in the average growth between sources of start-up capital.

Growth would demand that entrepreneurs perform a critical SWOT analysis. This study clearly shows that when considering growth decisions, the entrepreneurs have to look critically at the internal factors over which they have some form of control. The external factors account only for about 10% of the variation in the growth of the business. This therefore suggests that the focus of SWOT analysis should be on the internal environment-especially management (36%) and finance (12.79%).

### **8.13 Determinants of Growth**

The determinants of growth were done using multiple regression analysis. Different models were initially fitted to check the variation and influence of the independent variables, which are different groupings of questions measuring a certain trait against the dependent variable, average growth in employees.

A parsimonious regression model emerged that explained about 45% of the variation in average growth in the study.  $Average\ Growth = \beta_0 + \beta_1 q_4 + \beta_2 q_6 + \beta_3 q_7 + \beta_4 q_8 + \beta_7 q_{30} + \epsilon$ , where  $\beta_0$  = constant term and  $\epsilon$  = the error term. The variables found to have a significant influence on growth were: Level of Education ( $\beta = 1.027$ ;  $t = 3.05$ ;  $p = .016$ ), Legal Status ( $\beta = 3.131$ ;  $t = 10.1$ ;  $p = .0$ ), Start-Up Capital ( $\beta = 8.493$ ;  $t = 4.40$ ;  $p = .002$ ), Exposure to Training ( $\beta = 7.219$ ;  $t = 14.61$ ;  $p = .003$ ) and Business Support ( $\beta = 9.088$ ;  $t = 2.72$ ;  $p = .008$ ).

In analysing the variables it becomes evident that educational level has an effect on the growth of the business. As shown above tertiary education has a higher growth potential than secondary education. Partnerships as a choice of legal form have a higher growth potential than close corporations and companies in Pietermaritzburg. Literature has shown that access to finance is a serious constraint to growth, and this study has shown that external start-up funds have a higher growth potential than internal funding. Exposure to training (discussed above) also has the ability to record higher growth rates.

Business support in the literature was found to be lacking. Small enterprises are either unaware of or do not use the services offered by the government and where they do use government support, small enterprises are skeptical about the quality of this support (Small Enterprise Development Agency, 2004: 65). In this study, a majority (64.4%) of business owners attested to this fact and only two of the nine support agencies were utilised. This indicates that the support agencies are not fulfilling their purpose due to a lack of advertising or that their support is not of a suitable standard. Therefore, it can be concluded that meaningful business support is required for business growth.

#### **8.14 Conclusion**

This chapter has, utilising the results obtained from this study and the reviewed literature satisfied the hypotheses that were formulated for this study. However, the results and conclusions obtained reveal shortcomings and problems that constrain the growth of the small business sector in Pietermaritzburg. The following chapter provides recommendations based on these shortcomings to business owners and policy makers alike, to foster and promote the growth of the small business sector.

## **CHAPTER NINE**

### **RECOMMENDATIONS**

#### **9.1 Introduction**

This chapter will revolve around changes that need to be considered with regard to business growth and what recommendations can be made to business owners, the Pietermaritzburg Chamber of Commerce, business support agencies and policy makers in both the government and private sector. In formulating policies and developing SMME assistance programs, information is required so that attention and finances can be focused on the appropriate growth areas, and where the rewards can be greatest in terms of per Rand cost or assistance.

An awareness or knowledge of the problems / constraints influencing small business is a vital first step in the managing and avoiding some of these issues. Furthermore, the awareness of possible future problems facing entrepreneurs/small business managers will enable them to be forewarned and proactive in their decision making. Starting a business is risky at best, but the chances of success are enhanced if the problems anticipated are properly understood and addressed prior to the business starting.

#### **9.2 Recommendations**

The recommendations provided are based according to the results and constraints identified in this study, especially from the external and internal environments. The internal environment gave rise to problems resulting from a lack of management skills, management behaviour and problems experienced in the functional areas of finance, human resources and the use of technology. Growth would demand that entrepreneurs perform a critical SWOT analysis. This study clearly shows that when considering growth decisions, the entrepreneurs have to look critically at the internal factors over which they have some form of control. The external factors account only for about 10% of the variation in the growth of the business. This therefore suggests that the focus of SWOT analysis should be on the internal environment-especially management (36%) and finance (12.79%), as reflected by the factor analyses.

### **9.2.1 Lack of management skills / Business expertise**

One of the most common causes of business failure is poor management (Hodgetts and Kuratko, 1995: 17). This study has found that a lack of managerial skills and business expertise is prevalent in the small business sector in Pietermaritzburg. The shortage of managerial skills was also identified, in this study as a significant constraint in the factor analysis. Therefore, success and performance of any business venture requires relevant management skills and business expertise. These skills are also necessary to formulate goals and objectives and map the course of the business to meet these objectives through planning, organising, leading and controlling. It is recommended that all small business owners have a comprehensive business plan that is followed religiously. Those that lack business expertise need to undergo training that will enable them to achieve business skills. For those that are planning to start a new business venture, the Masters in Business Administration, is an excellent course that teaches the requisite business skills needed for business success.

Other important management skills required by small business managers are strategic planning and time management. The small business manager is known to spend long hours at work and enjoys a reduced social life. With careful planning and time management as well as the art of delegation a small business manager can achieve a better balance in terms of business and social life.

### **9.2.2 Financial management**

Financial management skills was shown to be necessary throughout the entire entrepreneurial process as well as the life cycle of the business ( Nieman and Bennet, 2002: 62; Hisrich and Peters, 2002: 223; Wickham, 2001: 190 and Sullivan, 2000: 164). The second factor arising from the factor analysis was labelled finance and comprised of variables cash flow, obtaining finance and lack of financial understanding. Many small and medium sized businesses fail to grow because their strategy is not aligned to the financial objectives of the business. This occurs because more time is spent working inside the business and less time is spent on growing the business. In order for the business to be successful, the following strategic questions need to be answered:

- What profit levels are needed?
- What are the fixed costs?
- What is the percentage profit margin that can be achieved?
- What level of turnover is needed to cover the costs, i.e. what is the breakeven point? and
- What additional turnover is needed to achieve the desired level of profit?

These financial objectives can be easily calculated from a simplified income statement using vertical trend analysis. It is imperative for business owners to understand that turnover is the one variable that they have least control over, as this depends on attracting the correct customer at a reasonable margin with the correct product mix. The strategic choices to make the business more profitable without chasing sales indiscriminately, is to influence the gross profit margin by:

- manipulating the product and customer mix, or
- forming alliances, in the spirit of the Porterian framework, with suppliers and obtaining better prices, or
- the more desired route of cutting operating costs.

In choosing the last option, the business owner can reduce the increase in costs below that of growth in turnover and this will increase operating profit substantially.

Finance costs are another dimension that can be manipulated by using your terms as far as debtors and creditors are concerned, with the result that you improve your debtor collections and extend your creditor payments. In so doing, the cash conversion cycle is improved and the business is made self-funding, while avoiding costly finance charges.

Access to finance, identified from the factor analysis, both for start-up and for expansion purposes, plays a crucial role in making the business successful. Start-up capital was identified in this study as one of the independent variables of the parsimonious regression model that contributed to average growth of the business. It was further established that external sources of funding produced on average a higher growth rate than other sources of funding. It is therefore recommended that banks and business support address this issue by making access to finance easier and affordable.

### **9.2.3 Human resource practices**

It was established in the Investment Climate Survey that worker skills and high wages make the management of human resources difficult (Investment Climate Survey, 2004: 37). Labour regulations further compound this problem (Investment Climate Survey, 2004: 66). However, employee productivity is one of the key determinants of a business's efficiency and cost structure. The more productive the employees, the lower will be the unit costs (Hodgetts and Kuratko, 1995; 371). The challenge for the small business is to devise ways to increase employee productivity. This study has identified recruiting and retaining staff as growth constraints. It is recommended that the small business utilise job profiling psychometric testing, once the preserve of big companies, to recruit new employees. Such testing although expensive will ensure that the correct employee, with the requisite skills and aptitudes is employed.

One way of retaining staff is through training and development as well as lucrative salary offers. Training of staff has been identified in this study as lacking. Very few respondents indicated employee training. Training can upgrade employee skill levels, bringing the business productivity-related efficiency gains. These training programmes need not be costly and can be achieved by rotating employees through the various departments. This will ensure that they acquire general skills. Extensive use can also be made of on-the-job training and employees can be encouraged to obtain required skills through correspondence courses, whose costs the employers can reimburse on completion of the course. Lastly, participation in team activities focused on improving business performance results in a general upgrading of employee skill levels. Such a workforce is essential for cost reductions, improved production and creates a climate conducive for growth and expansion. This climate is also necessary for innovation and risk taking and ultimately helps the business to achieve a competitive advantage and a larger share of the market.

### **9.2.4 External Environment**

Unfortunately, little can be done by the individual entrepreneur, to curb the impact of environmental variables such as corruption, inflation and interest rates but small business entrepreneurs should plan strategically and take into account the possibility of a volatile economic environment (Fry *et al*, 2000: 165). Through constant scanning of the environment by

using the management tools, SWOT and PESTLE (political, economic, social, technological, legal and environmental), the entrepreneur / manager will be able to take advantage of favourable changes in the economic environment and protect the business against adverse changes (Hill and Jones, 1995: 11). The business managers must realise that due to the size of the small business, they can respond more quickly and at a lower cost, to adverse changes in the environment than large corporations.

### **9.2.5 Innovation**

This study has revealed that less than a third of the surveyed respondents are innovative. Innovation is perhaps the single most important building block of competitive advantage. Although not all innovations are successful those that are, give the business something unique that competitors lack. This allows the business to differentiate itself from rivals and charge a premium for this uniqueness (Hill and Jones, 1995: 109). As South Africa becomes an integral part of the global and electronic economy, innovative and differentiating strategies have to be implemented in order for small businesses to obtain a competitive advantage. This can only be achieved by allowing entrepreneurs and employees to take risks, embrace new technology and experiment with different ideas. This implies that a climate conducive for the sharing of ideas and creativity must be created and encouraged within the business.

### **9.2.6 Use of Technology**

Technology was identified as one of the variables of factor one from factor analysis. The efficient use of technology, such as computers is one of the generic building blocks of competitive advantage. Information technology plays a significant role in helping the small business to realise its full potential (Longenecker *et al*, 1994: 593). However, this can only be achieved if the small business makes a solid technological investment, by partnering an experienced consultant who can offer guidance and advice on the most suitable technology deployment programme. Information technology must not be seen as a grudge expense and small business owners need to realise that they do not have to invest in the most elaborate technology on offer, but should rather consider by making use of the total cost of ownership method, the technology that will add the most value to their specific business needs. To leverage this technology investment fully, the business owner needs to identify a technology adoption strategy that will add the most 'cents' to

the bottom line. This can be done by investing in the most fundamental business services first, including e-mail and the internet, which are critical tools and play an important role in driving business growth. The internet provides the small business owner access to a whole world of research, competitor data and other useful information that gives them an added advantage.

### **9.2.7 Crime**

Crime in Pietermaritzburg was found to be a big problem that affected 95% of respondents. The Investment Climate Survey has shown that losses due to crime amount to 2,272 millions of Rands across all business sectors in South Africa (Investment Climate Survey, 2004: 96). In order to combat and prevent crime, joint ventures between the police, the business sector and the Pietermaritzburg Chamber of Commerce have to be created. This venture can then focus on improving safety in the business sector where crime is most predominant, by first conducting business surveys. The criminal justice system can also contribute by imposing stricter sentences for crimes against the small business sector.

### **9.2.8 Business Support**

The regression results also clearly show that business support significantly influences growth. Business support is an area for concern, as surveyed respondents indicated that they were unhappy with the current support provided. The government has itself admitted that measures to support small enterprises have been less than satisfactory. Business support according to (Orford *et al*, 2004: 45-53) is found to be lacking in three respects:

- Lack of awareness about the programmes offered by the government;
- difficulty in accessing these programmes, and
- poor service delivery by government programmes.

Therefore, in order to increase use of government programmes, government would need to significantly improve its communication and marketing of its support services and the delivery thereof. However, improved awareness and greater utilisation is likely to significantly strain the capacity of existing programmes and potentially further reduce the quality of these programmes. A more promising strategy, therefore, may be to focus efforts on improving the quality of



services offered by exploiting the capacity and knowledge of private service providers through public-private partnerships, and sack incompetent 'managers' in the public sector. Therefore, rather than redoubling its efforts, government should refocus its efforts as success is likely to come from doing less well rather than more badly.

### **9.2.9 Educational Level**

The educational level, of both the owner and employees, has the ability of enhancing the growth of the business. Numerous studies have shown that higher levels of education, more especially tertiary education, produce more growth than secondary education (Storey, 1994: 129; Small Enterprise Development Agency, 2004: 62; and Von Broembsen *et al*, 2005: 29). In this study, education (more especially tertiary) has also been shown to possess a greater job creating potential than secondary education. Therefore, the educational system has an important role to play in creating an entrepreneurial culture as well as imparting knowledge and skills necessary for meaningful employment. Academics and educators can direct their teaching and course development towards addressing specific problem areas, to increase the chances of business success by teaching students to better understand the anticipated problems when entering the business arena.. A sound education relevant to business and market needs will enable small business managers to be better equipped and more informed to make decisions and to steer business away from known problem areas. The recruitment of staff with high levels of education will also add value to the business.

### **9.2.10 Regulations and Laws**

Regulations and laws affect the financial management of businesses either directly or indirectly. Highlighted in chapter four were the findings of the small business project's: Counting the cost of red tape. It was shown that the average business employing fewer than five people spends about R13000 a year per head on regulatory compliance (Small Business Project, 2005: 45). The Investment Climate Survey (2004: 66) has shown that labour regulations have a constraining effect on the growth of the business. This study has also found that regulations and laws constrain the growth of the business. This has serious implications for job creation as the small business sector has been shown to create more employment than larger corporations do. It is recommended that the regulatory authorities need to simplify the regulatory environment. This can be achieved

by making use of established techniques such as regulatory cost surveys and regulatory impact assessments. The golden rule should be that cost imposed on the small business sector by regulations must be justified by the benefits it creates.

### **9.3 Conclusion**

This chapter has made recommendations for business owners, the Pietermaritzburg Chamber of Commerce and policy makers from all levels of government. Such recommendations are necessary for the formulation of policies that will create an enabling environment for the growth of the SME sector. The penultimate chapter briefly explains the limitations of this study and provides guidance for future research.

## **CHAPTER TEN**

### **LIMITATIONS AND FUTURE RESEARCH**

#### **10.1 Introduction**

This chapter aims to highlight the limitations experienced by the researcher in conducting this study and provides guidance for further research.

#### **10.2 Limitations**

The limitations, which have impacted on the researcher, were the following:

##### ➤ 10.2.1 Time Constraints

Time was a limitation in two ways. Firstly, due to the nature of this research, ethical clearance had to be obtained from the relevant authorities of the University. This clearance was only obtained on the 19<sup>th</sup> of July 2006. Therefore, the questionnaires could only be handed out after this date. Secondly, the task of administering and collecting the questionnaires was heavily constrained by time as submission deadlines had to be met.

##### ➤ 10.2.2 Finances

Financial constraints are a continual and obvious limitation. The researcher did have some financial limitations, but endeavoured to deliver the best results. Owing to the financial and time constraints, a larger sample, though desirable, could not be considered.

##### ➤ 10.2.3 Non Responses or Neutrality

The structured nature of the questionnaire limited the amount and content of data gathered. In the firm specific section of the questionnaire, respondents were asked to rate factors affecting business growth using a Likert scale. One of the options of the scale was “neutral”, the researcher feels that this option was mostly chosen for certain questions and may have invariably provided an “escape” to not answering the question. Though overall the researcher found this not to be a major concern as it was only a minority of respondents.

In spite of these constraints, the results can be deemed satisfactory, by producing a Cronbach Alpha value of 0.8687.

### **10.3 Future research**

Cross sectional studies provide a “snapshot” of the situation at a specific point in time. Such studies are therefore limiting in making recommendations and conclusions for the future. It is suggested that in order to get more valid results, longitudinal studies are recommended in the area of SME entrepreneurship, using robust statistical techniques. Too many studies concentrate on success and trait factors. Future research should go beyond these saturated areas and the approach should focus on a holistic perspective.

## CHAPTER ELEVEN

### CONCLUSION

The importance of the Small Medium Enterprise (SME) sector lies in its contribution to the Gross Domestic Product and its employment creation potential. These contributions are imperative for a developing economy such as South Africa. Recognising the potential of this sector, the government has, since 1994 endeavoured to promote and grow the SMME sector. However, to date the policies and regulations created to enable this growth has not met with resounding success.

With a view of unearthing possible constraints to the growth of the SME sector, the researcher has undertaken this study in Pietermaritzburg. Using reliable and valid statistical methods, the determinants of the growth of the firm in terms of labour employment and the internal and external constraints to business growth in Pietermaritzburg were identified. The parsimonious regression model explained about 45% of the SME employment growth in the Pietermaritzburg region. The factor analyses jointly explained about 60% of the internal and external constraints on business growth. The average growth in terms of employment looks promising and can only improve with developments such as the Liberty Mall extension and the imminent Camps Drift development.

Knowledge of problem areas experienced by small businesses provides valuable information for policy makers in both the government and private sector in formulating policies and developing SME assistance programs. Based on the results, recommendations are made to the policy makers with an interest in SME development, on how to address some of the constraints, to secure on optimal development of small business in Pietermaritzburg. These recommendations are also useful to the actual entrepreneurs and to business networks, such as the Chamber of Commerce and funding institutions.

SME entrepreneurs are the wealth creators and they deserve to be supported and treated with dignity and respect!

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APPENDIX :A

ETHICAL CLEARANCE



RESEARCH OFFICE (GOVAN MBEKI CENTRE)  
WESTVILLE CAMPUS  
TELEPHONE NO.: 031 – 2603587  
EMAIL : ximbap@ukzn.ac.za

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19 JULY 2006

MR. MK PILLAY (862868796)  
MANAGEMENT STUDIES

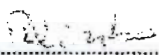
Dear Mr. Pillay

**ETHICAL CLEARANCE APPROVAL NUMBER: HSS/06285A**

I wish to confirm that ethical clearance has been granted for the following project:

**“Entrepreneurs’ perception of the environment for business growth in Pietermaritzburg”**

Yours faithfully

  
.....  
MS. PHUMELELE XIMBA  
RESEARCH OFFICE

**PS: The following general condition is applicable to all projects that have been granted ethical clearance:**

**THE RELEVANT AUTHORITIES SHOULD BE CONTACTED IN ORDER TO OBTAIN THE NECESSARY APPROVAL SHOULD THE RESEARCH INVOLVE UTILIZATION OF SPACE AND/OR FACILITIES AT OTHER INSTITUTIONS/ORGANISATIONS. WHERE QUESTIONNAIRES ARE USED IN THE PROJECT, THE RESEARCHER SHOULD ENSURE THAT THE QUESTIONNAIRE INCLUDES A SECTION AT THE END WHICH SHOULD BE COMPLETED BY THE PARTICIPANT (PRIOR TO THE COMPLETION OF THE QUESTIONNAIRE) INDICATING THAT HE/SHE WAS INFORMED OF THE NATURE AND PURPOSE OF THE PROJECT AND THAT THE INFORMATION GIVEN WILL BE KEPT CONFIDENTIAL.**

cc. Faculty Officer (Post-Graduate Studies)  
cc. Supervisor (Prof. D Mahadea)

**APPENDIX: B**

**THE MEASURING INSTRUMENT / QUESTIONNAIRE**

An investigation of Entrepreneurs' perceptions of the Environment for Business Growth in the Pietermaritzburg region.

**CONFIDENTIALITY**

This Questionnaire will be used strictly for the abovementioned research and for no other purpose. Your name will not be recorded in order to maintain your anonymity and to allow you to answer the questions honestly and to the best of your ability.

---

**DEMOGRAPHIC DATA**

**Mark the Appropriate Box**

1. State the Number of years your business is in operation.

-----

2. Tick the appropriate box:

Male	Female
------	--------

3. Please indicate your ethnic group: Tick appropriate box.

White	Black	Asian	Coloured	Other, Please Specify
-------	-------	-------	----------	-----------------------

4. Highest Level of Education of Owner:

No Formal Education	
Primary School Education	
High School Education	
College Education	
University Degree	
University Post Graduate Degree	
Other, Please specify	

5. What is the main activity of your business?

Manufacturing	
Trade	
Transport	
Construction	
Travel and Tourism	
Agriculture	
Finance	
Services	
Other( Please Specify)	

6. What is the Legal status of your business?

Sole Proprietorship ( incl. husband & wife )	
Partnership	
Close Corporation	
Company	
Other ( Please Specify)	

7. What was the source of capital for start up of your business?

Internal ( Personal Funds)	
External (Banks, Investors ...)	
Combination of Both	

8. Have you been exposed to any Training?

YES	NO
-----	----

9. If Yes, What was the Nature of such training?

-----

-----

10. Please state the duration of the above Training?

-----

**FIRM SPECIFIC DATA**

**LIKERT SCALE:** 1= Strongly Disagree; 2 = Disagree; 3 = Neither Agree nor Disagree;  
 4 = Agree; 5 = Strongly Agree

**USING THE ABOVE SCALE, PLEASE RATE THE FOLLOWING QUESTIONS**

11. In what ways are you looking to grow the business?

Move into new markets	1	2	3	4	5
Introduce new products/services	1	2	3	4	5
Increase turnover/sales with existing product/market mix	1	2	3	4	5
Something else, please specify					

12. Do you expect that growing your business will require you to do any of the following?

Take on (more) staff	1	2	3	4	5
Expand premises/add more sites	1	2	3	4	5
Invest in more capital equipment	1	2	3	4	5
Seek external funding, borrowing	1	2	3	4	5
Something else, please specify					

13. Do you expect to fund your business growth using internal finances or from external finance providers?

Internal finance	1	2	3	4	5
External finance	1	2	3	4	5
Both	1	2	3	4	5
Other Please Specify					

14. What would you regard as the main obstacles to the growth of your business in general?

The Economy	1	2	3	4	5
Obtaining Finance	1	2	3	4	5
Cash flow	1	2	3	4	5
Taxation	1	2	3	4	5
Recruiting staff	1	2	3	4	5
Retaining staff	1	2	3	4	5
Transport issues	1	2	3	4	5
Regulations and Laws	1	2	3	4	5
Keeping up with new technology	1	2	3	4	5
Competition in the market	1	2	3	4	5
Shortage of managerial skills/ business expertise	1	2	3	4	5
Lack of financial understanding	1	2	3	4	5
Crime	1	2	3	4	5
Other Please Specify					

15. Which of the following do you regard as a major hindrance to the growth of your business?

VAT ( Indirect Tax )	1	2	3	4	5
Income Tax (Direct Tax )	1	2	3	4	5
U.I.F	1	2	3	4	5
Skills Development Levy	1	2	3	4	5
Other, please specify					

16. In which of the following ways do you consider taxation to impact negatively on your business?

Takes up too much managerial time/attention	1	2	3	4	5
Amount of time involved in keeping records , paperwork	1	2	3	4	5
Impact on cash flow of paying tax	1	2	3	4	5
Tax takes money out of the business that could be used for investment	1	2	3	4	5
Penalties for late payment are excessive	1	2	3	4	5
Competition from businesses that perhaps avoid tax	1	2	3	4	5
Other, please specify					

17. Which other regulations do you consider to be an obstacle to the growth of the business?

Minimum wage regulations	1	2	3	4	5
Health and safety regulations	1	2	3	4	5
Environmental regulations	1	2	3	4	5
Affirmative Action and BEE Policies	1	2	3	4	5
Other please specify					

18. How big a problem is crime in relation to your business and the area around you?  
(Tick appropriate box)

A very big problem	
A fairly big problem	
Not a very big problem	
Not a problem at all	

19. Has your business been a victim of crime in the last 12 months? Tick appropriate box.

YES	NO
-----	----

20. If, Yes what was the frequency of such acts?

-----



21. What type of crime was this / were these? (Tick appropriate box /es)

Burglary	
Theft by staff	
Fraud	
Arson	
Theft by others	
Violent crime ( Armed Robbery)	

22. How has crime affected your business?

Costs of replacements and repairs	1	2	3	4	5
Cost of increased security	1	2	3	4	5
Increased insurance premium	1	2	3	4	5
Loss of income from closure	1	2	3	4	5
Absence of staff	1	2	3	4	5
Loss of customers through fear of crime	1	2	3	4	5
Difficulty in recruitment	1	2	3	4	5
Other, please specify					

23. Over the past 12 months, has your business arranged any staff development or training?  
Tick the appropriate box.

YES	NO
-----	----

24. If Yes, Please indicate the nature of the training

-----

25. Does your business use technology such as computers. Tick the appropriate box.

YES	NO
-----	----

26. Do you use it for...? (Tick appropriate box/es)

E-mail	
Sales	
Purchasing	
Record Keeping	
Wages and salaries	
Stock Control	
E- Commerce	

27. Do you think modern technology is helping you to grow your business? Tick appropriate box.

YES	NO
-----	----

28. With regards to innovation and the conduct of your business, are you doing something **unique** that others cannot so easily replicate or match? Tick appropriate box.

YES	NO
-----	----

29. If yes, can you mention any unique feature of your business? -----

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30. Do you think there is enough business support available in your local area for small businesses? Tick appropriate box.

YES	NO
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31. Have you heard of any of the following organisations that provide business support? (Tick the appropriate box/es)

Industrial Development Corporation	
Ntsika	
Khula	
Brain ( Business Referral and Information Network)	
Frain (Franchise Advice and Information Network)	
Namac Trust (Manufacturing Authority)	
Business Partners Limited	
Ithala	
Seda ( Small Enterprise Development Agency)	

32. Lastly, please provide the following information. Remember all information is strictly confidential.

	At Inception	2004	2005
Number of Employees			
Average monthly Sales in Rands ( an estimate is acceptable)			

**YOUR TIME AND VALUABLE INPUT IS MUCH APPRECIATED!!!**

APPENDIX: C

CONSENT FORM

I .....( Full names of participant)  
hereby confirm that I understand the contents of this document and the nature of the research  
project, and I consent to participating in the research project.

I understand that I am at liberty to withdraw from the project at any time, should I so desire.

SIGNATURE OF PARTICIPANT

DATE

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