

ANALYSING THE NEEDS OF SMALL AND MICRO-ENTERPRISE OWNERS: A SOUTH AFRICAN SUBURB CASE STUDY

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—Abstract —

Small and micro-enterprises are significant contributors to the economy of a country with regard to growth, employment and poverty alleviation. However, small and micro-enterprises in South Africa are faced with prevalent threats to their survival and growth. A lack of access to finance and the basic skills and knowledge to manage these enterprises create several challenges. This study analysed the motivations behind start-up and the most prevalent needs, especially regarding financial literacy, of small and micro-enterprise owners with the aim to assist these owners in overcoming the challenges. In total 50 small and micro-enterprise owners from a selected suburb took part in the study. Purposeful sampling was used. Data was gathered using a newly developed survey and analysed using SPSS. The study established that a significant number of enterprises were started out of necessity, with the majority of initial funding coming from personal capital. The findings further revealed a great need for financial literacy among the owners; however, funds to grow their enterprises seemed the greatest need. In addition to contributing to the limited corpus of data on small and micro-enterprises in South Africa, this study provides valuable insight into start-up motivation and financial literacy and support needs of small and micro-enterprises. This should be useful in establishing interventions to spur on enterprise start-ups and addressing the need for financial literacy. Relevant government departments should consider implementing an advisory programme for prospective enterprise owners before funding is granted, as well as a financial literacy mentorship tier programme for small and micro-enterprises. Furthermore, an opportunity exists for the Unemployment Insurance Fund to contribute in this regard by implementing an entrepreneurship training programme.

Keywords: Small and micro-enterprise, enterprise start-up, needs, financial literacy

JEL Classification: G00

1. INTRODUCTION

Small and micro-enterprises are significant contributors to the economy of a country with regard to growth, employment and poverty alleviation, especially in developing countries (Fielden *et al.*, 2000; Okpara & Wynn, 2007; Singh *et al.*, 2015). They are, however, faced with a wide range of challenges that impede on their development and long-term viability (Okpara & Wynn, 2007; Bowen *et al.*, 2009). Given their vital role in the economy (Fielden *et al.*, 2000; SBP, 2013), it is essential to understand and address these challenges (Mthimkhulu & Aziakpono, 2015).

Benzing and Chu (2009) note that an understanding of start-up motivation would further aid policy-makers in designing policies that encourage and promote the creation of enterprises. The purpose for starting an enterprise depends on the circumstances of the prospective owner at the time of start-up (Watson *et al.*, 1998; Shaver *et al.*, 2001). The 2014 Global Entrepreneurship Monitor report (Singer *et al.*, 2015) shows that 28.2% of South African enterprises established are motivated by necessity, whereas 71.3% are driven by opportunity.

One of the most prevalent constraints faced by prospective enterprise owners is access to start-up financing, specifically third-party financing (Fielden *et al.*, 2000; Mthimkhulu & Aziakpono, 2015). Restricted access to finance is also a major reason behind the failure of enterprises (Okpara & Wynn, 2007). A lack of financial literacy in small and micro-enterprises is often associated with challenges such as a lack of access to finance (Miller *et al.*, 2009; Chimucheka & Rungani, 2011). Small and micro-enterprises are prevented from accessing finance due to, among other things, improper business plans, insufficient financial management knowledge and inadequate book-keeping (Chimucheka & Rungani, 2011). Other challenges identified from the literature (Fielden *et al.*, 2000; Bowen *et al.*, 2009, 2010; Kvedaraite, 2014) include the inability to find suitable employees and deal with competition, and a lack of institutional support. The current study first investigated the start-up motivation of small and micro-enterprise owners in South Africa. This will add to the limited research on small and micro-enterprises in South Africa.

The challenge is however not only on creation but also sustaining the enterprise. Statistics indicate that small and micro-enterprises have a high failure rate within the first five years from commencing trade (Okpara & Wynn, 2007; Ligthelm,

2008). What appears to be more important than encouraging enterprise start-up, is therefore sustaining these enterprises, given their low survival rate (Okpara & Wynn, 2007; Ligthelm, 2008). According to Kolvereid and Isaksen (2006), it is crucial that prospective enterprise owners assess whether they are equipped with the basic skills necessary to ensure the sustainability of their enterprises before starting an enterprise.

Research on the failure of these enterprises has outlined a lack of financial literacy as the main determinant of failure (Okpara & Wynn, 2007; Chimucheka & Rungani, 2011; Irwin, 2013; Barte 2012). The South African Minister of Small Business Development, Lindiwe Zulu, agrees by stating that the high failure rate among small and micro-enterprises in the country is mainly due to a lack of financial literacy (Zwane, 2014). Analysing the needs of small and micro-enterprises could assist in developing strategies and delivering support services to the owners (OECD, 2004). This is the second focus of the study.

Below follows the background to the study, as well as the research methodology for the study. This is followed by a summary and discussion of the findings, recommendations and conclusions.

2. BACKGROUND

According to Shaver *et al.* (2001), a new enterprise is created as an intentional act that engages repeated attempts to exercise control over the business process, in order to achieve the desired outcome of the entrepreneur.

Micro-enterprises, for the purpose of this study, are defined as enterprises that employ up to a maximum of five employees, while small enterprises between six and 50 employees. This is consistent with the definition of small and micro-enterprises by the OECD (2000) and the National Small Business Amendment Act, 2003 (Act 26 of 2003, RSA).

Various studies (ANZ Banking Group, 2003; Miller *et al.*, 2009; Lusardi & Mitchell, 2014) have defined financial literacy as signifying the knowledge of financial matters, the comprehension of such matters and the ability to apply essential financial knowledge through effective decision making regarding the use and management of money.

According to the SA Department of Trade and Industry (2008), small and micro-enterprises represented 93.1% of all active enterprises in the country in 2007. Government acknowledges the contribution that small and micro-enterprises make

in relieving unemployment and related poverty and has made provision in their National Development Plan 2030 to assist these enterprises (National Planning Commission, 2012). Yet, despite these efforts, small and micro-enterprises still have a low survival rate (Ligthelm, 2008).

The low survival rate may be linked to the reasons for starting the enterprise. Headd (2003:52) asserts that determining the reasons for establishing an enterprise would allow us to draw a link between the owner's start-up intentions and the success of the enterprise. A review of various studies (Watson, 1998; Kolvereid & Isaksen, 2006; Van Gelderen & Jansen, 2006; Benzing & Chu, 2009; Ligthelm, 2008; SBP, 2013; Kvedaraite, 2014) indicated that the most prevalent start-up motivations are: striving toward autonomy and independence; searching for self-fulfilment and growth; following personal passion; pursuing new opportunities; increasing and supplementing income; and taking financial care of family. In some instances, motivations are also fuelled by necessity due to unemployment and retrenchment.

The World Bank, OECD and Department for International Development emphasise prevalent arguments that financial literacy levels across the globe are unacceptably low, even more so in developing countries (Miller *et al.*, 2009). Similarly, the Financial Services Board (Roberts *et al.*, 2014) found that financial literacy levels are low and reported in their financial literacy social attributes survey that South Africans, on average, had an overall financial literacy score of 52%. In the same study, unemployed individuals and females scored lower than the national average.

Lusardi and Mitchell (2014) note that a deficiency in financial literacy is associated with poor financial decision making and investment selections, negative income related to spending decisions, poor borrowing and saving choices, poor financial planning, exceptionally high debt levels, poor attitude towards saving, vulnerability to investment fraud and schemes, and bankruptcy and blacklisting. It is also believed to impede on the development and growth of small and micro-enterprises (Okpara & Wynn 2007; Ligthelm, 2008; Chimucheka & Rungani, 2011; Irwin, 2013; SPB, 2013).

According to findings by Seikei *et al.* (2013), small and micro-enterprises that acquired financial literacy skills through a financial educational programme showed enhanced performance. Lusardi and Mitchell (2011) found that financial literacy needs differed among various population subgroups and recommended that financial education programmes be structured to effectively address the

specific needs of each group. In addition, the FSB (Roberts *et al.*, 2014) stated that financial literacy is not properly understood in developing countries which, in turn, limits the effectiveness of financial literacy programmes. Thus, in order to improve financial literacy in small and micro-enterprises, the specific needs of the owners should be investigated.

Small and micro-enterprises are driving forces of the SA economy. However, they face a range of challenges that impede their development and viability. This study investigated the motivations behind starting small and micro-enterprises in South Africa and identify the current greatest needs of their owners, specifically related to financial literacy. The findings should provide insight to stakeholders and inform their development of interventions to fulfil these needs.

3. RESEARCH METHODOLOGY

3.1 Research approach and sampling

The study was based on a positivism paradigm, and a mixed methods approach (questionnaire and structured interviews) was followed. The study was conducted on small and micro-enterprises in a previously disadvantaged suburb of Potchefstroom, Promosa, in South Africa, using purposive sampling, given the fact that the population size of these enterprises within the suburb was not readily known. Purposive sampling allowed for a full inclusion of the enterprises within the population. The researcher visited all enterprises in the suburb and invited participation. In total, 50 enterprise owners voluntarily participated in the study and the follow-up interviews.

3.2 Instrument

The questionnaire was carefully compiled based on existing literature. It comprised four sections pertaining to socio-economic profile; start-up motivation and initial funding methods; current greatest needs of enterprise owners; and the need for financial literacy. Part of the questionnaire was based on a tried and tested questionnaire on financial literacy of university students developed by Louw (2009). The enterprise owners were interviewed following the completion of the questionnaire and were probed as to whether they understood the questions. The researcher recorded the findings of the interviews.

3.3 Data collection and analysis

A statistical analysis of the questionnaire data was performed by the Statistical Consultation Services of the North-West University (NWU). The analysis included descriptive statistics, as well as reliability and internal consistency tests, which were performed using SPSS software version 23 (IBM, 2016) for statistical analysis of data. Interview data was used to verify the questionnaire data.

3.4 Ethical considerations

Before the distribution of the questionnaire, ethical clearance was obtained by the NWU. Participation in the study was voluntary. The questionnaire did not request any personal information of the participants or their enterprise apart from general demographic information. With regard to the interviews, no respondents were forced to answer any questions that caused them discomfort.

4. RESULTS AND DISCUSSION

4.1 Profile of participants

In total, 50 small and micro-enterprise owners (68% male and 32% female) completed the questionnaire and took part in the follow-up structured interviews. Of these, 76% were sole proprietors and 56% traded from home. A total of 32% held additional employment positions, and 44% had been unemployed before they started their enterprises. Half (50%) of the enterprises have been in trade for five years or less. As mentioned earlier, small and micro-enterprises have a high failure rate within the first five years of trade (Okpara & Wynn, 2007; Ligthelm, 2008). Small and micro-enterprises are indeed job creators, as 74% of the participants employed between zero and three employees, while the remaining 26% employed between four and 15 employees.

4.2 Enterprise start-up

As per Table 1, 46% of the enterprises had been started out of necessity due to unemployment and/or retrenchment. This coincides more or less with the 44% of the enterprise owners who indicated that they had been unemployed prior to starting their enterprises. A total of 24% wanted freedom and independence. South African unemployment rates paint a bleak picture (StatsSA, 2014; 2016). It is therefore no surprise that 46% of the participants were driven by necessity, as they were either unemployed or retrenched at the time of starting their enterprise. This is higher than statistics reported by the Small Business Project (SBP, 2013), namely that one in every five small-and medium-sides enterprises in South Africa

is driven by necessity. It is pleasing to note that 42% of the owners were driven by the opportunities of achieving independent, pursuing their dreams, taking advantage of a gap identified in the market and supplementing their income from formal employment.

Table 1: Motivation behind starting enterprise

Start-up motivation	Percentage
Unemployment and struggling to find work	36%
Freedom and independence	24%
Retrenched and unable to find other work/not wanting to search for other work	10%
Pursuing a dream to do what the individual loves	10%
To supplement income earned from other formal employment	10%
Taking on new opportunity to fill a gap in the market within the community	6%
Retired from previous employment and started enterprise as a pursuance of a dream or to keep busy	4%
Total	100%

As per Table 2, 34% of the owners obtained initial funding solely from their life savings, whereas 14% solely used their retirement money to start their enterprises. A total of 12% obtained funding from friends and family, and only 12% obtained funding solely from a loan from the bank. Overall 58% of the enterprises were initially funded solely through personal funds. As indicated, access to finance is a challenge in the start-up of small and micro-enterprises (Fielden *et al.*, 2000; Mthimkhulu & Aziakpono, 2015).

Table 2: Initial funds to start enterprise

Funding source	Percentage
Solely from savings	34%
Retrenchment package money	14%
From family and friends	12%
Loan from a bank	12%
Savings and loan/money from family and friends	10%
Loan from a bank and savings	6%
Savings and salary	4%
Retrenchment package money and savings	4%
Loan from a bank and friends and family	2%
Retirement funds and savings	2%
Total	100%

Table 3 indicates that 64% of the participants had investments or savings other than their enterprises. This result can be ascribed to the fact that these enterprise owners displayed a high interest in learning how to save and invest money and that they have learned that they need to have some savings for difficult times.

Table 3: Investments and savings outside of enterprise

Question	Yes	No
I have investments/deposits/savings account, other than my enterprise	64%	36%

4.3 Current greatest needs of enterprises

The final item in the questionnaire was an open-ended question that probed for the present greatest need of the owners with regard to their enterprises. Table 4 shows that 64% of the participants needed funds to expand and grow their enterprises. This concurs with the finding that they had mainly used own funds to start the business. It was also found that 12% needed more customers and contracts for their enterprises. Of the owners, 8% indicated that they needed reliable and trained employees.

The greatest need of the owners are funds to expand their business (64%), which is consistent with reports by many researchers (Fielden *et al.*, 2000; Miller *et al.*, 2009; Mthimkhulu & Aziakpono, 2015). The second greatest need (12%), namely more customers and contracts, appeared to be consistent with the economic downturn at the time of the study (SARB, 2015). If left unaddressed, the challenges faced by the small and micro-enterprises could prohibit their development and sustainability (Okpara & Wynn, 2007; Bowen *et al.*, 2009).

The Department of Trade and Industry has an existing range of incentive schemes, loans and grants available for small and micro-enterprises (Entrepreneur Magazine, 2016). The National Credit Regulator (NCR, 2011) reported a poor uptake of these programmes due to a lack of a single source from which enterprises can obtain information. In cases where enterprises did attempt to take up the support offered, the actual implementation of the programmes did not seem to deliver the intended outcome (Mbekeni, 2009). Furthermore, banks are not able to cope with small loans for entrepreneurs, and micro-finance institutions charge high interest rates, which are not affordable (NCR, 2011).

Table 4: Current needs

Need	Percentage
Funds to expand and grow enterprise	64%
More customers or contracts	12%
Reliable and trained employees	8%
None; satisfied with the current state of the enterprise	6%
New ideas, reinvention and diversification of products and services	4%
To learn how to manage it more effectively	2%
Financial support from the government	2%
Not sure, have not given it much thought	2%
Total	100%

4.4 Need for financial literacy

This section of the questionnaire comprised 15 questions in which respondents were asked to rate their responses from “Strongly disagree” (score of 1) to “strongly agree” (score of 5). An internal consistency test was performed on the questions and a Cronbach alpha of .976 was established. A Cronbach alpha of .7 or higher is acceptable (Falissard, 2012).

Table 5: Importance of obtaining knowledge and learning more about financial literacy by concept

Statement	Average score out of 5
How to save money	4.40
How to invest money	4.40
How to budget for daily/weekly/monthly/annual finances of your enterprise	4.36
How to plan for the long-term financial future of your enterprise	4.32
Managing your enterprise	4.32
Ways to reduce the spending within your enterprise	4.32
The basics of the economy (inflation, interest, growth, etc.)	4.28
Managing debt	4.26
Managing enterprise cash flow	4.24
Basic book-keeping (accounting)	4.18
Which financial records (invoices, receipts, bank statements, etc.) to keep and how to keep them	4.18
How to deal with banks or other financial service providers	4.16
How to broaden your knowledge on personal finance (even corporate finance)	4.16
How taxation works	4.04
Insurance and choosing insurance for your enterprise	3.96
Overall average	4.24
Std. Deviation	.82491

There seems to be a great need for becoming more financially knowledgeable and being exposed to financial education and financial advice. This is meaningful bearing in mind that financial literacy levels are said to be low (Miller *et al.*, 2009; Lusardi & Mitchell, 2011). As per Table 5, the highest category of financial literacy needs is to learn more about how to save and invest money (each scored 4.4). This is followed by learning how to budget, with a score of 4.36. The enterprise owners seemed equally interested (4.32) in learning how to plan for the long-term future of their enterprises, how to manage their enterprises and ways to reduce the spending of their enterprises. Even though a high average score is noted, the respondents seemed least interested in learning more about insurance and how taxation works. The question is whether they feel they have sufficient knowledge relating to insurance for their enterprise or whether they are disinterested in enhancing their knowledge in this regard. Small and micro-enterprises are also exposed to business risk which, in turn, is subject to risk management (Boubala, 2010). Taking out insurance is a way of transferring the risk of financial losses to an insurance company (Smit, 2012).

According to the NCR (2011), a lack of managerial skills and financial literacy, poor business plans and insufficient information on products are contributing factors to the inability of small and micro-enterprises to access finance. Higher levels of financial literacy should be of great significance in overcoming the challenges faced by owners. According to Sabana (2014), financially literate enterprise owners are able to identify the most suitable financing and financial management options for their enterprises and manage resources more wisely.

Table 6: Other statistics

Category/Question		N	Mean	Std. Dev.	**Sig.
Gender	Male	34	4.1961	.94180	.600
	Female	16	4.3292	.50857	.520
Are you in an employment position outside of your enterprise?	Yes	16	4.6208	.42144	.023
	No	34	4.0588	.90858	.004
Were you in an employment position immediately before you started your enterprise?	Yes	28	4.2690	.80400	.772
	No	22	4.2000	.86825	.774

***Significance based on t-test*

Further analysis of group statistics as per Table 6 indicates that, based on averages, females have a greater need to obtain knowledge. The ANZ Banking Group (2003) found that a greater percentage of females scored the lowest on financial literacy levels. The results are also supported by the findings of the FSB (Roberts *et al.*, 2014). Furthermore, individuals who hold employment outside of their enterprises or who have been employed prior to starting an enterprise have a greater need to obtain more knowledge. The preceding result raises the question as to whether people who were unemployed before starting their enterprises actually are aware of their lack of knowledge. As mentioned earlier, the FSB (Roberts *et al.*, 2014) found that unemployed South Africans are more likely to be vulnerable to financial illiteracy.

5. RECOMMENDATIONS

With regard to start-up financing, relevant government departments could consider developing an advisory programme for prospective enterprise owners before funding is granted, focusing on the reasons why applications are not accepted. Coaching should be provided to prospective enterprise owners targeting the areas of needs identified in the study, namely how to save and invest money, how to budget, how to prepare long-term plans, how to manage an enterprise,

how to manage debt and cash flow, how to reduce spending, how to do basic book-keeping, which financial records to maintain, how taxation works, the basics of the economy, insight into personal and corporate finance, how to deal with financial institutions, and how to choose the best insurance options for their enterprises.

Government should also consider the implementation of a small and micro-enterprise financial literacy mentorship tier programme. This should include incentives in the form of BEE points, grants and subsidies for medium to big enterprises to take on a mentorship role to prospective small enterprise owners. Upon successful completion of the programme, the small enterprises should then be incentivised to provide similar mentorship to micro-enterprises within their reach.

Opportunity exists for the Unemployment Insurance Fund to implement an entrepreneurship training programme to unemployed individuals wishing to gain entrepreneurial skills. The content could cover the design of business plans, registering of enterprises, budgeting, basic book-keeping, keeping record of cash flow, planning for the future of an enterprise, filing and keeping record of documents, how taxation (including value-added tax) works, how to apply for funds from government and financial institutions, and where to seek assistance.

6. CONCLUSION

Most of the participants in the study started their enterprise out of a need for employment, and most used own funds, which are limited when unemployed. The need for funds to grow enterprises was found to be the greatest among the small and micro-enterprise owners and the greatest constraint they faced agreeing to previous research findings (Fielden *et al.*, 2000; Chimucheka & Rungani, 2011; Mthimkhulu & Aziakpono, 2015). It has been reported that a shortage in skills related to financial literacy is one of the major reasons for the barriers encountered in obtaining finance (NCR, 2011). This was confirmed in this study. Should the need for financial literacy not be addressed, the development and growth of small and micro-enterprises could suffer, which could ultimately affect the growth of the SA economy (European Commission, 2006).

The study contributes to the literature in providing insight into the start-up motivations of small and micro-enterprises, which could be meaningful in the development of interventions to spur on the start of these enterprises. By identifying the current greatest needs of small and micro-enterprise owners, a

better understanding can be obtained in order to propose interventions aimed at growing and developing these enterprises, as well as enhancing their contribution to the economy. Lastly, this study contributes to the overall scarce data on small and micro-enterprises, especially in South Africa.

7. LIMITATIONS AND DIRECTIONS FOR FURTHER RESEARCH

Care should be exercised in interpreting the results, as the study took place in one suburb. Therefore, the results cannot be generalised to the whole of South Africa as each place has unique socio-economic characteristics. Further research opportunities exist for performing a similar mass-scale research to investigate how financial literacy levels affect the performance of small and micro-enterprises, and whether current financial education programmes are achieving the objective of improving the financial literacy of these business owners.

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