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## Critical environmental dynamics: barriers restraining business growth in rural areas of Southern region of KwaZulu-Natal province

### Abstract

The study intends to examine the understanding and awareness of environmental dynamics and their implications of rural SMEs in the southern region of KwaZulu-Natal (KZN) province. The study was conducted within the rural areas of the Southern region of KZN province, using quantitative research methods. The sample for the study consisted of 127 owners/managers of SMEs. The respondents were selected using quota sampling and required to complete a research questionnaire, with an interviewer present to assist. The research instrument consisted of closed-ended questionnaires made up of 5 point Likert scale responses and questionnaires were distributed to five selected areas in rural Southern region of KZN province. The research findings indicate the size of local market is very small to sell their products; poor infrastructure has an impact on their business growth, lack of financial support, as well as tough government regulations, just to mention the few. This study provides both theoretical and practical implications for rural entrepreneurs and policy-makers. The study presents a number of recommendations, including a conceptual growth model for rural SMEs.

**Keywords:** environmental dynamics, rural areas, business growth, SMEs.

**JEL Classification:** Q56, R11, O44.

### Introduction

Literature indicates that the identification of external factors affecting the development of SMEs is a very critical step towards reducing barriers, while, on the other hand, increasing more chances for new opportunities of these enterprises (Govori, 2013). Eight factors which influence the success of SMEs business were examined. Factors identified include resources and finance, customer and market, strategy, products and services, SMEs characteristics, management and know-how, the way of doing business and cooperation (Chithamas, Islam, Keawchana, Yusuf, 2011). A UK and Nigerian comparison study conducted by Ihua (2009) reveals poor management as the utmost critical factor prompting SMEs failure in the UK, while both difficult economic conditions and infrastructure indicated to be important determinants in Nigeria. Enterprises are, furthermore, also exaggerated by various uncontrollable external macroeconomic environment, these include political, economic, social, technological and legal aspects (Grimsholm and Poblete, 2010).

### 1. Literature review

**1.1. Financial constraints as determinants for rural SMEs growth.** Ogubazghi and Muturi (2014) mentioned that lack of access to financial support for SMEs perceived to be common characteristics shared by least developed countries. Fakoti and Asah (2011) hold that the limiting factor for SMEs' survival and growth in South Africa is perceived to be non-availability of debt financing. SME failure to come up with a viable proposal that can persuade potential

finance institutions, difficulty in accessing markets and difficult business regulations and legislation contribute negatively to SMEs' ability to obtain funding. El-said, Al-said and Zaki (2013) highlight that banks recognize SMEs as high risk types of businesses to give financial support. This perception prompted by the characteristics of the owner/managers. Jasra, Khan, Hunjra, Rehman and Azam (2011) emphasize that the most important factor for SMEs to succeed in business is financial resources. However, the challenge of SMEs obtaining access to finance affects their survival and growth (OECD, 2013). This is supported by Zhou and De Wit (2009) who concurs that availability of financial capital is found to be crucial to firm growth. Previous studies also indicate finance as a major constraint for SMEs, with owners/managers finding it very difficult to access the capital needed to grow and expand (Report on Support to SMEs in Developing Countries through Financial Intermediaries, 2011; Ibrahim and Ibrahim, 2015; Kwaning, Nyantakyi and Kyereh, 2015). Access to finance assists all firms to grow and prosper (Bwisa and Ngugi, 2013) and Beck, Kunt and Maksimoic (2006) substantiate this view in finding that businesses which have access to capital are more likely to experience growth and gain more investment opportunities. Furthermore, it has been found that 77% of all small firms which have applied for debt financing got rejected (Kira, 2013). Furthermore, Abdisamad and Wahab (2014) state that the firm's age and size, as well as SMEs that need to be considered for bank loan have significant influencing on the bank decision to approve loan for most SMEs.

**1.2. Institutional impact on SMEs' growth.** According to Schiebold (2011), in Gatukui and Katuse (2014), institutional environment defines, official and

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unofficial rules that are setting to an entrepreneur and which amount to the business operation as constraints. Holmes, Miller, Hitt and Salmador (2013) indicate that established orders within which entrepreneurs and SMEs operate are guided by rules and standards created from economic, political and regulatory situations. Furthermore, Shirry (2008) articulates that constitutions and laws can be written and formalized, as well as tacit and informal constraints. These include norms, conventions and self-imposed codes of conduct. Nevertheless, for some economies, including Africa, achieving the correct policy mix can be challenging. Trademark (2014) indicates that the potential on the continent to develop deeper and wider is well recognized. Trademark (2014) concluded that Africa is moving towards the right direction of economic development shown by rising middle class and more focused innovation, especially among the youth. Gonzalez (2014) stresses that a key to achieving economic development is to ensure a good business environment for SMEs. It has been found that the basic policies, laws and regulations affect SMEs' program and services (Jesselyn, 2012). Hove and Tarisa (2013) find that government strategies and policies for small and micro agribusiness firms can positively improve their growth and survival. Lack of finance has further been found to be cause of many challenges contributing to the failure of SMEs to secure credit for the financing of their operations. These difficulties force owner/managers to use personal savings and family/friend support (Ekwem, 2011). Puffer, McCarthy, Jaeger and Dunlap (2013) emphasize that personal relationship remain crucial for SMEs regarding the institutional and environmental uncertainties that might hinder success development.

**1.3. Politics and law.** According to Wanjiru (2013), intrinsically linked to government's attitude towards allowing business freedom within which it is operating defined as politics. This means that actions that may be taken by government that create potential political risks to business fall into three categories of operational restrictions, exchange controls and employment policies which are insistence on locally shared ownership and particular product requirements.

**1.4. Socio-demographics.** It was found that there is a significant socio-demographic effect in factors that shape the decision to start an own business (Agyemang, Deh and Asuamah, 2013). In a study conducted in India by Venkata, Raman and Ramachandra (2009), the findings highlight that a high level of education does not guarantee entrepreneurial success and senior citizens do not achieve a higher level of entrepreneurial success. The study further indicates that those who were unemployed in their previous occupation, turned out to be the most successful entrepreneurs.

**1.5. Socio-economics.** Socio-economic factors are the main, key aspects influencing entrepreneurial behavior and operation of the business (Khan, 2014). According to Bawuah, Buame and Hinson (2006), growth of the economic suggest the growth and increase in resources and predicts the rate of technical change. The resources in the factors of production comprise land, labor, capital and entrepreneurship. These were identified by many economists as the primary source of economic growth. Schumpeter (1994), in Bawuah, Buame and Hinson (2006) states that entrepreneurship contributes to the growth of every nation. The entrepreneurs are innovators of new ideas and often they are responsible for growth of innovation technical progress. They are not only fostering economic development, but entrepreneurs are also taking risk of innovation, organizing and coordinating the inputs (Bawuah, Buame and Hinson, 2006).

**1.6. Technology.** New technology becomes a main driver for innovation and, hence, successful innovation leads to sustainable business growth (Klongpayabal and Thawesaengskulthai, 2014). Therefore, there is a need for SMEs to acquire new knowledge or new technology, in order to create competitive advantages from innovation. According to Jirayuth, Un Nabi and Dornberger (2013), strategic source of growth and wealth at national and firm levels are determined by technological capabilities of each country. However, Lee, Kelley, Lee and Lee (2012) indicate that, although technology resources provide no direct survival benefits, the suggestion is that the increase of technology resources becomes more crucial if the firms seek international expansion. Klongpayabal and Thawesaengskulthai (2014) believe that the limitation of resources, expertise, time and the lack of capabilities to create in-house technology, force firms, especially SMEs, to focus on selecting or acquiring new technology from external sources.

**1.7. Competitive environment.** According to Ismail, Mokhtar, Ali and Rahman (2014), competition, today, is everywhere in the business environment. The survival of SMEs depends on their ability to take full advantage of the resources available. Wally (1998) states that when company is entering the completion, it is trying to find competitive advantages. However, in terms of business operation and good management, market knowledge, prudent investment and innovation SMEs are not competitive (OSMEP, 2007). It has been noticed that barriers and other restrictions favor these countries competing with less developed countries on owing to globalization and increased trade (Lind, 2009). The unfair competition represents high risk for survival of individual enterprises that includes the informal economy and tax systems (World Bank, 2012).

## 2. Research methodology

**2.1. Design of research.** This study used a quantitative technique, with the primary data to be collected, therefore, only quantitative data were collected. The pre-test was done with the developed questionnaire to check if it will be able to get information required for the survey. This study used a Likert-scale closed-ended questionnaire.

**2.2. Target population of the study.** The target population of this study was 127 SME owner/managers operating in selected rural areas of the South region of KZN.

**2.3. Sampling method.** The sample size for this study is made up of 127 SMEs, selected from general population using quota non-probability sampling technique. Struwig and Stead (2013) argued that non-probability sampling technique should be used in special cases, usually when the population has much in common, like the rural SMEs. In addition, in selecting the respondents within the target population, a census study was applied to collect data for all the 127 SMEs in rural KZN.

**2.4. Measuring instruments.** The study used closed-ended structured questionnaire as a measuring instrument to make the results valid and reliable as per the content and predictability of research. The questionnaire was used to measure the variables across the rural SMEs in KZN. Most of the study variable measures were extracted from the literature review which was the main source of information used to formulate questionnaire for this study. Researcher and research assistants were distributing questionnaire to the respondents to make sure that it will be filled by the right person and respondents will get assistance required at anytime with anything regarding the questionnaire.

## 3. Data collection

The study used closed-ended questionnaire for data collection. Primary data were collected from 127 SMEs operating in rural KZN. This research was quantitative in nature and a questionnaire was used to collect data from SMEs owners/managers in rural KZN. Since the SMEs are spread all over the five selected areas, the researcher travelled to all of the sampled SMEs' places to administer the questionnaires. With the help of research assistant, the questionnaires were left with respondents to be filled for the period of 7 days, then, later were collected for capturing.

## 4. Data analysis

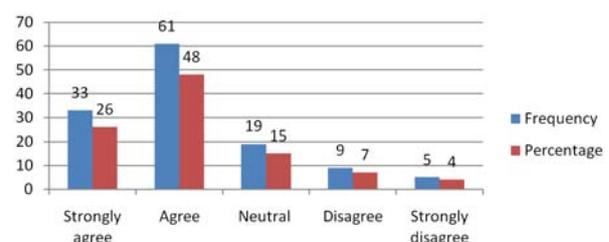
Frequencies were used to determine how often a respondent made a certain response to particular question, and were also used to check the coding of data. The descriptive statistical analysis method was used to determine extent of factors influence on the

survival and growth of rural SMEs in KZN. A chi-square test analysis was also done using the correlation analysis; Spearman rho test was applied to determine the relationship between the variables, Cronbach's coefficient alpha was performed for internal consistency tests to confirm the validity and reliability of the results; and the Mann-Whitney U test was done to identify non-parametric variables.

To establish the significance of individual variables, correlation analysis test was applied at 95% level of confidence. The data analysis was done using the Statistical Package for Social Sciences (SPSS) 23.0 version. The results obtained were presented using tables and graphs, then, analyzed according to the research objectives.

**4.1. Validity, reliability and trustworthiness.** 127 SMEs were selected as the respondents for this study to ensure that the results will be reliable and trustworthy. Further face validity and construct validity were done prior to the interviews for this study conducted in the rural areas of southern region of KwaZulu-Natal province in South Africa, 127 made sample size, and the analysis of the presented in the following section.

**4.2. Level of domestic taxation impact on business growth.** Bouazza, Ardjouman and Abada (2015) state that the SMEs growth is hampered by several factors, including external factors, such as legal and regulatory framework, access to external financing and human resources capacities. The growth SME is affected by internal factors including entrepreneurial characteristics, management capacities, marketing skills, and technological capacities. The main barriers have been "unfair competition" that includes tax systems, the informal economy and public services. These barriers continued with the same intensity throughout the post-war period (World Bank, 2012). The statement that the high level of domestic taxation impacts business growth had 33 (26 percent) and 61 (48 percent) respondents who strongly agreed and agreed, respectively. Only 19 (15 percent) remained neutral, while a small number of respondents, nine (three percent) and five (four percent) disagreed and strongly disagreed, respectively, with the statement.



**Fig. 1. Level of domestic taxation impact on business growth**

A correlation analysis of the results was performed to determine whether the high level of domestic taxation

has an impact on business survival and growth of rural SMEs. The statistical results found to be significant at ( $X^2 = .595$ ;  $df = 1.12604$ ;  $P = .000$ ), which confirms that the statistically significant can be trustworthy.

**4.3. Domestic demand and growth of the business.** Mugobo and Ukpere (2011) identified issues, such as small market, limited success to finance, shortage and high cost of raw materials, lack of technical and business skills, as well as inaccessible and unreliable communication and transport services, as the most severe constraints characterizing South African rural SMEs. Regarding the statement that weak domestic demand affects the growth of the business, 34 (27 percent) and 45 (35 percent) respondents strongly agreed and agreed, respectively. Only 26 (21 percent) remained neutral, while a small number of respondents, 17 (13 percent) and 5 (4 percent) disagreed and disagreed, respectively, with the statement.

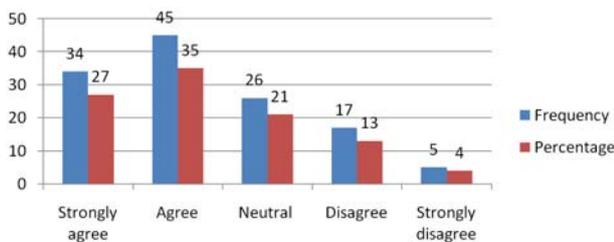


Fig. 2. Domestic demand and growth of the business

A correlation analysis of the results was performed to determine whether weak domestic demand affects the growth and survival of rural SMEs. The statistical results found to be significant at ( $X^2 = .590$ ;  $df = 1.19434$ ;  $P = .000$ ), which confirms that the statistically significant can be trustworthy.

**4.4. Level of skills and business growth.** The low level of labor skills affects the growth of the business management skills which, in turn, plays a role in determining the growth of the small business (Perks and Smith, 2008). With regards to the statement that the low level of skills has an impact on rural SMEs' business growth, 28 (22 percent) strongly agreed and 41 (32 percent) agreed, only 25 (18 percent) remained neutral, while a small number of respondents, 23 (18 percent) disagreed and 10 (8 percent) disagreed with the statement.

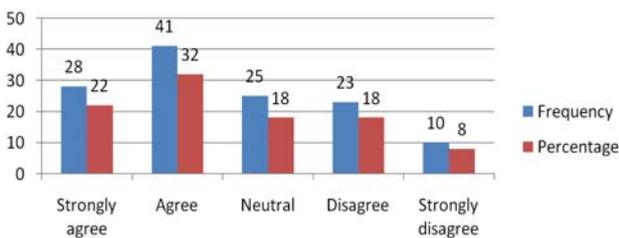


Fig. 3. The level of skills and business growth

**4.5. Equipment quality and business growth.** Yam et al. (2011) in Shin and Sangmoon (2013) indicate that distinct competitive strategies with quality or technological competitiveness. It was found that most respondents, 24 (19 percent) and 47 (37 percent) strongly agreed and agreed, respectively, with the statement that poor quality equipment impacts rural SME business growth. However, 24 (19 percent) of the respondents remained neutral to the statement. The number of respondents who disagreed and strongly disagreed that poor quality equipment impacts rural SME business growth were 21 (17 percent) and 11 (9 percent), respectively.

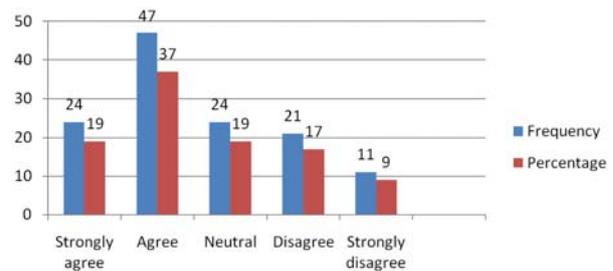


Fig. 4. Equipment quality and business growth

A correlation analysis of the results was performed to determine whether poor quality equipment impacts rural SMEs' business growth. The statistical results found to be significant at ( $X^2 = .764$ ;  $df = 1.15621$ ;  $P = .000$ ), which confirms that the statistically significant can be trustworthy.

**4.6. Institutional barriers to business growth.** Dragnic (2014) reports that both internal and external factors have a significant impact on the SMEs' performance effectiveness, including their sales growth and goals achievement. Karadag (2015, p. 184) adds that the complexity and costs of bureaucratic transactions with launching a new business are also among the major challenges of small and medium sized businesses. These include legislative procedures and reduction of re-tape. Therefore, this study was testing these variables in the rural areas context in KZN. The majority of the respondents, i.e., 19 (15 percent) and 47 (37 percent) strongly agreed and agreed, respectively, that there is some environmental regulation requirements that remain as a challenge for business growth. While 28 (22 percentage) were not sure whether they are affected or not, less than half of the respondents, 24 (19 percent) disagreed and nine (seven percent) strongly disagreed with the statement.

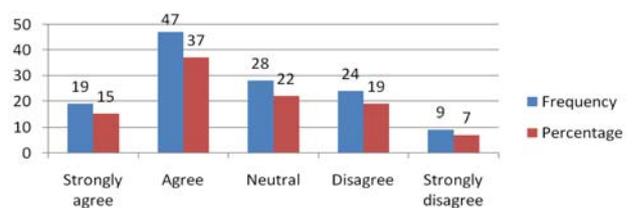
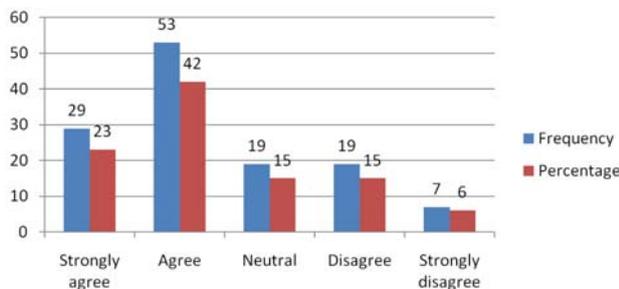


Fig. 5. Environmental regulation requirements as challenges for business growth

A correlation analysis of the results was performed to determine whether environmental regulation requirements remain a challenge for business growth. The statistical results found to be significant at ( $X^2 = .709$ ;  $df = 1.11095$ ;  $P = .000$ ), which confirms that the statistically significant can be trustworthy.

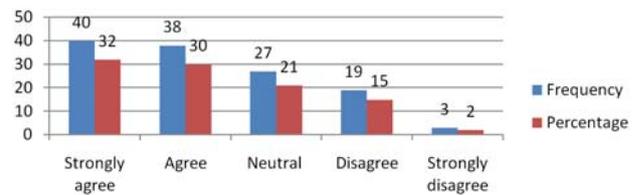
**4.7. Government regulations and requirements affecting business growth.** Alert (2015) reports that SMEs growth is affected by the burdensome regulations. The majority of the respondents, i.e., 29 (23 percent) strongly agreed and 53 (42 percent) agreed with the statement that tough government regulations and requirements to obtain business licences affect business growth. While 19 (15 percent) of the respondents were neutral with regard to the statement very few, 19 (15 percent) disagreed and seven (six percent) strongly disagreed.



**Fig. 6. Government regulations and requirements affecting business growth**

A correlation analysis of the results was performed to determine whether tough government regulations and requirements to obtain business licences affect business growth. The statistical results found to be significant at ( $X^2 = .641$ ;  $df = 1.09435$ ;  $P = .000$ ), which confirms that the statistically significant can be trustworthy.

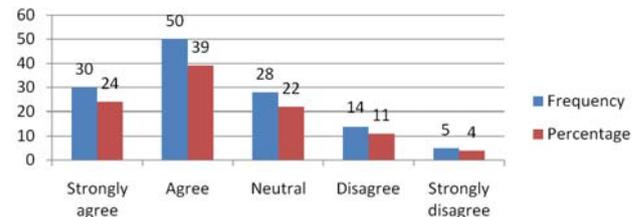
**4.8. Financial barriers contributing to business growth.** According to Gumede and Adams (2012) at the outset, DTI noted that one of the factors that affected SMEs ability to get funding was the fact that many were unable to come up with viable proposals that persuaded the finance institutions of their viability and sustainability, as well as their difficulty in accessing markets, and the hurdles posed by business regulations and legislation. The majority of the respondents, 40 (32 percent) strongly agreed and 38 (30 percent) agreed with the statement that most banks ignore SMEs' right to obtain loans, which has an influence on rural SME business growth. Respondents who indicated neutral numbered 27 (21 percent), with 19 (15 percent) who disagreed and three (two percent) of respondents strongly disagreed disagreeing with the statement.



**Fig. 7. Banks ignoring SMEs request for loans**

A correlation analysis of the results was performed to determine whether their business have been ignored for getting financial assistance by the banks. The statistical results found to be significant at ( $X^2 = .632$ ;  $df = 1.13003$ ;  $P = .000$ ), which confirms that the statistically significant can be trustworthy.

**4.9. Impact of high collateral requirements impact business growth.** Terungwa (2011) states that the need for collateral by financial institutions is also a major obstacle to SME funding, as many of them are unable to come up with the collateral demanded. For example, some SMEs find it difficult to obtain funds, as a result of their lack of security. It was found that the majority of the respondents, 30 (24 percent) strongly agreed and 50 (39 percent) agreed that high collateral requirements impact business growth. There were 28 (22 percent) of the respondents who remained neutral to the statement, while a small number of respondents, 14 (11 percent) disagreed and five (four percent) strongly disagreed.



**Fig. 8. Impact of high collateral requirements impact business growth**

A correlation analysis of the results was performed to determine whether high collateral requirements impact business growth. The question was based on the null hypothesis of uniformity of expected responses to questions. The statistical results found to be significant at ( $X^2 = .712$ ;  $df = 1.07417$ ;  $P = .000$ ), which confirms that the statistically significant can be trustworthy.

**4.10. Social barriers contributing to business growth.** Doern (2015) stipulates that SMEs do not grow due to the notion of barriers including social barriers. Ilegbinosa and Jumbo (2015) stress that the creation, growth, advancement, as well as development of SMEs have provided evidence essential to the growth and development of many countries. The results indicate that 31 (24 percent) strongly agreed and 41 (32 percent) of the respondents agreed with the statement that lack of trust in society, with regard to quality good/services, has an impact on business growth, while 21 (17 percent) were neutral.

A number of the respondents, 26 (21 percent) and eight (six percent) disagreed and strongly disagreed, respectively, with the statement.

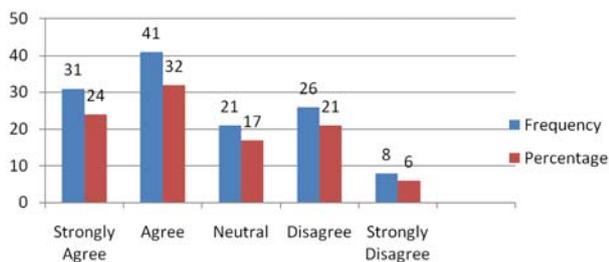


Fig. 9. Trust in society and business growth

To determine whether lack of trust in society, with regard to quality good/services, has an impact on business growth, a correlation analysis of the results was performed. The statistical results found to be significant at ( $X^2 = .626$ ;  $df = 1.44654$ ;  $P = .000$ ), which confirms that the statistically significant can be trustworthy.

**4.11. Support from local communities.** Tran (2015) indicates that intense competition from domestic businesses makes it difficult to have enough consumer markets. The results of the findings show that 42 (33 percent) and 39 (31 percent) of the respondents strongly agreed and agreed, respectively, with the statement that lack of support from business consultancy services affects rural SMEs business growth. While 18 (14 percent) were neutral, a few more of the respondents, 21 (17 percent) and seven (six percent) disagreed and strongly disagreed, respectively, with the statement.

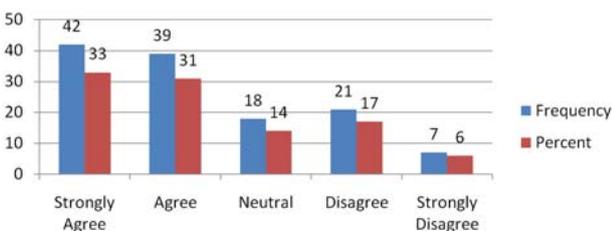


Fig. 10. Support from local communities

A correlation analysis of the results was performed to determine whether lack of support from local communities affects rural SME business growth. The statistical results found to be significant at ( $X^2 = .695$ ;  $df = 1.24411$ ;  $P = .000$ ), which confirms that the statistically significant can be trustworthy.

**5. Limitations**

A structured questionnaire was used for this study, which limited the respondents to providing broad input. The findings are limited by the study’s objectives. The survey also did not include all local municipalities that cover other rural areas. This study used a closed-ended, structured questionnaire, which limited respondents in saying more about their

attitudes, with regard to the constraints that affect survival and growth of their businesses. These include limiting respondents to explain other business networks they use, other motivating factors to start their businesses and other factors influencing their entrepreneurial orientations.

**6. Research implications**

The intention of this study is about making a rural entrepreneurship growth theory contribution to the existing body of knowledge, with regard to growth theory in the rural SME sector, with specific reference to South African SMEs in rural KZN. Based on the reviewed literature and empirical findings of this study, it has been noted that, for better rural economic developmental growth intervention strategies, South Africa and other nations need to obtain a clear understanding of the relevant theories that can help to solve a turbulent and complex environment, leading to many challenges faced by rural communities and business stakeholders in rural areas. This study contributes new information and adds more focus on growth theories in rural entrepreneurship and new growth strategies that are proposed to be implemented. The development of new models and theories in rural entrepreneurship should underline the important components for business growth practices in the rural areas. Rural SMEs’ owners/managers need to be encouraged to implement new, suggested growth theories. This study suggests that a theoretical framework for rural SME growth should adopt the intention of growth theories and growth models.

**Conclusion**

As regards the external environment, for example, institutional environments, which have an effect on the survival and growth of rural SMEs in KZN, it is concluded that environmental regulation requirements remain a challenge for rural SMEs’ business growth, while strict government policies make their expansion difficult, along with public procurement regulations and requirements to obtain a licence. With reference to the socio-cultural environment, it is concluded that a lack of trust among the society, with regard to quality of goods and services has an impact on business growth, as does a lack of support from business associations, with a lack of support from business consultants and communities as other major factors affecting business growth. It has been indicated that most banks ignore SMEs for bank loans, with high collateral requirements. It has been found that institutional environments negatively impact the survival and growth of rural SMEs in KZN. The study hypothesized that environmental regulation requirements and tough government regulations make it difficult for rural SMEs’ expansion. The study also revealed that social environment negatively affects

rural SMEs' survival and growth. This includes a lack of trust among the society, with regard to quality of goods and services.

### Recommendation

This study recommends that taxes regimes and regulations should be reviewed and improved in order to create a suitable business climate for rural SMEs growth and prosperity. South African policy-makers should be encouraged to make improvements on commercial and legal infrastructure that will look at property rights, commercial, accounting and other legal and assessment services and institutions that support or promote SMEs including rural places. It is suggested that South Africa business policy be reviewed so that it can ease access to physical resource-communications, utilities, transportation and land or space at a price that does not discriminate against SMEs including in rural areas. Municipalities and district administrators should run workshops and short courses for local communities in particular for those who want to be entrepreneurs. These courses should be free and should cover financial management and marketing management. Municipalities and local banks should regularly monitor all SME owners/managers who have

obtained financial support from financial agencies. This will assist in correcting any untoward situation at a very early stage. The result should see well-established businesses provide cash/stock to emerging enterprises, in order to kick-start their business, as a strategic partnership. In addition, as part of social responsibility, established businesses together with government will make resources available, from which all small businesses operating in these areas will benefit. SMEs owner/managers should form financial organizations in their areas, where they can contribute an agreed percentage of money from their profits every month over the agreed period. This money can be used to assist all members within the organization with their business needs. They can also form a financial regulating body in their areas. This body will help with any financial related matters including looking for financial donations from NGOs, local and international donors. SMEs should network with other business partners in order to get financial capacity skills and knowledge. SMEs owners/managers must be transparent with regard to financial skills and how they deal with their financial records. This will help them to get loans from the banks or business financial support agencies.

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