Determinants of the Performance of Small and Medium Scale Enterprises (SMEs) in Tanzania. A case of SMEs business oweners in Songea Municipality

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ABSTRACT

Small and Medium Scale Enterprises (SMEs)have been playing a significant role in the socio-economic development of the countries world over. Despite this vital role in contributing to economic growth and job creation, SMEs are facing many challenges. Consequently, SMEs owners earn low incomes making them poor. A study was conducted in Songea Municipality to assess factors that influence SMEs success. Specifically, the study sought to identify the type and characteristics of SMEs in the study area, establish factors that influence SMEs performance and, identify challenges that face SMEs. A total of 113 SMEs business owners randomly drawn from the area constituted a sample for the study.. The study involved a cross-section survey carried out in the area between April to May, 2015. Data were collected from respondents through face-to face interview using semi structured questionnaire. Collected data were analyzed using SPSS software version 20. Findings show that, the factors that influence SMEs performance as measured in terms of sales turnover, included sex of the business owner, with men's business performing better than those of female; education level, number of employees, types of business, entrepreneurship skills, start-up capital, access to market and tax rates. Considering the current state of business informality, there is a need to encourage entrepreneurs to formalize their businesses. Procedures for obtaining business licenses should be simplified along with building the capacity of SMEs owners though training to improve their entrepreneurial skills.

Keywords: Small scale enterprises, performance

1.0 INTRODUCTION

Small and Medium Scale Enterprises (SMEs) are considered as the backbone of the economy world over, due to their significant contribution in socio-economic development in terms of higher growth of employment, output, promotion of exports, and fostering entrepreneurship (Gupta *et al.,* 2013). It has been found that during the 20th century, 60% of the innovations were in the SME sector, but many of them were not successful due to lack of professionalism and inability to collaborate with other enterprises (Rothwell, 1986).

The World Bank (2004) shows no universally accepted single definition of SMEs whereas every country defines SMEs differently depending upon the purpose, objective and use to which is put. In the context of 2003 Tanzania SMEs policy, SMEs are those employing from 5 up to 99 people, mostly family members; or/and employing capital amounting from TZS 5 million up to 800million, and majority of micro enterprises fall under the informal sector (URT, 2003).

SMEs can be easily established since their requirements in terms of capital, technology, management and even utilities are minimal, can be established in rural settings where there is a large number of poor people and thus can add value to the agro-products, while at the same time they are easily dispersed, and serve as a training ground for emerging entrepreneurs (URT, 2003).

It is estimated that SMEs contribute 35% to GDP and 20% of the total labour force (Wangwe, 1999). In recognition of the SMEs, the government formulated Small and Medium Enterprise Development Policy in 2003 to support their development. The policy has brought some improvements in enhancing business environment (URT, 2011). However, despite of SMEs' potential contribution to economic growth and job creation, the enterprises may be facing several challenges that could limit their contribution. Scant information exists on factors influencing performance of SMEs as well as challenges facing the enterprises in the country. Therefore, this study was carried out in Songea Municipality to assess factors that influence SMEs success. Specifically, the study sought to identify the type and characteristics of SMEs in the study area, establish factors that influence SMEs performance and, identify challenges that face SMEs.

2.0 METHODOLOGY

This study was carried out Songea Municipality in five selected Mitaa between April to May, 2015. A study design involved a cross-sectional survey to 113 randomly selected SMEs business owners. Data were collected from respondents using a sem-structure questionnaire. Data were analyzed for both descriptive and

inferential statistical analysis using SPSS software version 20. Descriptive statistical analysis included frequencies, percentages, means, standard deviations. Multiple-linear regression analysis was used to determine factors influencing firm performance.

In determining factors influencing firm performance through Multiple linear regression analyis, a dependent variable was a Firm Turnover per year calculated as Sales Turnover less Tax plus Interest , i.e. Sales Turnover (Total Revenue)= Total Sales - (Tax + Interest). Independent variables included characteristics of a respondents (age, sex, marital status, education level); firm/bussiness characteristics (Type of business, age of business, number of employees, owners equity/start-up capital); access to entrepreneurship skills; business conditions/environment such as perception on amount of tax paid, licence processing period, access to credit and market. Equation 1 indicate econometric model for this analysis and detailed descriptions of variables in the model are shown in Table 1.

$$\text{SMEs PS} = \beta_0 + \beta_1 \text{Age} + \beta_2 \text{Sex} + \beta_3 \text{Gender} + \beta_4 \text{Marit} + \beta_5 \text{Educ} + \beta_6 \text{Year} + \beta_7 \text{Employ} + \beta_8 \text{Typbus} + \beta_9 \text{SMESSkills} + \beta_{10} \text{Credit} + \beta_{11} \text{Capit} + \beta_{12} \text{Markt} + \beta_{13} \text{Bbul} + \beta_{14} \text{Tax} + \varepsilon i$$

………………………………………………………………………….Equation 1

Table 1: Description of variables used in econometric model

Variable	Description of the variable
SMEs PS (Dependent variable-Y)	Sales turnover (Profit) after Tax.
β_0	Constant term of the regression
β_i	Regression Coefficient
Age	Age of respondents (continuous variable)
Sex	Sexr of respondents(1=Male,0=Female: Dummy variable)
Marit	Marital status of entrepreneurs (1=Married and 0=0thers (Single, Widowed and Divorced): Dummy variables.
Educ	Education level of SMEs owner (1=Secondary and above and 0=primary level: Dummy variable.
Year	Age of SMEs(Continuous variable)

Variable	Description of the variable
Employ	Number of employees in SMEs
Typbus	Types of business 1= retail trade and 0=.food processing
SMEs Skills	1=access to entrepreneurship skills and 0 otherwise: Dummy variable
Credit	Access to finance (1 if entrepreneurs access to credit and 0 if otherwise: Dummy variable).
Capit	Owners equity/start- up capital(Continuous variable)
Markt	Access to Markets(1=Access to Market,0=otherwise: Dummy variable)
Bbul	1 if there is bureaucracy in business licensing and 0 if Not (Dummy variable).
Tax	Amount of tax paid (Continuous variable)
εi	Error term (disturbance/stochastic error term).

3.0 RESULTS AND DISCUSSION

3.1 Socio-demographic Characteristics of the Respondents

The SME owner has considerable personal influence over a firm's strategies, tactics and operations to engage in decision-making process across the firm which tends to be quite centralized around the owner. Studies have found that socio-demographic characteristics such as age, sex, marital status and education have an impact on entrepreneurial intention and endeavor (Mazzarol*et al.,* 1999: Kolvereid, 1996; Siegel, 2002; Levy and Powell, 2005). The factors investigated were age, sex, marital status and education level. Table 3 shows the distribution of respondents by demographic and socio-economic characteristics. Results shows that women were the majority of the respondents (54.9%), majority of entrepreneurs were between 31 and 50 years (56.6%); were married couples (59.3%) and had secondary education (52%)

Table 2: Distribution of respondents by Demographic and socio-economic characteristics (n=113)

Category	Frequency	Percent (%)
Sex		
Female	62	54.9
Male	51	45.1
Age		
11-30	42	37.2
31-50	64	56.6
51-70	7	6.2
Marital status		
Married	67	59.3
Single	30	26.5
widow	12	10.6
divorce	4	3.5
Education level		
Primary	18	15.9
Secondary	59	52.2
Diploma	24	21.2
Degree and above	12	10.6

3.2 Firm Characteristics

The distribution of characteristics of business activities in terms of location, types of business and their forms, age of firm, source of capital and income are presented in Tables 3 and 4

Results in Table 3 indicate that most of the firms (34.5%) were located in *Mjinimtaa*. This implies that the location had more customers, social services, lower labor costs, proximity to suppliers, reliable transport and other resources. These findings concur with those of Herzong and Schlottmann (1991) who found that, the change that initiates a location search is the need for new customers and production capacity to meet market demand.

Globally, business activities may be categorized into two types namely wholesale and retail trade which fall under different forms of ownership such as sole proprietorship, partnership, corporation and cooperative form of business (Kivalia, 2003). Types of businesses undertaken by respondents were either food

processing or retail. More than 50% of respondents practiced retail business which might have been caused by shortage of capital and technology for operating other types of businesses. The findings concur with Forfás (1999) who found that, retail trade was made up of large number of small shops offering specialized services than other type of enterprises.

Findings from Table 3 further reveal that majority of enterprises (77%) were registered and operating legally, and 23% of enterprises were informal. These findings are contrary to Bird (2008) who found that most of the businesses in Nairobi were not registered

Table 3: Distribution of Respondents by location, type and age of business (n=113)

Category	Frequency	Percent
Location of the Business		
Bombambili	16	14.2
Mjini	44	38.9
Msamala	20	17.7
Seedfarm	17	15.0
Mjimwema	16	14.2
Types of business		
Retail trade	60	53.1
Food processing	53	46.9
Forms of business		
Informal	26	23.0
Formal	87	77.0
Age of the firm(years)		
1-5	68	60.2
6-10	39	34.5
11-15	4	3.5
16+	2	1.8

Studies have shown amount of start- up capital greatly influences the performance of business enterprise (World Bank, 2007). It can be learnt from Table 4 that about 61% of the respondents started businesses from their own savings or from family members, followed by loans from financial institutions (30.1%). These findings concur with Robinson (1993) that informal sector is the main source of credit.

The sales turnover for respondents shows that 30.9% of businesses had turnover of between TZS 5,000,000-12,000,000while only 2.7% of the respondents had substantial turnover of above TZS 33,000,000. Regarding age of the business, most of the enterprises (60.2%) aged between 1 and 5 years followed by those between 6 to 10 years (34.5 %.) (Table 4).

Table 4: Distribution of Respondents by source of capital, amount of start-up capital and sales turnover (n=113)

Category	Frequency	percent	Mean
Source of capital			
Owner	34	30.1	1.79646
Family	69	61.1	
Relatives	10	8.8	
Start-up capital(TZS "000")			
>5,000	8	7.1	3.19469
5,000-12,000	35	30.9	
12,000-19,000	22	19.5	
19,000-26,000	26	23.0	
26,000-33,000	19	16.8	
<33,000	3	2.7	
Sales turnover(TZS "000")			
5,000-13,000	27	23.9	2.539823
13,000-21,000	32	28.3	
21,000-29,000	26	23.0	
29,000-37,000	22	19.5	
<37,000	6	5.3	
5,000-13,000	27	23.9	
13,000-21,000	32	28.3	
21,000-29,000	26	23.0	

3.3 Factors Influencing SMEs Performance

Recent studies (Indarti and Langenberg, 2005; Thibault *et al*., 2002; Cooper *et al.,* 1994) have identified the key factors influencing SMEs success which comprises the characteristics of the entrepreneurs; the characteristics of the SMEs; and the contextual elements of SME development which are either internal or external factors to the firm. Our framework includes all the above three growth influences and results are presented in Table 5.

Table 5: Regression results for factors that influence SMEs sales turnover

Predictor	B	Std.Error	Sig.
(Constant)	-.3149362	.3800897	0.409
Age(years)	.0031349	.0181928	0.864
Sex 1=Male 0=Female(Dummy)	.1322147	.1132713	0.046 **
Marital Status 1=married 0=Others(Dummy)	-.0787446	.0731615	0.284
Education level 1=Secondary and above 0=Primary	-.1579408	.0772471	0.044**
Age of SMEs(Years experienced) 1=1-5 0=6 and above	-.0949223	.088484	0.286
Number of Employees (continuous variable)	.240399	.0894234	0.008***
Types of business 1=retail trade 0 =food processing	.1256758	.1451958	0.089*
Entrepreneurship skills 1=access to entrepreneurship skills 0=otherwise	-.1036627	.1352634	0.045**
Access to Credit 1=accessibility to credit 0=otherwise	.0806345	.1552876	0.605
Start-up capital (continuous variable)	.7938941	.0450934	0.000***
Access to Market 1=access to market 0=otherwise	.1274903	.1616213	0.032 **
Business registration 1=Bureaucratic 0=otherwise	.0550096	.2092674	0.793
Tax rate	.0633328	.0513395	0.020 **
R			0.889
R square			0.791
Adjusted R square			0.765
F statistics(prob>F)		F statistics=28.82	0.0000

*, **and *** means Significance levels at10%, 5% and1% respectively.
a. Dependent variable: SMEsPS=Sales Turnover (Tshs "000").
b. Predictors :(Constant) and other explanatory variables used in the model.

Table 5 shows that age of the owner has no significant influence on sales turnover of SMEs (coeff=0.003; p=0.864). The findings are contrary to most of the studies (Kristiansen, 2003;Reynolds *et al.,* 2000; and Sinha, 1996) who found a significant correlation between age of the entrepreneur and business success. The relatively mature entrepreneurs were generally likely to be more successful than the younger ones.

As regards to the gender of the respondents, we might expect Tanzanian women to have fewer opportunities to develop relevant business experience, fewer contacts and greater difficulty in assembling resources (Cooper *et al*., 1991). In this study, sex had a significant influence on sales turnover (coeff=0.13; p=0.046) with males having higher sales turnover compared to their female counterparts. The findings concur with Kolvereid (1996) found that males had significantly higher entrepreneurial intentions than females. This implies that males use high entrepreneurial minds and bargaining power in business than females. Another study by Fielden*et al*.(2003) has however, identified influential management issues that have a distinctive gender dimension such as access to support, finance, premises and childcare and have, therefore, conclude that the business owner's sex is not a significant factor in explaining a small firm's success.

Marital status had no significant influence on increase on sales turnover of the business in the study area (coeff=0.08; p=0.284). The finding is inconsistent with Talaia and Mascherpa (2011), who found that, the entrepreneurial team demographics such as marital have a positive relationship in the determination of performance of SMEs.

Education is believed to increase intrinsic motivation and energizer behaviors, and that the more enterprise education an individual receives, the greater the possibility of the SME's success (Clover and Darroch 2005; Guzman, 2004). The findings by Storey (1994) and Bekele and Worku (2008) indicated that education level increases the chance of survival of the business and performance. Results of the regression analysis model revealed that, education level had a significant influence on the performance of SMEs (coeff=-0.16; p=0.044). However, business owners with high levels of education (secondary and above) had lower sales turnover compared to those with primary level education in the study area. This is in agreement with the findings by Barkham*et al.,* (1996) who observed that owners of SMEs who had degrees generally achieved lower rates of growth than those who were less educated.

In terms of age of SMEs, various studies (Storey, 1994; Barkham*et al.,* 1996 and Kristiansen (2003) have found the age of the firm is an important factor influencing the growth of the firm; sometimes younger SMEs growing more rapidly than older enterprises, while others have found that length of time in operation is significantly linked to business success. The findings in this study show no significant influence on sales turnover (coeff=-0.09; p=0.286).

Results from Table 5 further shows that type of business had significant influence on sales turnover in the study area (coeff=-0.13; p=0.089). Retail businesses had

positive influence on sales turnover than food processing businesses. This implies that innovative SMEs are able to respond within the bounds of the knowledge about existing products or services to changes required by the customer within their niche market. This finding is contrary to Barkham, (1996) and Storey *et al.,* (1994) who found that types of business were not significant to their success.

Start-up capital had a significant influence on sales turnover of SMEs (coeff=0.79; p=0.000). This result also implies that, SMEs in which their owners invest large amount of money, they get higher sales turnover compared to those who invest small amount of money. This finding is supported by the study conducted by Olugbenga and Ekiti (2012) on the performance of SMEs who found a positive relationship   between output and initial capital invested.

Determining staffing levels is an important decision in retail operations and performance. Fisher *et al.,* (2006) show that more labor at retail stores is associated with higher customer satisfaction and higher sales. In this study, the number of employees had significant influence on firm's sales turn over (Coeff=0.24; p=0.008).   This implies that, increasing the amount of labor, and thus reducing the workload per employee, reduces the likelihood that employees would make errors or cut corners in performing their tasks and more likely to employees to spend time with customers and therefore increase sales turnover. This finding concurs with Fisher *et al.,* (2006) who found that, more labor at retail stores is associated with higher customer satisfaction and higher sales.

 Access to Entrepreneurship Skills training of SMEs owners had marginally significant negative influence on sales turnover of SMEs (coeff= -0.10; p=0.045).. This implies that, the type of entrepreneurship skills attained by SMEs owners might have had no relevance to the business they conducted. These findings are contrary to Charney and Libecap (2000) who found that, entrepreneurship education of employee increased the sales   of emerging firms' products.

Credits are also important determinants in business performance. Limited access to capital and credit schemes and the constraints of financial systems are said to be the main hindrances to business innovation and success in developing economies (Meier and Pilgrim, 1994; Steel, 1994).The findings from this study, however, show that credit access has no significant influence on SMEs sales turnover (coeff=0.08; p=0.605). This can partly be explained by the fact that the area had various forms of financial intermediation for the SMEs. Whether the entrepreneurs were using them or not, depended on the individualperception of risks involved, informational barriers, and the associated costs (Biekpe, 2004).

Access to markets remains an important factor to SME growth and competitiveness in Tanzania owing to a shrinking domestic market due to globalization. Either, access to market information makes SMEs more aware of opportunities in the market. The increased accessibility to the market helps increase overall aggregate demand for the sector's products and therefore increase markets share of SMEs. It was found that access to markets had a significant influence on sales turnover of SMEs (coeff=0.13; p=0.032). The findings are supported by Kristiansen (2003) who observed that market stability was very significant in determining business success.

Business formality is an important aspect of entrepreneurship (Stiglitz and Weiss, 1981). When businesses are registered, clients and other supporters put more faith in them. Formal enterprises enjoy great incentives to take risk in business activities increases a chance of higher profitability, and business growth compared with informal enterprises (Harhoff, 1998; Mnenwa and Maliti, 2008). The procedures involved in registering for the right licenses are often cumbersome and bureaucratic. However, this study found that, bureaucracy in business licensing had no significant influence on sales turnover of SMEs in the study area (coeff=0.06; p=0.793). The findings contradicts results by Mashenene*et al.,* (2014) and Fjeldstad*et al.*, (2006) who found that bureaucratic procedures in business registration significantly constrained potential growth of SMEs in Tanzania.

Findings from Table 5 also revealed that, tax rates had significant influence on SMEs sales turnover (coeff = 0.06; p=0.020). The amount of tax paid had a positive relationship with the increase on sales turnover of the business. This finding is contrary to that of Mungaya *et al.,(*2012) who indicated that high taxes imposed on SMEs impacted their growth in terms of profits.

3.4 Challenges Facing SMEs in the Study Area

There were various challenges facing business operations in the study area, which are related to policy, legal and regulatory. Small enterprises had inadequate space to operate and physical facilities in which to conduct their business, didn't own land, operated their   activities in areas not planned for, received limited extension services, and suffered from unlawful behavior of Municipal militia who frequently seized their property (Table 6).

Table 6: Distribution of respondents by challenges of business operations (n=113)

Challenges*	Frequency	Percent
Disturbance from Municipal militia	65	57.5
Improper business location	58	51.3
Unreliable power supply	56	49.6
Limited extension services	63	57.8
Inadequate customers	78	69.0
Inadequate loans	48	42.5
Prohibitive rent	97	85.8

*Data were based on multiple responses of respondents.

4.0 CONCLUSION AND RECOMMENDATIONS

SMES business activities are largely formal and retail in nature whose main sources of capital are own savings, family members and relatives. Factors which significantly influence SMEs performance include gender and education level of business owner, number of employees, types of business, receipt of entrepreneurship skills, amount of start-up capital, access to market and tax rates. Among the major limitations of SMEs development are high rent, inadequate customers and harassments by Municipal militia.

There is a need for the Municipal Council to intensify promotion of SMEs through the following key measures:

- Reduce the regulatory burden to enable informal businesses to translate their activities into formal businesses by reviewing the costs and procedures involved. This can be done by establishing one stop centre where all key support activities will take place, and also review the current tax regime so as to institute a friendlier one for the SMEs.

- Intensify support in terms of training and finance; The Songea Municipal Council, Ministry of Industry and Trade, and the funding programmes such as Women Development Fund (WDF) and Youth Development Fund (YDF) should intensify their support to SMEs in terms of loans and entrepreneurship training in order to improve their performance.

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