

RELATIONSHIPS BETWEEN EXTERNAL BUSINESS ENVIRONMENT AND PERFORMANCE OF SMALL AND MEDIUM ENTERPRISES (SMES)

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ABSTRACT

SMEs are regarded as to be very important in any economy. SMEs are important to any economy as they provide employments and contribute to the gross domestic product to all economies. It is therefore important SMEs are given necessary attention by researchers to suggest how they can improve their performance. For this study, external business environment was studied and its influence on SME performance by reviewing critical empirical studies. Therefore, the objective of this study is to harness the findings of these studies and come up with a grand conclusion. Studies were reviewed form different parts of the world to ensure wide coverage. From the review of literature, this study concludes that external business environment enhances SME performance. The study recommends that managers of SMEs should ensure they are always knowledgeable of the activities in their business environment in order to perform effectively.

KEYWORDS: Business environment, SME& Performance

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1. INTRODUCTION

Small and Medium Enterprises (SMEs) are widely acknowledged as the key engine of economic development (SMEDAN, 2013). This sector play a pivotal role to the economic growth and development of any nation. It has been studied that the small and medium enterprises are germane to growth and development of any economy. A central issue dominating policy debates around the world and Africa has been to induce economic growth through the growth of SMEs. SMEs contribution to the Nigerian economy is essential for the accomplishment of the broader development objectives such as poverty relief, spreading of employment opportunities and increasing indigenous ownership of resources in the economy (Chidoko, Makuyana, Matungamire & Bemani, 2011). This has made the government to make efforts at encouraging the growth of small and medium scale enterprises in Nigeria. Various policies, programs and plans have been initiated for the benefits of the small and medium scale enterprises. Small and Medium Scale Enterprises (SMEs) contribute about half of Nigerian GDP and accounts for over 25 percent of employment in the country (SMEDAN, 2013 Small and Medium Enterprises contributes about 48% to Nigeria Gross Domestic Product in nominal terms (SMEDAN, 2013). This typifies the importance of small and medium scale enterprises to the economy of Nigeria. This sector is responsible for most of the advances in new products and process and provides most of the employment opportunities, as a central indicator of the overall operation of an economic system (Enterprise Baseline Survey, 2012).

SMEs is classified based on various criteria, among the common criteria used are the number of employees, gross assets, turnover, and investment level. The most common divisional basis used is employment, with varying levels of upper and lower size limits. Small and Medium Development Agency of Nigeria

(SMEDAN) classification was adopted because it primarily set up to foster the growth and development of SMEs in Nigeria. It classifies SMEs based on employment and assets as those enterprises whose total assets (excluding land and building) are above Five Million Naira but not exceeding Five hundred million Naira with a total workforce of above 10 to 199.

Baloyi (2010) opined that despite the existence of SMEs, their performance has become a thing of concern as SMEs in the country still continue to weaken (not all SMEs are experiencing growth). Studies show that 90% of the business start-ups do not operate beyond the third anniversary due to lack of environmental factors (Douglas, Micah & Tom, 2014). More so, there are other SMEs that have stagnated at the survivalist stage this may be due to poor performance (Bidzakin, 2009). There are various factors that can be attributed to poor failure of SMES in Nigeria. There are inadequate credit facilities for small business owners, harsh economy, unavailability of insurance for small businesses etc. Thus, performance can also be employed to consider how an organization is performing in terms of market share, volume of products, customer's demand, loyalty and investment. (Obiwuru, Okwu, Akpa & Nwankwere, 2011). Consequently, Wang (2010) viewed performance as product accomplishments, results oriented and achievements in an organization. Organization performance can be met if such organization has a favourable business environment.

Business environment is marked by different dynamic features such as global competition, information technology, cultural factors and corporate social responsibility which compel managers to rethink and reshape their approach to various operational responsibilities. The external environment is that system which consists of factors that affect a business enterprise from outside such as socio-cultural factors and technology among others (Alkali & Abu, 2012; Pearce & Robinson, 2007).

Technology has been identified as a major player in making SMEs competitive. But according to European Union (year), a full potential of IT will be harnessed if labour force is equipped with right skills and having access to high-tech infrastructure. However, in the case of Nigeria, some SMEs lack physical telecommunication infrastructure and high speed internet to compete globally (Dzisi, John & Ofori, 2014). Information and communication technology has not thrived well in Nigeria as a result of poor internet infrastructure which can influence the practice of small businesses.

Socio-cultural business environment is integral to industrial and economic well-being of entrepreneurship in general and entrepreneurs in specific terms. This ensures that new innovations come into existence because of interaction that takes place between environmental conditions and entrepreneurial tendencies of the people which is naturally influenced by the socio-cultural business environment (Shivani, Mukherjee & Sharan, 2006). This showcases the importance of the socio-cultural environment to small business enterprises made possible as a result of interaction between environment and the people. Culture is "the software of the mind; a collective mental programming of the people". It is the combination of material and spiritual wealth designed by man through the process of social and historical growth (Hofstede, 1998).

One of the major issues affecting SMEs in Nigeria may be tied to an unconducive environment to enable SMEs flourish (MSME banking study sector report, 2016). Agreeing to a report by Small and Medium Enterprise Development Agency of Nigeria SMEDAN (2013), 95% of SMEs in Nigeria still operate as micro businesses and only around five percent of start-up companies survive and develop to maturity SMEDAN (2008). The business environment in Nigeria is a harsh terrain and the possibility of success is not even guaranteed. This has been met with lots of efforts by the government to ensure ease of doing business in Nigeria. Thus, Omolomo, Odunayo and Tobora (2014) indicated that irrespective of

country, more than 50% of SMEs collapse within their first five years and about 25% go bankrupt or fold up in Nigeria. It is therefore important to study if external business environment affect the performance of SMEs in Nigeria. Therefore, this study will examine the effect of external business environment on SME performance by reviewing critical empirical literature.

LITERATURE REVIEW

2.1 Knowledge Based Theory of the Firm (KBT)

The KBT focuses on knowledge as the most strategically important of the firm's resources (Grant, 1996). Kirsimarja and Aino (n.d) argued that organisations perform differently as a result of the difference in their stock of knowledge and capabilities in using and developing knowledge. This implies that the pace at which an organization will develop will be influence by the quality of knowledge the employees have and deploys in getting things done in the organization. Knowledge should not only be inherent in prople, it must be deployed to get results and influence organizational growth. The authors further opined that organizations exist to create, transfer, and transform knowledge into competitive advantage. Knowledge is related to humans. Individuals are intentional and intelligent agents. In complex situations that cannot be understood by any single individual, Kirsimarja and Aino (n.d) argued that there is a need for integration and coordination of knowledge. Some Knowledge can be leveraged and transferred. This highlights the importance of interpersonal relationship as a skill that can foster performance in any organization. With differences in the knowledge bank of people, having good relationships along the lines of duty can facilitate knowledge transference from one person to the other which will be made applicable in that context.

Technology and the socio-cultural environment are always used by organisations to gather knowledge for the use of organisations. Technology environment is used to gather knowledge which can influence how the organization can be innovative. While, sociocultural environment is used by the organization to gather knowledge, on the culture, behaviour, attitude, and lifestyle of the environment. The KBT emphasises that these knowledge can lead to organizational performance (Grant, 1996).

Conceptualization of Performance

Iskandar, Ahmad and Martua (2014) describe performance in an organization as one of the elements that is assessable through the level of their productivity. This includes the quality, quantity, knowledge or creativity of individual towards the accomplished works that are in accordance with the responsibility during a specified period. Armstrong (2009), also define performance as assessment of an organization through output, product quality, productivity, cost management, safety and health, employees relationship and development. Understanding determinant factors of SMEs performance is considered an important area of focus in Enterprises (Rosli, 2011). However, Anastasia (2008) viewed organizational performance measurement as effectiveness, efficiency, satisfaction and innovation of product. Also according to Apolot (2012), organizational performance metrics in sales growth, customer's satisfaction and profitability were measured in their business. *Concept of External Business Environment*

The external environment of an enterprise is defined as factors that affect the business from outside. These include economic dynamics, government policy, political atmosphere, social and cultural values and technological factors. As revealed in the works of Alkali and Abu (2012); Pearce and Robinson (2007) and Beal (2000). However, Ehlers and Lazenby (2011) pointed out that the external environment represents the variables in the environment that have a direct and indirect influence on the performance of an organization. They are factors which influences the performance of an

organization. Furthermore, Ojeda, Julieta and Simpson (2007) opined that the external environment consists of the macro environment and micro environment, which both affect the performance of SMEs. Macro environment, in this case include the socio-cultural, political, technological, demographic, and economic factors while microenvironment are the factors involved directly with the company and affect the company, consisting of suppliers, customers, government institutions, and competitors. For the purpose of this study, socio cultural factors and technology is used as a measure of external business environment because these are the major factors that may affect business performance. *A look at Technology Environment*

Small Scale Entrepreneurs find it difficult to gain access to technology which limits innovation and SMEs competitiveness (Kayanula & Quartey, 2000). According to McNamara and Watson (2005) technology can be defined as the totality of means such as knowledge, methods, materials, and tools used to achieve practical outcome in other for the enterprise to establish work methods, work patterns, and information structures. It is the tools and the means, but not the primary goal or result to be pursued. Technologies have the potential to improve speed, quality and efficiency.

Socio Cultural Environment

Social system and culture of people are what mix-up to form the Socio-cultural Business Environment and consequently the entrepreneurs become moulded by it (Azim, 2008). All the man-made intangibles that directly or indirectly affect the people's behavior and total way of life are referred to as Socio-cultural business environment (Akpior-Oboro, 2012). People acquire their shared characteristics and pattern of behaviour through socialization processes which involves factors like education, religion and family background. By socialization, the socio-cultural expectation and demands of the society is being learnt and this basically starts from the family. These dimensions happen to be the most prominent in describing the Socio-cultural business environment (Yeboah 2014).

Empirical Review

Ajayi (2016) examined the relationship between external business environment on the performance of SMEs in Osun State, Nigeria. From their study, findings revealed that economic, political, legal, socio-cultural environment, demographic, natural, technological, global and financial environment have influence on SMEs in Nigeria. Adeeko (2017) carried out a study on the impact of external business environment on SME performance in Lagos, Nigeria. 478 SMEs in Lagos were sampled by the study using multi-stage sampling. Results of empirical analysis of the study show that infrastructural facilities, taxation policy and insecurity have effect on SME performance. In the study of Obasan (2014) the impact of external business environment on the survival of small scale businesses in Ogun state, Nigeria was assessed. Logistic regression was used to analyse data collected from respondents. The study concluded that external business environments affects small scale businesses' survival. All these studies showed that the external business environment which is a composite of many factors is a major factor which affects small and medium scale enterprises in Nigeria.

Kowo and Sabitu (2018) carried out their study in Nigeria. The study sought to determine if there is a relationship between external business environment and organizational performance of frozen fish companies in Nigeria.. The authors concluded that variables like technology environment and sociocultural environment influences how well frozen fish companies in Nigeria performs. The study of Ridwan and Ina (2015) examined the problems of performance of organisations in relation to external business environment. The study aim to solve the problem of poor performance of organisations using business environment tools. It was revealed in the study that business performance has implication for

organisation performance. The performance of pharmaceutical industries in Kumasi in relation to external business environment was examined by Akrofi (2016). The result of the study showed there is a significant relationship between external business environment and firm performance.

Productivity of small scale enterprises and environmental factors in Rivers state was examined by Jonah, Aginah and Martins in 2018. The study examined the implications of environmental factors on the productivity of small and medium scale enterprises in some selected SMEs in Port Harcourt, Riverstate. Their empirical analysis showed that environmental factors affect productivity of SMEs. Similarly, Ansir and Edi (2016) assessed how external environment affects firm performance. The purpose of their study was to analyse the effect of external environment on business strategy and firm performance on small and medium enterprises in West Java. Results of the study showed that external business environments affect firm performance. The relationship between organisational environment and its effects on performance was assessed by Almanae (2006). The study concluded that organisational environments affects firm performance.

Bagenda, Sule, Febrian and Sari (2016) studied the influence of business environment on performance of ship-building industry in Indonesia. The study concluded that business environments may improve or decrease organisation performance as the case may be. Udu (2015) also carried out a study on the subject matter. The author concluded that environmental factors affects business operations. The performance of SMEs in Indonesia was assessed by Dananjaya and Kuswanto (2015). Results of the study showed that there were significant positive influence of external factors on the performance. How business environment affects survival of the tourism industry was assessed by Ndife (2014). The study specifically studied the effects of socio-cultural, political and economic environment on the survival and performance of firms in the tourism industry in Nigeria. It was concluded by the study that both political and economic environment significantly predicts the survival and performance of firms in the tourism industry.

Machuki and Aosa (2011) similarly examined the influence of the external environment on the performance of publicly quoted companies in Kenya. 23 companies listed on the Nairobi stock exchange were used as case studies for the study. On the other hand, external environmental factors and organisational performance was assessed by Andre and Rogerio (2006). Brazilian companies were studied by the researchers between 1990 and 2003. The study concluded that external environmental factors predicts significantly organisational performance. Environmental turbulence and its influence on business performance was assessed by Aghadavood and Fakhimi (2014). Results of the analysis show that environmental turbulence significantly predicts firm performance. Performance of firms in the telecommunication industry can be improved by positively engaging external business environments. This statement is according to Sigit and Galih (2016). Sigit and Galih empirically analysed the relationship between external business environments and performance of firms in telecommunication industry in Indonesia. The authors found out that organisational performance is affected by external factors such as community, government and security. The impact of external environment on organisational performance was studied by Nguyen and Nguyen (2013). The authors studied the food industry in Vietnam. Findings were reached by using qualitative research design. It is concluded in their study that external environment affects overall organisational performance.

In the study of Wetende (2014), the relationship between external environmental factors and performance of firms in the export sector in Kenya was assessed. The objective of the study was to establish the external environmental factors affecting the performance of the services export sector in Kenya. 28 professional bodies were used as respondents for the study. The study used economic factors, competitive rivalry, market factors, technological factors and regulatory factors as

independent variables. The study concluded that these factors have great influence on organisational performance. Environmental factors and its influence on small scale businesses performance was examined by Abubakar (2015) studying small scale businesses in Kano and Sokoto states, Nigeria. The study revealed that environmental factors have significant impact on the performance of small scale businesses. In the study of Herri and Syed (n.d.), the influence of external factors on the performance of SMEs in Indonesia was assessed.. Result of the study revealed that external factors contribute to the performance of SMEs.

Quite a number of studies have examined the relationship between environmental factors and organisational performance, just like the study of Nnamani and Ajagu (2014) that studied company's performance in Nigeria in relation to environmental factors.. The study from their analysis found out that environmental factors influences organisational performance. Another was done on SME performance in Mekong, Delta and how local business environments affects their performance by Dut (2015).. It was found out in the study that local business environments influences business performance. Another study was conducted in Cameroon by Nguimkeu (2013). The study examined the impact of business environment on the productivity of retail firms in Cameroon. A structural econometric analysis was used to quantify the impact of these factors over firm performance.

The performance of 20 most capitalised companies in Nigeria in relation to how business environment affects them was examined by Gado (2015) in Nigeria. The study used ordinary least square and simple multiple correlation methods to analyse data. Government expenditure, inflation, exchange rate and interest rate were seen to significantly predict organisational performance.

RESEARCH METHODOLOGY

This study aimed at examining the influence of external business environment on the performance of SMEs. To add, this study sought to assess whether innovation mediates the relationship between external business environment and SME performance. To achieve this, reviewed critical literature from which findings and conclusions was reached. Studies that have been empirically done that are related to this studies were reviewed and their findings were used as conclusions for this study.

DISCUSSION OF FINDINGS

From this study, the external business environment was conceptualized as socio-cultural environment, economic environment and technological environment.

External business environment is the independent variable in this study

The major finding of this study revealed that the trio of political, socio-cultural and economic environment influences and significantly predicts SME performance (Aghadavood & Fakhimi, 2014; Sigit & Galih, 2016; Abubakar, 2015; Nnamani & Ajagu, 2014; Dut, 2015; Nguimkeu, 2013). That is to say organisations must learn to use these external business environments to their advantage.

The environments of business organisations is so important that it must be given necessary attention by SMEs. SMEs may not perform well if they ignore what happens in their environments. This can be said as reviewed studies in this present study acknowledges the importance of external business environment on business performance. External business environments exert significant influence on SMEs performance.

CONCLUSION AND RECOMMENDATIONS

SMEs are seen as important asset to almost all countries especially the developing countries as they ensure growth in the economy and also provide employment (Mead & Liedholm, 1998; Beck, 2005; Li Xue, 2011). The study concludes that external business environment has significant effect on SME performance. The study, therefore, recommends that owners/managers of SMEs should make sure they are well knowledgeable about the business environment in order to perform effectively. In addition, owners/managers should endeavour to know what is happening in their environments in terms of technology, politics and economically. This will help organisations react quickly to new events in their environments and hence improve performance.

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