Factors Affecting the Business Success among MSMEs in Sri Lanka: The Case from Kurunegala District

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ABSTRACT

The Micro, Small and Medium Enterprise (MSME) sector plays a major role in Sri Lankan economy. It immensely contributes to regional development, employment generation and poverty alleviation and hence, this sector has been identified as the backbone of the Sri Lankan economy. In Sri Lanka, despite the fact that some MSMEs have been declining or stagnant, some other have been successful and growing. The focus of this study was to identify the factors affecting the business success among MSMEs in Sri Lanka. Based on the survey of 150 entrepreneurs, the study discloses that marketing, technology, access to capital, government support and infrastructure affect the business success significantly and positively. The results of the ANOVA and t-test revealed that origin of enterprises and the education level significantly affected the business success. It further explained that the educational background did not give applicable skills for running the business. These findings suggest that to be a successful MSME, the owner of the MSME should pay more attention to improve their marketing strategy, to acquire and demonstrate advanced sophisticated technology, and to get capital access. Other interested parties with development of MSMEs such as government agencies, business development services, and business supporting institutes should also be prepared to offer the needed assistance with relate to those aspects.

KEYWORDS: Business success, MSME, Sri Lanka, Success factors

INTRODUCTION

The Micro, Small and Medium Enterprise (MSME) sector has been identified as the backbone of the Sri Lankan economy. It is identified as a driver of change for inclusive economic growth, regional development, employment generation and poverty alleviation. They also play a prominent role in developing appropriate technology, entrepreneurship and business innovations. It covers broad areas of economic activities such as agriculture, mining, manufacturing, construction, and service sectors.

The Micro, Small and Medium Enterprises are defined differently by different countries and multilateral agencies based on different parameters such as number of employees, business turnover, capital investment. Different definitions are also being used by different organizations within the same country to define MSME for different purposes which is a fact that practiced in Sri Lanka.

In the Sri Lankan context, the definition of MSME is based on the annual turnover of the enterprise and under the latest credit line for MSMEs from the World Bank, MSMEs were defined as an enterprise with an annual turnover of less than Rs.350 million. For the purpose of taxation, the 2012 budget proposal defines small industries as an enterprise with an investment of less than Rs.25 million (Somaratne, 2012).

The SME policy framework in Sri Lanka defines MSMEs based on the number of employees and annual turnover (Anon, 2015). According to the survey of non-agricultural economic activities in Sri Lanka conducted by department of Census and Statistics (2013/2014), 91.8% of the establishments in the country are micro enterprises whereas 7% are small, 1% are medium and the balance 0.2% are large enterprises (Anon, 2014).

The MSME sector has enormous potential in generating high level of socio-economic benefits to a developing country with a low level of investment. However, according to the Department of Census and Statistics of Sri Lanka, investment to generate employment or investment per employee is said to be the low. The MSME sector is an ideal platform for the Government to invest and support to reduce the gap between the haves and the have-nots (Weerakkody, 2015).

According to the national policy framework for small medium enterprises, MSME accounts for more than 75% of the total number of enterprises, provides 45% of the employment and contributes to 52% of the Gross Domestic Production (GDP) (Anon, 2015). However, in developed countries the contribution by the SME sector to the GDP and employment is as high as 65% and 70% respectively (Weerakkody, 2015). Hence, these statistics reveal that there is immense potential

to enhance the present level of contribution made by the MSMEs to the economy when compared with the GDP contribution in other countries in small-scale industries, compared to large entities.

From the inception of industrialization of the Sri Lankan economy, micro and small business sector was recognized as an important to be developed. But the progress of this sector is not up to expectation. The empirical evidence shows that 45% of the start-ups entering to the market in Sri Lanka disappear at their first year after establishment (Bandara, 2016).

Running a micro, small and medium business is a difficult and risky matter. The path from starting a business to launching continually is operating with challenges and issues. The Banking Survey of the SME Market in Sri Lanka (2006-2007) of the International Finance Corporation (IFC) listed five principal constraints faced by the MSME Sector. They were difficulties in obtaining bank finance, absence of technical and management skills, marketing constraints, inadequate infrastructure facilities for production, and outdated technologies (Nanayakkara, 2011).

Causes for business failure differ from country to country, region to region, and business to business, but there are common factors such as lack of managerial skills, lack of improper accounting, lack of financial control, lack of internal control systems, lack of business experience *etc*. Apart from these mentioned causes, integrity and business policies as disciplines are critical. The lack of these critical factors can bring misfortune to business. Therefore, business success cannot be expected without practicing integrity and business disciplines (Bandara, 2015).

In Sri Lanka, despite the fact that some MSMEs have been declined or stagnant, some others have been growing and successful. Even though there were lots of studies regarding constraints, barriers for the MSME failure in Sri Lanka, there are a few of studies on business success factors among MSMEs. Therefore, it is an essential need to conduct a research regarding the factors affecting the business success among MSMEs in Sri Lanka.

The aim of this study was to identify the factors affecting the business success among MSMEs in Sri Lanka. It further examined the relationship between the identified factors and the business success.

METHODOLOGY
Theoretical Framework

Storey (1994) identified key components to be important in analyzing the growth of MSMEs; the characteristics of the entrepreneur,

characteristics of the MSME, and the type of the strategy associated with the growth. Instead of the last component, contextual elements of MSME development have been added. The theoretical framework was developed using these adjusted three component as shown in the Figure 1.
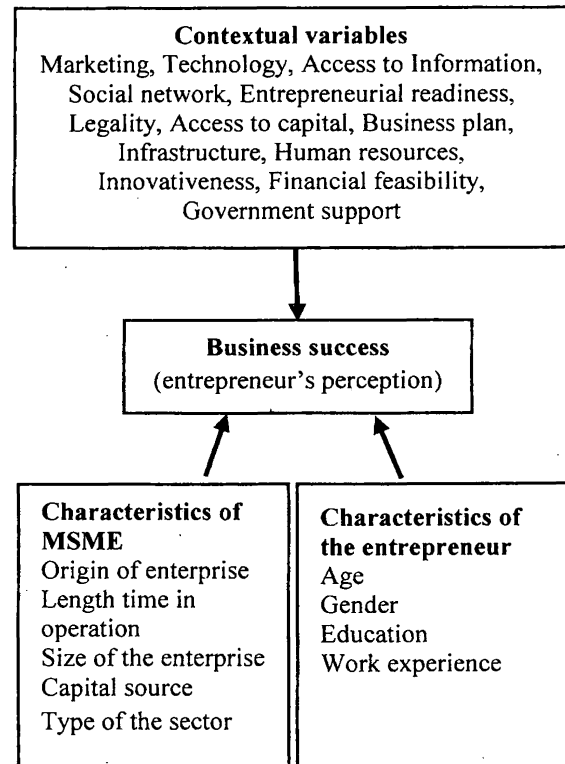

Figure 1. Theoretical framework. *MSME-Micro, Small and Medium Enterprise*

Data Collection

Primary data were collected using pre tested questionnaire from a randomly selected sample of 150 owners of the MSME in the Kurunegala district covering all the divisional secretariats during the period from March to April 2016. Thirty questionnaires could not be considered since the information given were not sufficient for the analysis.

As a basis for developing the questionnaire, focus group discussion and in-depth interviews with business owners, and officers of some business development institutes were used to identify the factors affecting the business success.

It was comprised the demographic information of the respondents and a set of items to measure business success. Five-point Likert scale anchored by strongly disagree and strongly agree were applied to measure perceived success. Under the demographic information, age was categorized according to the survey conducted for non-agricultural economic activities in Sri Lanka by the Department of Census and Statistics.

Next, the respondents were asked to score the importance of thirteen factors considered to take part in determining business success using five-point Likert scale anchored by very unimportant to very important. The respondent were asked to rank the statements on contextual condition related to each success factors faced by the respondents.

Data Analysis

Data were analyzed using both descriptive and inferential statistics with the statistical package SPSS version 16. In addition to descriptive statistics, t-test, ANOVA and regression analysis were employed. Prior to apply the regression analysis, the reliability of the research instrument was examined using factor analysis and value of Cronbach's alpha. The t-test and ANOVA were used as appropriate tests to examine the relationship between characteristics of entrepreneur and MSMEs and business success, while regression analysis was employed to look at the relationship between contextual variables and the business success. Post hoc test using LSD (least significant differences) method was also applied when ANOVA revealed significant difference among group compared.

Responses for contextual variables and the perceived success were obtained through a set of statements rated on five-point Likert scale ranging from strongly disagree to strongly agree. For the analysis, fourteen indices were prepared using these statements. The developed indices are ranging from point two to one. The business success index (BSI) was developed as follows.

$$BSI = \frac{\sum_{k=1}^{K} X_k}{K * X_{max}}$$

Where,

X_k -score given to the statement by the kth respondent

X_{max} – maximum score that could be given by a respondent

K- Total number of statement in a group

Similarly, indices for contextual variables were developed.

RESULTS AND DISCUSSION

Descriptive Statistics

As depicted in the Table 1, the majority of entrepreneurs (69.2%) were male and the female enrolment in the businesses was 30.8%. Most of the entrepreneurs (60.8%) were within the age range of 25-44 years. According to their education, the vast majority of respondents (87.5%) had secondary or tertiary education. However, the business engagement of the respondents who were having higher education was considerably low (8.3%).

These results revealed that the entrepreneurs with secondary or tertiary education tend to do business more than the others. Despite the general education level, 62.5% of the entrepreneurs had business education. A large percentage (62.5%) of entrepreneurs had former work experience prior to running the business which was mostly (92.5%) established by themselves.

Obviously, personals savings (64.2%) and the banks (25%) were the dominant source of capital. Most of the MSMEs (58.3%) were running in agricultural industries. In terms of employee, the higher percentage (80.8%) of establishments in Kurunegala district was micro enterprises.

Table 1. Background information of Micro, Small and Medium Enterprises (MSMEs)

Variable	Percentage (%)
Gender	
Female	30.83
Male	69.17
Education of the entrepreneur	
No school education	1.67
Primary education (grade 1-5)	2.50
Secondary education (grade 6-G.C.E. O/L)	40.83
Tertiary education (G.C.E A/L)	46.67
Higher education (University etc.)	8.33
Age	
18-24 years	1.67
25-44 years	60.83
45years <	37.50
Business education	
Yes	62.5
No	37.5
Previous experience	
Yes	69.17
No	30.83
Sources of capital	
Personal savings	64.17
Joint ventures	2.50
Family investment	8.33
Bank	25
Other	-
Type of the sector	
Agricultural	58.33
Nonagricultural	41.67
Size of the business (in terms of employee)	
Micro (1-4)	80.83
Small (5-24)	13.33
Medium (25-199)	5.83
Origin of enterprise	
Established	92.5
Inherited	7.5

Relationship between demographic information and Business Success

Characteristics of the entrepreneur

The results revealed that age of the entrepreneur had no any significant relationship with business success. Similarly, there was no any significant impact in terms of gender for business success.

Previous employment of the entrepreneur had no significant relationship with business success. Neither previous experience nor business education had significant effect on business success.

The results of the ANOVA test found that there was a relationship (p value= 0.02) between education level and business success at the significant level of 0.05. Surprisingly, entrepreneur with university education was significantly less successful than those with secondary and tertiary education. The appropriate p values were 0.004 and 0.011 respectively. It reveals that education up to secondary or tertiary level enough for running the business to success. Another possible explanation is that the Sri Lankan education system does not cater for entrepreneurial skill development.

Characteristics of MSMEs

The relationship between origin of the enterprise and business success was statistically significant at the level of 0.1 (p value=0.066).

Comparing the mean values of success related to the origin of the enterprise, inherited business were more successful than businesses which were established by themselves. Business which inherited from family were already existed and established in the market. The market for those establishments were developed up to some extent. Therefore, the expenditure on those activities may be minimum with compared to the enterprises which were established by themselves.

There was no difference in business success in terms of size of enterprise, length time in operation and source of capital.

The study examined that whether there was any relationship between business success and type of enterprise as agriculture and non-agriculture. However, there was no significant relationship between business success and type of the enterprise. It further reveals in other way that, whatever the type of enterprise, research findings related to business success were common for all enterprises.

Reliability Analysis

The results of the Cronbach's alpha were depicted in the Table 2. According to Hair *et al.*, (1998), it was acceptable when Cronbach's alpha was higher than 0.7.

Mean ratings of perceived importance of contextual variables

The Table 3 summarizes mean ratings that indicate perceived importance of variables related to business success. Marketing (mean= 4.53) was considered to be most important

factor in running the business, while government support (mean=3.96) was perceived to be less important in business operation.

Table 2. Cronbach's alpha values of contextual variables and perceived success

Variable	No. of Items	Cronbach's alpha
Marketing	4	0.760
Technology	4	0.796
Access to information	5	0.824
Access to capital	3	0.768
Financial literacy	5	0.778
Social network	3	0.691
Legality	2	0.792
Business plan	2	0.888
Entrepreneurial readiness	4	0.867
Government support	3	0.808
Infrastructure facilities	4	0.892
Innovativeness	3	0.826
Human resources	2	0.789
Perceived success	4	0.872

Table 3. Results of the mean ratings of perceived importance of contextual variables

Variable	Mean	Standard Deviation
Government support	3.96	0.99
Business plan	4.06	0.99
Infrastructure facilities	4.09	0.91
Social network	4.12	0.86
Financial literacy	4.16	0.81
Entrepreneurial readiness	4.23	0.73
Legality	4.25	0.66
Human resources	4.26	0.81
innovativeness	4.28	0.83
Access to capital	4.28	0.70
Technology	4.34	0.77
Access to Information	4.36	0.68
Marketing	4.53	0.62

Results of the Multiple Linear Regression Analysis

Using the multiple linear regression analysis, the impact of contextual variables on business success were examined (Table 4). It was revealed that the regression model was significant (probability value =0.000) and the model explains 73% of the variables.

The Table 4 indicates that, marketing, technology and access to capital affect business success significantly and positively at the level of significance of 0.05.

The probability value of the government support and infrastructure were 0.076 and 0.08 at 0.1 significant level and it was found that they affected the business success in positive direction. However, in the mean ratings of perceived importance of contextual variables, it

showed that the government support was less important for success of a business (Table 3).

According to the results, marketing, technology, access to capital, government support and the infrastructure were the determinants of the business success.

However, access to information, social network, legality, business plan, entrepreneurial readiness, human resources, innovativeness, and financial literacy were not found to be statistically significant (Table 4), even though they were depicted as important in the Table 3.

Table 4. Results of the multiple linear regression

Variable	Coefficients	Probability value
Marketing	0.470	0.000*
Technology	0.156	0.018*
Access to capital	0.198	0.003*
Access to information	0.067	0.349
Social network	0.032	0.633
Legality	-0.050	0.378
Entrepreneurial readiness	0.067	0.322
Business plan	-0.096	0.114
Government support	0.116	0.076**
Infrastructure	0.116	0.081**
Human resources	0.063	0.330
Innovativeness	0.015	0.788
Financial literacy	-0.023	0.750

*Note: *Significant at 5% level, ** Significant at 10% level; $Adj.R^2=73\%$;*

CONCLUSIONS

The analysis revealed that origin of the enterprise was significantly related to business success while education also positively significant with business success. However, education up to secondary or tertiary level rather enough for running a business. It further explains that the education system in Sri Lanka does not cater for developing entrepreneurial skills. The success of a business does not depend on the type of the sector as agriculture or non-agriculture. The regression analysis implied that marketing, access to capital, technology, government support and infrastructure were the determinants of the business success of MSMEs.

These findings have to be taken into consideration in programmes designed to develop MSMEs.

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