

## TITLE

### **THE INFLUENCE OF HUMAN INVESTMENT ON THE PERFORMANCE OF SMEs IN THE MANUFACTURING SECTOR OF HARARE, ZIMBABWE**

**(COMPETITIVE PAPER)**

#### **ABSTRACT**

*The purpose of the paper is to investigate the influence of human investment on the performance of Small and Medium Enterprises (SMEs) in the manufacturing sector of Harare, Zimbabwe. The target population for this study was 609 SMEs of which a sample of 241 SME owners or managers participated in the study. Data analysis was done using the Chi-square test to test for association. The results indicated that human resources and managerial skills do affect the performance of SMEs in the manufacturing sector of Harare, Zimbabwe. Based on the results it can be concluded that staff motivation and staff development are the most important human resources management skills for the growth of SMEs in the manufacturing sector of Harare, Zimbabwe.*

**Key words: SMEs; Factors; Performance; Human investment and Manufacturing**

#### **INTRODUCTION**

SMEs are an important sector in both developed and developing countries' economy. This sector plays a significant role in economic growth and development, employment creation and improving the standards of living of many citizens. The high level of unemployment being experienced in many developing countries can be addressed if attention is paid to this important sector of the economy. However the potential of this sector as an economic role player is hindered by many challenges. These challenges range from economic, political, social and technological.

Small and medium sized firms dominate both developed and developing economies in terms of employment and number of companies, yet their full potential remains untapped. These trends need to be changed. The ability of smaller firms to create jobs is clearly a major attraction for governments in the short term. SMEs must be encouraged and supported to flourish. This is important so that economic objectives (economic growth and development, favourable balance of trade and payment and employment) and social objectives (poverty alleviation and improving standards of living) can be realised. Zimbabwe must respond to the needs of SMEs as they form an important component of the economy (Schlogl, 2004:46).

The paper wants to indicate the influence of human investment on the performance of SMEs in the manufacturing sector of Harare, Zimbabwe. The paper will furthermore also provide a focus on the problem statement and the purpose of the study. This will be followed by a focus on the objectives of the study and an overview of the theory relating to the factors affecting SMEs. This is followed by a discussion of the methodology applied to the study and the major findings and managerial implications which form an inherent part of the research.

#### **LITERATURE OVERVIEW**

Smaller enterprises face higher transaction costs than larger enterprises in obtaining credit, insufficient funding has been made available to finance working capital and poor management and accounting practices have hampered the ability of smaller enterprises to raise finances (Abedian, 2001; Peel & Wilson, 1996). Studies by Liedholm, MacPherson & Chuta (1994) and Paul (2001:4) indicate that a large number of small enterprises fail because of non-financial reasons such as a lack of forecasting or planning skills, a lack of skilled human resources and poor management practices. A discussion of the human resources factors affecting performance of SMEs follows in the sections below.

- **Human resource development and its influence on the performance of SMEs**

Cronje *et al.* (2003:98) stipulates that one of the primary causes of failure in a small enterprise is poor management. This is also echoed by Longenecker *et al.* (2006:385)

who argue that SMEs are more vulnerable to managerial weakness as a result of a lack of professional staff due to financial constraints. The managerial inadequacies in SMEs can be attributed to low levels of formal education among the majority of owners and/or managers. A major challenge for the SME sector worldwide is therefore the development of the managerial skills of the owners or managers of SMEs to ensure their long term success (Kyambalesa, 1994:174; Murphy, 1996:14 and Cronje, *et al.*, 2003:98).

- **The development of management skills in the SME sector**

If the desired outcomes of a venture are to be achieved in SMEs, certain tasks need to be performed by owners and/or managers. However, the extent to which the managers of SMEs perform these tasks is relatively different in comparison to big businesses because of a shortage of technical and managerial skills (Kyambalesa, 1994:174). Research findings by Sawas & Feng (2005), Kakati (2003) and Sonfield & Lussier (1997) have indicated that a lack of managerial competence result in the failure of SMEs worldwide.

The literature above clearly highlights the challenges being faced by SMEs in general. The paper seeks to explore the effect of human investment on the performance of SMEs in the manufacturing sector of Harare, Zimbabwe.

#### **PROBLEM STATEMENT**

Zimbabwe is currently experiencing economic hardships which are characterised by a high inflation rate (516 Quintillion% as per December 2008) (Burgess, 2008). High interest rates make the borrowing of capital expensive, resulting in low levels of investment and a weaker currency which makes the importation of raw materials difficult and expensive at the same time. Access to finance becomes a challenge to SMEs in Zimbabwe. Due to these prevailing economic conditions most of the skilled personnel have left the country and this has a negative impact on the performance of SMEs as they now suffer from insufficient management skills. It is against this background that the research seeks to investigate whether human resources and management factors affect the performance of SMEs in the manufacturing sector of Harare, Zimbabwe.

#### **OBJECTIVES OF THE PAPER**

The primary objective of the paper is to determine the influence of human investment on the performance of SMEs in the manufacturing sector of Harare, Zimbabwe.

The secondary objectives are:

- To establish whether a lack of skilled human resources contributes to the poor performance of SMEs as perceived by the manufacturing sector of Harare, Zimbabwe;
- To establish whether poor management skills such as human resources management, financial management, general management, production management and marketing management result in the poor performance of SMEs as perceived by the manufacturing sector of Harare, Zimbabwe; and
- To identify other factors which influence the performance of SMEs in the manufacturing sector of Harare, Zimbabwe.

#### **RESEARCH HYPOTHESES**

- H<sub>0(1)</sub>: A lack of skilled human resources does not contribute to the poor performance of SMEs in the manufacturing sector of Harare, Zimbabwe.
- H<sub>1</sub>: A lack of skilled human resources does contribute to the poor performance of SMEs in the manufacturing sector of Harare, Zimbabwe.
- H<sub>0(2)</sub>: Poor management skills such as human resources management, financial management, general management, production management and marketing management does not result in the poor performance of SMEs in the manufacturing sector of Harare, Zimbabwe.
- H<sub>2</sub>: Poor management skills such as human resources management, financial management, general management, production management and marketing management does result in the poor performance of SMEs in the manufacturing sector of Harare, Zimbabwe.

## **RESEARCH DESIGN**

This study made use of a quantitative research approach and applied a descriptive research focus since it primarily depended on the interviewing of respondents (the managers or owners of SME's in the manufacturing sector of Harare, Zimbabwe). The study was also cross sectional since the respondents were only interviewed once.

### **Population and sample**

The population of the study was 609 SMEs in the manufacturing sector of Harare, Zimbabwe. A list of SMEs was obtained from the Ministry of SME Development in Zimbabwe. A sample of 241 SMEs was used for the study. A computerised random number generator was used to select the 241 respondents out of the total population of 609. The researcher applied the simple random sampling technique for the study because each element of the population had an equal chance of being selected.

### **Measuring instrument**

The measuring instrument used was a structured questionnaire which included some adapted items from previously tested measuring instruments and items, for example the instruments of Fatoki and Chiliya used in similar studies on SMEs in South Africa. In addition, structured interviews were conducted with the owners or managers of SMEs in the manufacturing sector of Harare, Zimbabwe.

Closed-ended and Open ended questions were used in the questionnaire. The questionnaire also consisted of six sections. Section A consisted of seven questions to gather biographical data on the SMEs and the owners or managers of SMEs. Section B consisted of nine questions to gather information on the requirements of the Ministry of Small and Medium Enterprise Development. Section C consisted of ten questions to obtain information on factors affecting the performance of SMEs. Section D consisted of

five questions focusing on managerial aspects. Section E consisted of four questions to establish the required skills for SME development. Finally, section F consisted of eight questions to gather data on SME support by the Zimbabwean government and other institutions.

### **Data analysis**

Ordinal Multinomial Logit Models were used to test for the effects of explanatory variables on those responses that had more than two categories. For the binary responses Ordinary Logit Models were used. To assess or evaluate the association among the response factors, Loglinear Modeling was used. Chi-square was used to test for association. These statistical procedures were used as follow-up analyses to the graphical analysis (bar charts and pie charts. All tests were carried out at a five percent (5%) significant level. These statistical tools were used since the data contained some categorical variables where responses are classified. Furthermore the sections in the questionnaire were divided into an explanatory section, namely sections A and B and response sections, that is, sections C to F.

## **RESULTS**

The results of the study are discussed in the three sections below. The focus is on human resources skills required for SME development, management skills influencing the performance of SMEs and factors influencing the development of SMEs.

### **❖ Human resource skills required for SME development as perceived by the manufacturing sector of Harare, Zimbabwe**

Seventy six percent (76%) of the responses from the respondents shows that staff motivation and performance appraisal is important to ensure the future success and growth of their businesses. Sixty six percent (66%) stipulated that staff recognition, staff development and staff promotion is important for the future success of their businesses. An analysis of this result highlights motivation and staff development as important human resources management skills required for the growth of SMEs in the manufacturing sector of Harare, Zimbabwe. Human resources are an important

component of any organisation and it is therefore important for SMEs in the manufacturing sector of Harare, Zimbabwe to ensure that they have all the necessary human resources management skills. This is due to the fact that the performance of an organisation highly depends on motivated staff.

A study by Ferlig, Prasniker & Jordan (2004) indicate that a link indeed exists in that human resource efforts in SMEs contribute to the competitive advantage of companies. This therefore implies that SMEs in the manufacturing sector of Harare, Zimbabwe must ensure that they have adequate human resources management policies to enhance the performance of their employees.

❖ **Management skills influencing the performance of SMEs in the manufacturing sector of Harare, Zimbabwe.**

Forty seven percent (47%) of the respondents highlighted the importance of skilled personnel and planning skills in their business. Fifty three percent (53%) of the respondents indicated that financial management skills are important in the performance of their business, whilst sixty two percent (62%) of the respondents view customer care as the most important function on the performance of their business. Forty seven percent (47%) of the respondents concluded that marketing knowledge and skills are important for the performance of their business. Forty five percent (45%) of the respondents regarded knowledge of human resources as an important managerial function which has a positive effect on the performance of their business. A closer analysis on the responses of the respondents shows that customer care, marketing knowledge and skills, planning skills and financial management skills are the most essential management functions that affect the performance of SMEs.

A stronger focus on the four areas indicated above will empower the owners and/or managers of SMEs in the manufacturing sector of Harare, Zimbabwe to strengthen the success of their businesses in the future. This implies that more research needs to be done amongst the consumers of SMEs to determine their needs and wants on a regular basis. This would require training in the field of consumer research and questionnaire design to

empower the owners and/or managers of SMEs to apply a more structured approach to marketing research. There is also a clear need for increased training opportunities in the fields of marketing and financial management to be provided to the owners of SMEs. Furthermore, there is also a need for SME owners to be taking their employees for refresher courses on customer care to enhance customer loyalty which will lead to the success of SMEs. The emphasis should also be on enhancing planning skills in SMEs since it is a key area for the success of SMEs in the manufacturing sector of Harare, Zimbabwe.

The outcome of the findings is in agreement with a study carried out in Botswana which focused on small business critical success/ failure factors in developing economies. The study showed that marketing activities such as product marketing, market research and demand forecasting were perceived by the respondents to have greater impact on their business than any other factor. Investment analysis and working capital management related problems were also rated by the respondents as having a significant impact on small business performance. Identifying the right sources of capital for the right purpose is a challenge for SMEs. Proper management of fixed capital may lead to proper implementation of strategic plans while proper management of working capital minimizes short-term obstacles to achieve competitive advantages in the marketplace. Customer relationship was also rated high by the respondents in its impact on the performance of SMEs. Service and merchandising firms spent much time and resources to retain their customers. Customer loyalty and retention have been the main strategy for these firms to achieve competitiveness (Temtime & Pansiri, 2004:8). All these aspects call for adequate management skills which validates the importance of human investment.

❖ **Factors influencing the development of SMEs in the manufacturing sector of Harare, Zimbabwe**

Sixty nine percent (69%) of the respondents felt that economic factors such as inflation, interest rate, tax rates and currency fluctuations have a direct influence on the performance of their businesses. Currency is the exchange value of the Zimbabwean

dollar against major currency such as the South African Rand, the US Dollar and the British Pound. Fifty five percent (55%) of the respondents indicated that the investment level in Zimbabwe has a direct impact or influence on the performance of their businesses. Investment is both in their businesses and in the economy at large as SMEs depends on larger businesses for inputs (e.g. raw materials) and services (e.g. accounting, marketing and advertising). Sixty eight percent (68%) respondents indicated that fuel shortages, power cuts and exchange rate have a direct influence on the performance of SMEs as most of their operating activities require fuel, energy and foreign currency. The Zimbabwean dollar is weaker versus other currencies. This result indicates that economic factors have a direct influence on the performance of SMEs.

This result is consistent with the findings of a study carried out in Botswana which concluded that economic factors were important for the positive performance of SMEs. According to Temtime & Pansiri (2004:5) economic factors refer to the influence of inflation, recession, changes in the interest rate and exchange rates, market size, the spending power of customers, the availability of business premises in the community and the intensity of competition in the market. The respondents evaluated these items and perceived them to be critical success factors for SMEs.

Sixty nine percent (69%) of the respondents are affected by the shortage of finance. This result indicates that the shortage of finance is one of the major challenges being faced by SMEs in the manufacturing sector of Harare Zimbabwe. This is in agreement with an empirical study by Ligthelm and Cant (2003:5) which concluded that the limited access to financial resources available to smaller enterprises compared to larger organisations have negative consequences for their growth and development.

Sixty three percent (63%) view the cost of finance to have a direct influence on the performance of their businesses as it will be expensive for SMEs to borrow money from banks and lending institutions. This result is agreement with previous studies on SMEs. The role of finance has been viewed as a critical element for the development of small and medium-sized enterprises. Previous studies by Ligthelm and Cant (2003:5) have

highlighted the limited access to financial resources available to smaller enterprises compared to larger organisations and the consequences for their growth and development. Typically, smaller enterprises face higher transaction costs than larger enterprises in obtaining credit, insufficient funding has been made available to finance working capital and poor management and accounting practices have hampered the ability of smaller enterprises to raise finances (Abedian, 2001; Peel & Wilson, 1996). Seventy six percent (76%) of the respondents view the prevailing transaction costs as very high which in turn have a negative impact on the performance of their businesses. This result is consistent with the findings in Namibia where it was concluded that SMEs have limited access to low cost finance (borrowing is mainly through commercial banks via high cost overdrafts) (NEPRU, 1999:5). This limited access to low cost finance results in SMEs incurring high transaction costs which reduce potential rewards.

Transaction costs can be described as the costs incurred by commercial banks in evaluating the loan applications of small firms. Transaction costs also include the costs of monitoring the performance of small firms by the commercial banks once the loans have been granted. Obtaining reliable information on the creditworthiness of small firms is difficult and costly. The reason being that little, if any public information exists about their performance. Small firms are not quoted on the stock exchanges or rated by credit rating agencies. Furthermore, small firms often lack audited financial statements. Commercial banks, therefore, incur costs in obtaining reliable information about the performance of small firms. In addition, lenders usually incur costs in monitoring the credit arrangements with small firms. These costs are passed by the banks to the small firms in the form of transaction costs. The more carefully a loan appraisal is done, the higher the transaction cost (Nieuwenheizen & Kroon, 2003:129). Eriotis, Franguoli & Neokosmides (2002:89) also indicated that relatively high transaction costs, especially for smaller firms when issuing long-term financial instruments, is a major detriment to the use of debt by small firms. Therefore, when the high costs of debt are removed from the interest deductibility of debt, the tax advantage of debt becomes very small and insignificant. Information asymmetries associated with lending to small scale borrowers have restricted the flow of finance to smaller enterprises.

Fifty four percent (54%) felt that access to land has a direct influence on the performance of their businesses as SMEs do not have enough space for expansion purposes. Entrepreneurial skills have a direct influence on the performance of SMEs according to sixty six percent (66%) of the respondents as they lack the necessary skills to manage their enterprises in order to survive and grow. Forty four percent (44%) of the respondents indicated that general management skills have a direct influence on the performance of their businesses as they do not have enough skills to manage their businesses. Sixty three percent (63%) of the respondents concurred to the fact that government regulations have a direct influence on the performance of their businesses as the Zimbabwean government is the responsible authority which formulates the regulations on how businesses operate in the country.

Fatoki (2006:23) noted that although small businesses do make unique contributions to employment and economic development, there are specific challenges that affect them more directly than the influence of these challenges on large corporations. The major constraints facing small businesses in South Africa, are inadequate financing, access to markets, acquisition of skills and managerial expertise, inadequate access to appropriate resources and technology, the quality of infrastructures, especially in the rural areas, and bureaucratic government regulations. These challenges can result in limited profitability and the decision to voluntarily close the business due to financial failure.

Sixty nine percent (69%) of the respondents indicated that a business plan is important for the success of their business ventures. Sixty three percent (63%) of the respondents felt that the availability of business opportunities is also important for the success of their business ventures. Sixty eight percent (68%) alluded to the fact that an entrepreneurial team is essential for the success of their business ventures. Fifty eight percent (58%) concluded that training in business skills is important for the success of their business ventures. A closer analysis of the result leads to the conclusion that a business plan and an entrepreneurial team are the two most important aspects for the success of any business venture. Taking this into consideration, SMEs in the manufacturing sector of

Zimbabwe should therefore ensure that they equip their employees with the necessary business plan skills. A business plan enables SMEs to secure financing. An entrepreneurial team is necessary to implement the businesses' objectives as outlined in the business plan.

This result is consistent with the work of Hannan & Atherton (1997:4) who noted that for those businesses that developed and used a business plan, ninety three percent (93%) indicated that the plan helped in guiding company operations and seventy two percent (72%) responded that it assisted in attracting major customers. A business plan is the key to long term success for new and old businesses. The business plan is a framework which a business must operate within. It will ultimately determine whether the business succeeds or fails. For management or entrepreneurs seeking external support, the plan is the most important sales document that they are ever likely to produce. It acts as the key to raising finance. Preparation of a comprehensive plan will not guarantee success in raising funds or mobilising support, but having no plan at all will more likely result in failure (Cox, 2007:1-2). According to Renee (2007:1) a sound business plan may make a difference between a business that succeeds and a business that fails. Approximately 90% of small businesses fail before two years, according to the Small Business Association. And even after that two year mark has been passed, there are no guarantees. This is mainly due to a lack of business plan knowledge and the absence of a business plan (Cox, 2007:1-2; Renee, 2007:1).

#### ❖ Testing of hypotheses

##### *Research Hypothesis 1*

*A lack of skilled human resources does result in the poor performance of SMEs in the manufacturing sector of Harare, Zimbabwe.*

The statistical programmes ANOVA (Analysis of variance) as well as a regression analysis were employed to statistically test the significance of this assertion. The results indicated that skilled human resources do play a significant role in determining the

performance of SMEs. It was observed that variables such as the business plan ( $p=0.039$ ), and business opportunity ( $p=0.034$ ) play a significant role in the performance of SMEs in the manufacturing sector of Harare, Zimbabwe. Hence, this statistically implies that a lack of skilled human resources was causing the poor performance of the SMEs.

*Statistically, the null hypothesis which states that a lack of skilled human resources does not result in the poor performance of SMEs in the manufacturing sector of Harare, Zimbabwe is rejected and the hypothesis is accepted.*

#### *Research Hypothesis 2*

*Poor management skills such as human resources, financial, general, production and marketing does result in the poor performance of SMEs in the manufacturing sector of Harare, Zimbabwe.*

The statistical programmes ANOVA (Analysis of variance) as well as a regression analysis were employed to statistically test the significance of this assertion. The results showed that management skills do play a significant role in determining profitability. It was observed that management skills such as the advertising and promotion of products ( $p=0.016$ ), and manager's informational role ( $p=0.030$ ) play a significant role in the performance of SMEs in the manufacturing sector of Harare, Zimbabwe.

*The null hypothesis that states that poor management skills such as human resources management, financial management, general management, production management and marketing management does not result in the poor performance of SMEs in the manufacturing sector of Harare, Zimbabwe is rejected, but the hypothesis is accepted.*

#### **MANAGERIAL IMPLICATIONS**

The managerial implications are discussed in the two sections below. These implications are intended to help SME managers/owners in the manufacturing sector of Harare,

Zimbabwe and all others in this sector in the developing world. It focuses on factors influencing the development of SMEs and required skills for SME development.

#### **❖ Factors influencing the development of SMEs in the manufacturing sector of Harare, Zimbabwe**

SME owners in the manufacturing sector of Harare, Zimbabwe and the Zimbabwean government must form more direct partnerships to improve the skill levels in the sector. This can be done through increased funding for SME staff training by the government. Currently the Zimbabwean government does provide training through business incubators to increase the sustainability and growth of SMEs in Zimbabwe. However, such training is only mainly provided in the larger metropolitan areas such as Harare and Bulawayo and need to be extended to other cities, and eventually the rural areas of Zimbabwe. The Zimbabwean government, through the Ministry of Education, must also make use of Vocational Training Colleges and Polytechnic Colleges to develop programmes which could assist SMEs in developing their skills. They can initially start in the larger Metropolitan areas and then expand it to the rural areas and small towns. Furthermore there is need to establish SME consulting and training centres in certain areas or provinces to assist SMEs with their challenges. The number of centres will be determined by the number of SMEs in a specific city or rural area. SMEs can also be encouraged to make use of the Entrepreneurial Development Programme (EDP) which is a programme aimed at improving the skills levels in the SME sector. The EDP involves training of potential entrepreneurs in entrepreneurial skills. EDP could assist SMEs by lessening the challenge of skills shortages.

#### **❖ Required skills for SME development in the manufacturing sector of Harare, Zimbabwe**

On financial management skills SMEs must send their employees on training in bookkeeping and financial statement preparation. These are skills which must be possessed by SMEs to ensure its continued survival and growth. In addition, SMEs must limit debts in their enterprises. They can achieve this by ensuring that they purchase their inputs on a cash basis so that they can obtain discounts which will help them in

minimising the cost of production. This will be passed to customers in the form of lower prices and will improve the competitiveness of SMEs.

On marketing management skills SMEs must regularly send their employees on customer care refresher courses which involve customer management and complaints handling. In order to benefit from advertising and promotion, SMEs must form cooperatives for advertising whereby they run joint advertising initiatives to minimise costs. SMEs must also make use of special promotions in order to lure customers. SMEs must also carry out market research in order for them to have knowledge of the market. On selling their products SMEs must use persuasive selling whereby they encourage people to buy their products and outlining the benefits clearly of the products to the customers.

On human resources management skills the SMEs must have staff development programmes in place. These development programmes will include training on different skills required for the operations of SMEs. SMEs must take note of the employees who perform exceptionally well and have promotional measures in place. The promotional measures must clearly outline how the highly performing employees will be promoted. Since motivation is an important aspect in the performance of SMEs, entrepreneurs must ensure that they keep their staff motivated. This can be done through appraising employees who perform highly and creating a conducive working environment. This environment can be created by having flexible working hours, involving employees in decision making and having clear remuneration measures.

Therefore the researcher recommends that the owners of SMEs in the manufacturing sector of Harare, Zimbabwe be trained more in these areas. Furthermore, the Zimbabwean government needs to subsidise such training more comprehensively and also need to increase its funding to post school institutions such as technical colleges and universities to develop programmes which could educate the owners/managers of SMEs in these fields. Through these increased initiatives, the Zimbabwean government will further contribute to increasing the success rate of SMEs in the manufacturing sector of Harare, Zimbabwe.

## CONCLUSION

The results of the data gathered from the questionnaires have assisted the researcher to reach certain conclusions on the formulated hypotheses. Through these results, the researcher discovered that SMEs in the manufacturing sector still suffer from inadequate managerial skills. This result supports both the hypothesis that poor management skills such as human resources management, financial management, general management, production management and marketing management result in the poor performance of SMEs in the manufacturing sector of Harare, Zimbabwe. In addition, a lack of skilled human resources also contributes to the poor performance of SMEs in the manufacturing sector of Harare, Zimbabwe. In addition SMEs must ensure that they are well acquainted with all the managerial functions that have an effect on the performance of their businesses. These managerial functions are skilled personnel, financial management skills, planning skills, customer care, marketing knowledge and skills and knowledge of human resources practices. This can be done through training programmes, funded by the Zimbabwean government, and sending their employees on refresher courses regularly.

The above discussions clearly brought out the importance of human capital investment for the survival, growth and development of SMEs in the manufacturing sector of Harare, Zimbabwe. An ability to address this will result in an increased performance of SMEs which will ultimately lead to the achievement of both economic and social objectives of SMEs.

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