

# CHALLENGES AFFECTING SME'S GROWTH IN GHANA

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**Abstract:** The contribution and development of the private sector to the sustainable growth of any economy cannot be underestimated. In both developed and developing economies, small and medium enterprises are considered as an engine for economic growth. These SMEs not only contribute to the growth of national GDP but also contributes to reduction of unemployment (Mullineux, 1997; Abor & Quartey, 2010).

In developed economies such as the United Kingdom and Germany, small and medium enterprises comprises of a major number of registered companies. In developing economy such as Ghana, despite there is limited data on the growth and development trends of SMEs, data available from the registrar general department suggests that about 92% of companies registered are small and medium firms.

Furthermore, small and medium enterprise provides 85 percent of manufacturing employment and contributes 70 percent to the national GDP. This supports the fact that, small and medium enterprises play a significant impact on economic growth and development, employment and income (OECD, 1997; Villars, 2004). Therefore most nations strived to create a harmonious environment and policies that support the sustainable growth of these small and medium enterprises.

SMEs in Ghana contribute massively on national GDP and employment in the manufacturing sector as stated above. It leads to the creation of employments, manufacturing of locally made goods and services for export, and helps the local government to generate tax revenues for national socio-economic development. These make the sector a very essential to the growth and development of national economy.

Despite the enormous contributions towards the development of economy, SMEs still face a number of challenges which has being our motivation for this study. This study, focus on the number of challenges that hinder the development of small and medium enterprise development in Ghana.

The study outlined the definition and contributions of SMEs to the Ghanaian economy and also review current literature to arrive at the pertaining challenges that faces small and medium enterprises in Ghana.

According to the study, despite the fact that there are numerous challenges affecting this sector, the most pertaining ones included, the lack of credit schemes and facilities, low capacity of research and development in technology, globalization and inadequate managerial knowledge and skills.

Furthermore, to curb this situation there should be collaboration among stakeholders such as government, financial institutions to provide credit facilities that are flexible to assess and repay.

**Keywords:** Credit facilities, Economic development, Ghana, SME's.

## INTRODUCTION

The contribution of development from the private sector to the sustainable growth of an economy cannot be underestimated. In both developed and developing economies, small and medium enterprises are considered as an engine for economic growth. These SME's not only contribute to the growth of national GDP but also contributes to the reduction of unemployment (Mullineux, 1997; Abor & Quartey, 2010). In developed economies such as the United Kingdom and Germany, small and medium enterprises comprises of a major number of registered companies. In a developing economy as Ghana, despite there is limited data on the growth and development trends of SMEs, data available from the registrar general department suggests that about 92% of companies registered are small and medium firms. Furthermore, small and medium enterprise provides 85 percent of manufacturing employment and contributes 70 percent to the national GDP. This supports the fact that small and medium enterprises play a significant impact on economic growth and development, employment and income (OECD, 1997; Villars, 2004). Therefore, most nations strived to create a harmonious environment and policies that support the sustainable growth of these small and medium enterprises. This is to enable small and medium enterprise turns out to be larger firms and corporations (Feeney & Riding, 1997). Furthermore, apart from small and medium enterprise being a source for job creation and employment, it also serves as a source of investment opportunities, provision of niche professional services and capacity building to both individuals and firms. It also serves as a revenue generation stream for government finances (Sowa et al, 1992; Mensah and Rolland, 2004; Palma and Gabriel, 2005). In a transition economy, small and medium enterprises play a vital role in the migration from state-led firms to a more private-led oriented firm (Aryeetey et al. 1994). Therefore, small and medium businesses serve as a seedbed for business development and economic growth in most developing economy including Ghana. The ability to motivate the development of sustainable small and medium enterprises is an essential ingredient to achieve rapid growth and economic development within the entire sub region.

Despite the numerous advantages that small and medium enterprise provides to the development of the national economy, its development has met a number of hurdles over the past decades. And this has declined the growth of a number of small and medium enterprises. These challenges enact from a number of sources that includes inadequate government policy to protect local businesses, globalization and entry of multinational firm, lack of finance in terms of credit facilities to SMEs, the inadequate use of technology, low R & D capability levels and others (Anheier & Seibel, 1987; Gockel & Akoena, 2002; Frempong, 2007). Therefore in order to achieve an efficient SME sector development, there is the need to deal with these challenges in a more proactive manner. This will enables firms to gain competitive advantage and be more competitive in their various industries. A healthy small and medium enterprise is the backbone for a healthy economic development.

The focus of this study is to examine the challenges affecting the growth and development of the small and medium enterprise sector of the Ghanaian economy. The paper is organized into the following sections, section 2 focus on the definition and development of SME's in Ghana, section 3 focus on the SME's and economic development, section four focus on the challenges of SME's in Ghana and then section 5 focus on the conclusion of this study.

### WHAT IS SME'S IN GHANA CONTEXT?

Over the period there has being a number of definitions for small and medium enterprises. Despite this, there is no universally accepted definition of small and medium enterprises. This is due to the fact that various scholars defines it from different point of views (Taylor and Adair, 1994). SME's in Ghana mainly consist of rural and urban enterprises. The World Bank defines small and medium enterprises as any firm that has an employee size of up to 300 and an annual sale of not up to US\$15 million (World Bank, 2002). In Ghana small and medium enterprises can be defined as any enterprise or business entity that employs less than 10 employees for small enterprise and firm with more than 10 employees is classified as medium and large enterprise according to the Ghana Statistical Service. The National Board for Small Scale Industries also defines SMEs by taking into account the size of employees and fixed asset. According to NBSSI definition of SME, a firm can be considered as a small and medium enterprise if it employs less than 10 employees and has a fixed asset including, plants and machinery not exceeding 10 million Ghana Cedis. This definition from the National Board for Small Scale Industries is limited and poses some form of inconsistency to be adopted universally due to a number of reasons that includes the frequent depreciation of the local currency and also the process of valuing these assets according to the Ghana Enterprise Development Commission (Kayanula and Quartey, 2000).

Furthermore, Osei et al (1993), classified SME's into four main categories that includes micro enterprises that employs less than 6 individuals, very small enterprises that employs 6-9 workers, small enterprises that employs 10 – 29 employees and medium enterprises that employs 29-50 individuals. Small and Medium enterprises according to the above definition emphasizes on employee size as compared to other definitions that takes into account fixed assets and others.

Table1: Summary table for SME definition.

<b>Enterprise Size</b>	<b>No. Of Employees</b>	<b>Revenue (including fixed Asset and Machinery) in Million Cedi's</b>
Medium	Fewer than 50	≤ 10
Small	Fewer than 30	≤ 10
Very Small	Fewer than 10	≤ 10
Micro	Fewer than 6	≤ 10

Source: Osei et al (1993).

#### **SME'S DEVELOPMENT IN GHANA**

Small and Medium enterprises evolved during the pre-colonial time where the middle class was trained to take over the businesses of European merchants. Despite this effort, the development of small and medium enterprises met impairment during the era of the first president of Ghana, who saw the rise of the private sector as a political threat, and therefore, formulated policies to discourage the formation of a vibrant private sector. The setback in the 1980's in large-scale manufacturing firms forced formal sector workers to seek for a secondary source of revenue stream, and this resulted in the setting up small and medium private enterprises. Therefore, government enacted policies to encourage the setting up of SME's (Kayanula and Quartey, 2000).

In 1981, National Board for the Small, Scale Industries was set up in accordance with the Act 434 as the upmost body to oversee the activities of small-scale industries in Ghana. The board was widened in 1991 and 1994 respectively by integrating the Ghanaian Enterprise Development Commission and Cottage Industries into the National Board for Small Scale Industries.

Furthermore, to promote the adaptation of technology in this sector the technology Industrial Service was set up in 1987 to monitor the transfer of technology and the Technology Transfer Unit. To further strengthen the private sector and small and medium enterprises the government introduced a number of policy reforms geared towards the improvement of this sector. Among these reforms the most significant ones among them according to Kayanula and Quartey (2000), includes the Private sector Advisory Group, the abolishment of the Manufacturing Industries Act 1971(Act 356), and this lead to the repeal of the price control law. Furthermore, the introduction of the Investment Code of 1985 under the PNDC law 116, this lead to the promotion of foreign investment and joint ventures.

The Private sector development ministry was established in 2001 to serve as a supervising body to promote private sector development. Since the private sector serves as the engine for growth for most economies around the global, this Ministry was charge with the responsibilities of providing training and skill based development programs to improve the skills and capacity of local entrepreneurs. To promote a sustainable agriculture sector since agricultural products serves as a major source of raw materials for most small and medium enterprises, the government launched the President Special Initiative (PSI). This initiative was set up to create job and also serve as a poverty alleviation scheme through agribusiness an export. Since the inception of this program, a considerable number of entrepreneurs in the agribusiness has benefitted from the capacity building programs and also the business network available for the export of commodities through the PSI offices and agencies.

The Rural Enterprise Development program is also one of the major reforms introduced by the government to promote rural enterprises. This program also aims at providing aid for the development of small and medium

enterprises in the district level. As part of the Rural Enterprise Development program, each district is to identify three (3) business development projects for development in their respective locality.

### **SME'S AND ECONOMIC DEVELOPMENT**

To achieve rapid economic development, the private sector cannot be sidelined. Notwithstanding this fact, small and medium enterprise plays a significant role in the economic development of many developing and developed countries (Abor, 2010; OCED, 2002). The entrepreneurial and innovative nature of small and medium enterprises contributes to poverty reduction in developing economies. This promotes competition and hence has a positive impact on the macro-environment and contributes to aggregate economic growth. It further boosts job creation and contributes extensively to government revenue generation stream (Snodgrass and Biggs, 1996; Beck and Demirguc-Kunt, 2004). The numerous advantages that the national economy enjoy from the growth of small and medium enterprises cannot be underestimated, and this can be ascertain through the various support from donor agencies over the years (World Bank, 2002). This area has served as a medium for economic growth.

Furthermore, one of the significant benefits that nations enjoy from a vibrant small and medium sector is the capacity of small and medium industries to enjoy a major number of unemployed citizens. Small and medium industries play an essential role in the improvement of income of household in last developed economies through job creation, industrial development and rural development. It furthers support government measures and policies to tackle poverty reduction (Tambuan, 2006). In Ghana, a small and medium enterprise sector provides almost over 85% of manufacturing employment. And this is a significant step in both job creation and poverty reduction (Abor and Quartey, 2010; Aryeetey, 2001; Steel ad Webster, 1991).

Whiles contributing to employment and job creation, small and medium enterprise turns out to be a major contributor to the national GDP and national income. Over 70% of the nation GDP of Ghana is sourced from small and medium enterprises. SME's turns out to be a major national revenue stream since over 92% of registered business in Ghana fall under this category. These entities provide value added manufacturing products and service to various market segments and customers (Abor and Quartey, 2010, Berry et al 2002; Gumede, 2000).

### **CHALLENGES AFFECTING THE SME SECTOR IN GHANA**

Small and medium enterprises plays a significant role in the development of national economies, despite this fact there happen to be a lot of hurdles that affect the growth and development of SME' in Ghana. These numbers of factors includes, lack of credit facility for small and medium enterprises, inadequate infrastructure, low managerial skills, low technological levels/upgrading, weak institutional and regulatory framework and globalization. In order to have a more vibrant and successful private sector there should be in place mechanism that will provide easy credit assess to small and medium enterprises.

One of the major constraints to the development of SME's is the access to credit (Lader, 1996; Parker et al, 1995; Green at al, 2002). It has being noticed over the years that financing for smallest and medium enterprises comes from personally saving of firm owners and sometimes from friends and family. This pool of financial resource is limited and cannot sustain the lifespan of these enterprises.

Another factor that serves as a hurdle for credit facility assessment is the documentation requirement from credit facilities such as banks and other (Davenport, 1967). Micro credit facilities have turned out to be a source of credit facility for small and medium enterprises. The high-interest rate charged by these micro-credit institutions turns to cripples these business since all the revenue made is used to repay their loans and nothing left to develop new innovative products and expand their business (Ayeetey et al, 1994).

The rapid change in the development has also serve as a hinder to the development of SME's in recent times. Since small and medium enterprise do not have the capacity to conduct research and development to develop new innovative product. And also the difficulty associated in having access to new technologies and modern methods of productions in their respective area poses a strict challenge to the growth of this sector (Aryeetey et al, 1994).

Furthermore, the gap in management literacy is higher since most owners' of SME's has little or no knowledge about management processes and procedures. There is the lack of management talents in this sector as compared with larger firms and MNC's (Kayanula and Quartey, 2000). And this can be attributed to the high cost

associated with training and consulting services, while others do not see the essence of upgrading their skills since their businesses thrive under current dispensations.

SME's existences have been advocated several decades now and have led to the establishment of individual bodies and institutions to regular this sector. Despite the role it plays in the development of the economy little has been done to enact laws and policies that will shield SME's from multinational companies that turn out to enjoy the vast amount of resources, making them more competitive even on the backyard of these SME's. The high cost of licensing, legal cost, strict processes and procedure involved in doing business also hinder the development of SMEs. In a survey conducted in 2006 into how business is conducted in many economies reports that it takes up to 127 days to deal with issues such as licensing and need to go through 16 different procedures to acquire needed license. This process slows down the development of SME's with legal status since owners of SME's operated with tightly financial resources and, therefore cannot cope with the cost and time consumed by these processes (Abor and Quartey, 2010; Kayanula and Quartey, 2000).

## CONCLUSION

This paper focuses on the challenges that are affecting the rapid development and growth of the small and medium enterprises in Ghana. SME's definitions in this context mostly focus on the employee size and firm turnover. In this paper small and medium enterprise was defined from the Ghanaian perspective. The paper further took a dive into the characteristics and contribution of small and medium enterprises towards the development of national economy. In assessing the factors that hinder the development of firm it turns out that specific issues such as the access to easy and reliable credit at affordable interest rate was unavailable, lack of managerial and technological know-how with this sector of the economy.

The paper suggests in order to gain a vibrant and sustainable small and medium enterprise sector these issues need to be addressed. Financial institutions and government should make available funds that can be accessed by SME's at a reasonable interest rate to aid the expansion and development of this sector since it is a major stakeholder in unemployment reduction and poverty alleviation. Furthermore government should provide incentives for SME's that enter into specific industries such as technological industries to boost indigenous technological competence and capabilities. The process of doing business also should be revised to a more flexible approach to encourage the informal SME business that comprises of larger sector of firms within small and medium enterprises to migrate into formal legal entities.

Finally, SMEs should embrace the benefit of business outsourcing to enable them gain competitive edge, have access to global IT knowledge, maximizing productivity, and lower direct staff cost.

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