

INVESTIGATING WHETHER A LACK OF MARKETING AND MANAGERIAL SKILLS IS THE MAIN CAUSE OF BUSINESS FAILURE IN SOUTH AFRICA

S Radipere and L van Scheers

School of Business Management, University of South Africa

Abstract

The literature reveals that 40 per cent of new business ventures fail in their first year, 60 per cent in their second year, and 90 per cent in their first 10 years of existence. The research problem of this study is suggested by this high rate of business failure. This study investigates whether lack of marketing and managerial skills in business owners contributes to the high rate of business failure in South Africa.

It is evident from the results that small business owners lack certain managerial skills, including financial, marketing and human-resource management skills, needed to operate their businesses successfully. The findings confirm that small business owners are in need of support services such as training, counselling, and financial assistance. They also show that small businesses are constrained not only by financial factors but also specifically by non-financial factors such as lack of education, inadequate managerial skills, poor access to markets, lack of information and unreliable infrastructure. The analysis also indicates that the managerial skills possessed by the respondents do not correlate with those that they preferably should have to run a successful business.

The study concludes that a lack of MARKETING AND managerial skills has a negative impact on the success, viability and development of small businesses. The challenge is to improve the managerial skills of small business owners, since the small business sector is widely considered to be the ideal site for the solving of South Africa's unemployment problems and the rejuvenation of its stagnating economy.

JEL M13

1 Introduction

South Africa is a country of growing business opportunity in which the spirit of free enterprise is evident. Although a large and growing pool of labour is available for training, there is a growing shortage of capable small business owners (Government Gazette, 1998: 124). Improving the managerial skills of small business owners/managers is therefore of crucial importance if unemployment is to be decreased. Unemployment is widely recognized as a major factor inhibiting economical stability in South Africa and therefore improving the managerial skills of small business owners can help to make

NEPAD's dream to improving the economy a reality (GEM, 2002: 22).

The research problem of this study focuses on the current high rate of business failure in South Africa. According to the Central Statistic Service (CSS) (2000: 35), 40 per cent of new business ventures fail in their first year, 60 per cent in their second year, and 90 per cent in their first 10 years of existence. Entrepreneurs need marketing and managerial skills to prevent business failure and therefore this study hopes to establish whether or not shortcomings in the managerial skills of entrepreneurs contribute to business failure.

2

Aim and objectives of the study

The aim of this study is to investigate entrepreneurs' perceptions, to establish why they fail and whether or not their lack of marketing and managerial skills has an impact on the success or failure of their businesses. This research study therefore focuses on analysing the managerial skills of small business entrepreneurs in the formal sector.

To achieve this aim, the objectives of this study are:

- to investigate whether or not there is a relationship between lack of managerial skills and business failure in South Africa,
- to collect data on the existing managerial skills of small business owners, and
- to investigate the gap between the managerial skills that small business owners should have and those that they actually possess.

3

Literature review

Small business undertakings create about 80 per cent of all new job opportunities; according to Bowler, Dawood and Page (1998: 109), more than 70 per cent of all South Africans are employed in the small business sector. This sector is thus an essential factor to consider in efforts to promote and achieve economic growth and development and the widespread creation of wealth and employment. Nager, Swanepoel and Van der Merwe (2001: 37) indicate that small business development should be an essential component of all reconstruction and development initiatives and that this has the potential to economically empower the majority of the country's people.

3.1 Small businesses in South Africa

A small business is defined by Bowler *et al.* (1996) as an independent profit-orientated business unit that is personally managed by the owners and has a small influence or market

share in the business world. Kroon and Moolman (1999: 13) state that managing a small business comprises several factors, for example creating and exploiting an opportunity; having a sense of enterprise, vision, innovation, commitment and motivation; taking calculated risks; coping with uncertain circumstances; and showing leadership and control. Pearce and Byars (2000: 267) explain that, though starting a business is risky, efficiently performing managerial skills and achieving competitive advantage can create a successful business. The small business owner needs to be multi-skilled to perform the many managerial functions necessary for business success. Managerial skills are specific abilities that result from knowledge, experience, information, practice and aptitude (Bateman & Snell, 1996: 16). The development of these managerial skills may improve business operations and consequently assist with the creation of employment in South Africa.

3.2 Managerial skills

Murphy (1996: 13-14) states that small business owners tend to exhibit certain personality traits that are responsible for the success or failure of their businesses. Owners with inadequate managerial skills create management problems in the small business sector. This deprives the country of healthy concerns that can provide employment opportunities for the unemployed masses.

Managerial skills can be improved through training programme and practical experience.

Managerial skills can be sorted into four main groups. The first group focuses on participation and human-relations skills, for example, constructive communication and team building, while the second group focuses on competitiveness and control, for example, assertiveness, power and influence. A third group focuses on innovativeness and entrepreneurship, such as creative problem-solving, while a fourth group focuses on maintaining order and rationality, for example time management and rational decision-making. In these four groups the following important managerial skills can be singled out

for attention: technical, conceptual, interpersonal, communication, analytical, decision-making, administrative and problem-solving skills.

3.3 Problems experienced by small business owners

Dockel and Ligthelm (2002: 2) classify the problems experienced by small business owners in conducting a successful business into two categories, namely:

- Market-related issues, such as marketing, locality, lack of knowledge of the market, product demand and competition, which are associated with the industry in which the enterprise operates; and
- Enterprise-based issues, which are the business's internal factors such as incompetent management, lack of managerial skills and poor financial control.

Enterprise-based problems are found to be associated with 65 per cent of small business failures (Dockel & Ligthelm, 2002: 3). Failure stems largely from the following areas: managerial skills, management behaviour and financial knowledge. Lack of expertise in the functional areas of marketing, human-resource management and financial issues is often reported.

4 Methodology

Both primary and secondary sources are used to gather information for an analysis of the managerial skills of small business owners. The main secondary sources are journals, articles, press reports, books and research studies.

Since the aim of this study is to understand the perceptions of small business owners, a qualitative paradigm is used for the primary research. The population investigated is made up of small business owners in South Africa. A Department of Trade and Industry list (2001: 48) of 10 000 small business owners forms the population of the study. A sample of 1000 small business owners was randomly selected from

this list, and each member of the sample interviewed face-to-face, using a questionnaire, between 1st and 28th of February 2004. 801 replies were received, which is a response rate of 80 per cent. This may be considered a good response rate, according to Nederhof (2002), considering the sensitivity of the topic, the nature of the problem under investigation and the inhibitions that management might have regarding the survey.

The measuring instrument used for this study is a questionnaire which consists of a set of questions divided into three sections. The first section, consisting of four closed-ended questions, investigates the demographic profile of the respondent. The second section of the questionnaire, consisting of seven questions, investigates the impact of enterprise-based issues such as the existing managerial skills of small business owners. Section two also measures the impact of market-related issues on the business. The last section, consisting of 10 questions, establishes the gaps between the managerial skills that small business owners should have and the respondent's existing skills, the factors that lead to business failure and also the relationship between lack of managerial skills and business failure.

4.1 Hypothesis formulation

According to Wegner (1999), in order to test claims or assertions, sample data must be gathered and analysed. On the basis of these sample findings, the hypothesised value of the population parameter is either accepted as probably true or rejected as probably false.

When formulating the research hypothesis, three hypotheses may be considered, namely:

- the null hypothesis,
- the confounding variable hypothesis, and
- the causal hypothesis.

The causal hypothesis may only be accepted if:

- the null hypothesis is rejected by statistical analysis,
- each potential confounding variable hypothesis is ruled out based on appropriate controls.

The primary data was analysed using a descriptive analysis method, to construct frequency distributions for the data. This descriptive analysis thus used survey data to construct hypotheses. Inferential analysis was then used to test the hypotheses using the significance approach. This approach has the following steps:

- Formulate the null and alternative hypothesis.
- Specify the significance level.
- Select an appropriate statistical test.
- Identify the probability distribution and define the region of rejection. This step involves calculating the critical value of a test statistic, which for this study is an average. The significance approach is used and assumes a normal distribution.
- Compute the value of a test statistic. This is the observed value obtained from the survey.
- Decide whether to reject or accept the null hypothesis.

In this research study a null hypothesis was used. The hypothesis formulated for this study is: There is a 60 per cent chance that no relationship exists between the managerial skills of small business owners and business failure in South Africa.

5 Research findings

The questions asked in the questionnaire establish the demographic profile of the small business owners. The study aims to establish whether or not the gender of the respondents influences the standard of their managerial skills and thus the failure rate of small businesses. The sample units, small businesses, are also described in terms of number of years in operation to establish whether the age of a business influences its success rate; industry type, to investigate whether businesses in certain industries are more susceptible to failure than others; ownership by population group, to see whether race influence failure rate; and prior

business experience of the owner, to establish whether this helps to prevent failure. The findings are as follows:

5.1 Demographic profile

5.1.1 Gender of respondents

73 per cent of the respondents surveyed are male and 27 per cent female. South Africa thus demonstrates a typical African profile, with men being twice as likely as women to be new enterprise entrepreneurs and one and half times more likely to be owner-managers of established firms. The study does not find evidence that gender has an influence on business failure rate.

5.1.2 Age of the business (number of years in operation)

The age of a business reflects its market experience and affects its ability to grow and move to the next size class. Furthermore, market experience and size of a business are important variables that determine the business's access to financial resources. According to the questionnaires, most businesses (74 per cent) have operated for two or more years. Only 26 per cent have been in operation for less than a year, and these range in age from one month to two years in operation. These findings seem to suggest that the longer a business survives, the greater its chances of continuing to survive. This is an encouraging finding considering the high unemployment rate in South Africa. International experience has shown that births and deaths among small businesses tend to be concentrated among younger and smaller firms.

5.1.3 Nature of industry

The results indicate that 62 per cent of the respondents operate in the retail industry. Of the total sample, approximately one third, 30.4 per cent, conduct business in the services industry. Only 7.6 per cent of the survey population participate in the construction and manufacturing industries. This correlates with previous studies which have found that small businesses in the retail sector have a higher failure rate as a result of the ease of entering this sector and the consequent possibility of overtrading.

5.1.4 Population group of respondents

The nature of small business owners by population group is presented in figure 1.

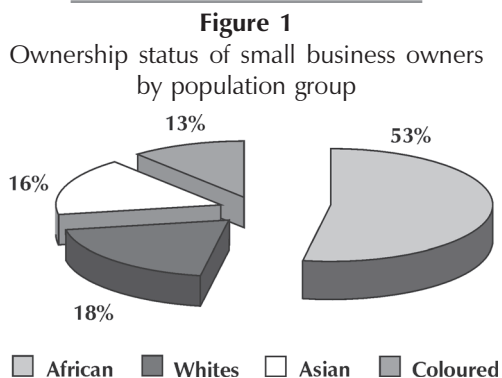


Figure 1 indicates that the highest proportion of small businesses, 53 per cent, are owned by Africans, followed by 18 per cent owned by Whites and then 16 and 13 per cent owned by Asian and Coloured people respectively. The study finds no evidence that race impacts on the failure of small businesses.

Prior business experience of respondents

The question, "Do you have prior business experience?" was asked to establish whether or not respondents with prior business experience have a better chance of success. Only 28 per cent of the respondents indicated that they had prior business experience, which means that 72 per cent of the respondents are first-time business operators. The results establish that respondents with prior business experience have a better chance of business success.

5.2 The impact of market-related issues on the business

The impact of market-related issues on small business owners was measured in question C2 of the questionnaire. Secondary research identified five market-related issues, namely: poor locality, ineffective marketing, lack of market knowledge, low product demand and increase in competition. The question tested whether any of these issues had an impact on the failure of the respondent's business. The findings are presented in figure 2.

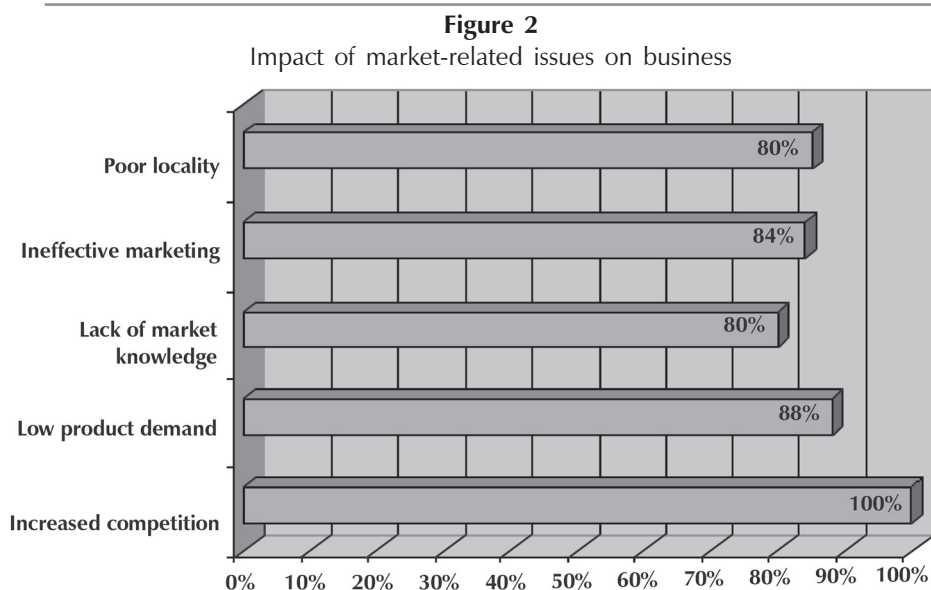


Figure 2 indicates that:

- 100 per cent of the respondents experienced increased competition,
- 88 per cent complained of low demand for their products,
- 85 per cent complained of poor locality of their small business,
- 84 per cent complained of ineffective marketing of their products, and

- 80 per cent experienced lack of market knowledge.

The respondents clearly believe that these five factors directly impact on the success or failure of a business. Increased competition indirectly decreases small business income, which can lead to business failure.

5.3 The impact of enterprise-based issues on the business

The respondents were asked whether enterprise-based issues such as managerial skills and business knowledge affected their businesses and also what influence factors such

as crime, the economy, finance, labour and rent have on their business success.

Managerial skills and business knowledge are an indication of how well an entrepreneur can perform important tasks and activities related to the functioning of a business. The respondents were asked in the questionnaire which of the managerial skills necessary for the successful running of a business they feel they lack. They indicated the following managerial skills: management of personal stress, time management, performance appraisal, motivation of employees, conflict management, problem solving, marketing, bookkeeping, record keeping, writing of business plans and pricing. Figure 3 presents these findings.

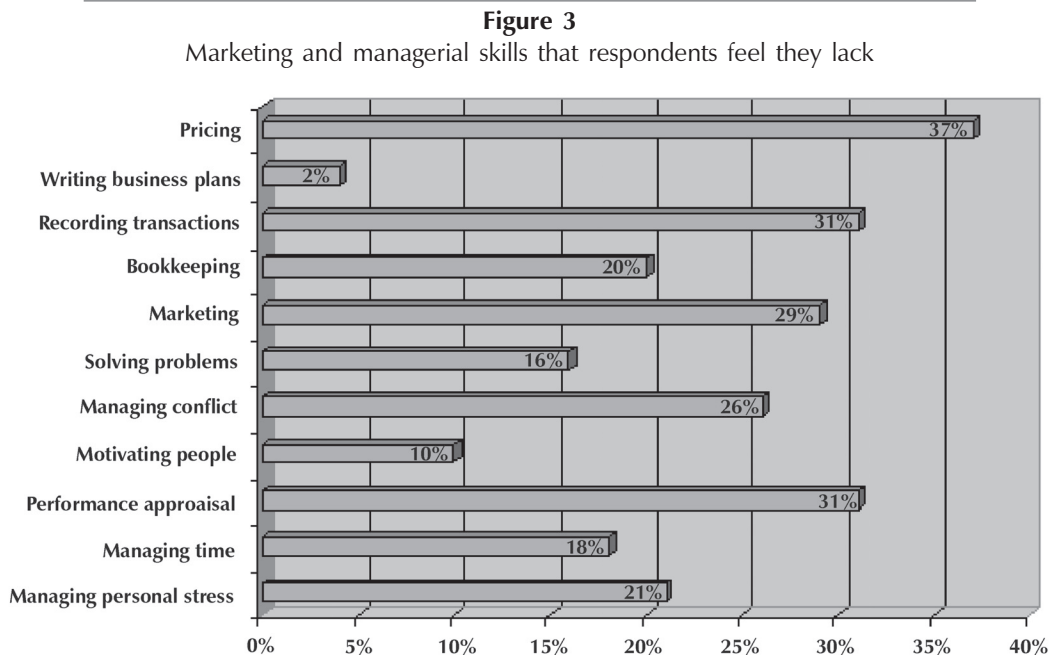


Figure 3 indicates that the respondents feel they lack the following managerial skills:

- 37 per cent of the respondents have problems establishing prices of products and services,
- 31 per cent do not know how to record business transactions,
- 31 per cent cannot write a performance appraisal,
- 29 per cent experience marketing problems,
- 26 per cent have difficulty managing conflict in the workplace,
- 18 per cent have problems with time management,
- 16 per cent have trouble solving problems,
- 21 per cent cannot manage personal stress,

- 20 per cent experience problems with bookkeeping,
- 10 per cent have problems motivating people, and
- 4 per cent cannot write a business plan.

The respondents were asked in an open-ended question to list the problems they faced. The following are the problems they list: crime, economic factors, finance, labour and rent. The findings are presented in figure 4.

Figure 4
Problems faced by respondents

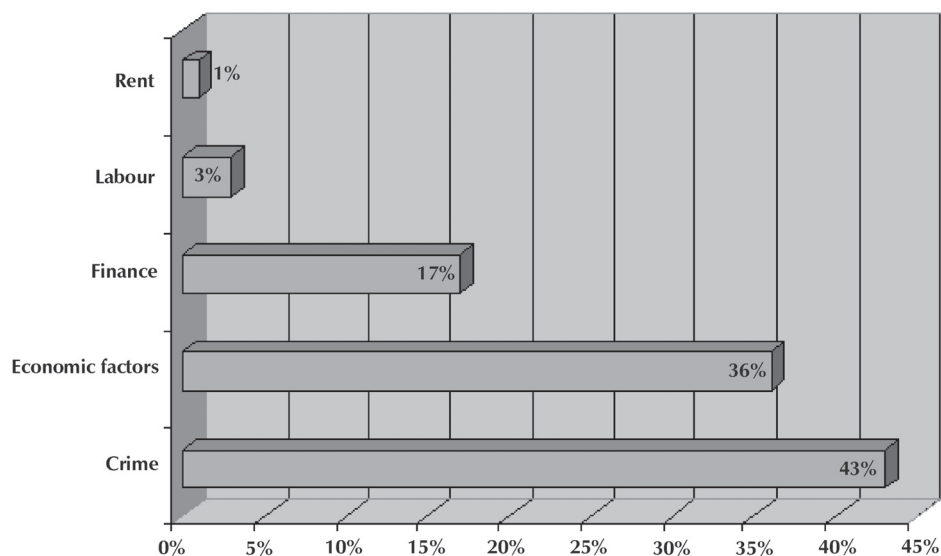


Figure 4 indicates that 43 per cent of the respondents perceive crime as the biggest problem they have to face. At least two out of five enterprises are affected by crime. Some respondents indicate in the comments section that formal businesses with premises away from home and those that hold stock are at greater risk, since this makes them more vulnerable to crimes such as burglary outside business hours. Some respondents also mention “off the record” that crime is a widespread problem in the black townships, in effect imposing an additional premium on running a business there, and that this is an incentive to relocate elsewhere, outside of the black areas. As indicated in figure 4, 36 per cent of the respondents perceive economic trends as an external factor causing problems to business. Small businesses cannot control these external factors that harm them. 17 per cent of the respondents with existing businesses regard finance as a problem. Only

three per cent of the respondents say that they experience problems with employees, and only one per cent complains about the rent they pay. Respondents overall agree that crime and economic factors are the most important negative factors impacting on the success of their businesses.

5.4 Factors contributing to small business failure

Factors contributing to the closure of small businesses investigated in the questionnaire include: failure of first attempt to establish a business, reasons why businesses fail and the relationship between lack of managerial skills and business failure.

5.4.1 Failure of first attempt to establish a business

This question attempts to find out whether the respondent’s first initiative in establishing a

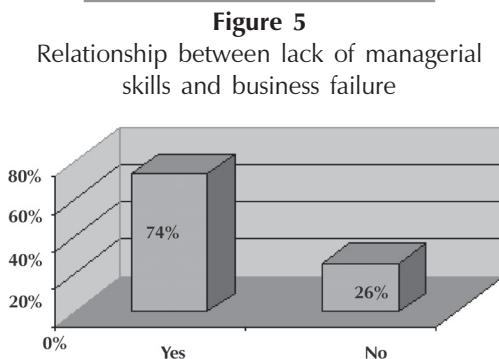
business had failed, or not. The findings reveal that for most respondents, for 83 per cent in fact, the first business initiative proved to be unsuccessful. Only 17 per cent of the respondents say that their first business venture succeeded.

5.4.2 *Reasons why businesses fail*

The respondents give the following two reasons for business failure: lack of managerial skills and financial problems. 90 per cent of the respondents believe that small businesses fail due to a lack of managerial skills. The findings show that the respondents lack the following key managerial skills: financial skills, record keeping, financial planning/budgeting, bookkeeping, business plan writing and credit management. 70 per cent of the respondents, whose first business initiative failed, blamed financial problems for this failure. The results suggest that a lack of money for running costs or capital items is a widespread problem facing small businesses.

5.4.3 *Relationship between lack of managerial skills and business failure*

The respondents were asked whether they believe that a positive relationship exists between lack of managerial skills in small business owners and business failure in South Africa. The results are shown in figure 5.



As indicated in figure 5, 74 per cent of the respondents believe that there is a positive relationship between lack of managerial skills in small business owners and business failure in South Africa, as opposed to only 26 per cent who do not think such a relationship exists.

The aim of this study, as discussed before, was to investigate whether lack of managerial skills is the main cause of business failure in the small business sector in South Africa. The null hypothesis is:

There is a 60 per cent chance that no relationship exists between the managerial skills of small business owners and business failure in South Africa.

This hypothesis will be tested as follows.

Formulate the null and alternative hypotheses:

The research will accept the hypothesis with a 95 per cent level of confidence.

$$H_0: \pi \leq 0.6 \quad (n = 2000)$$

$$H_1: \pi > 0.6$$

Specify the significance level:

Decide on the desired level of significance.

The allowable error is 5 per cent, therefore $\alpha = 0.05$

Select an appropriate statistical test:

The z-test is used because the sample is greater than 30 ($n > 30$) and ratio data is used.

Identify the probability distribution and define the region of rejection:

This step involves calculating the critical value of a test statistic, which for this study is an average. The significance approach is used and assumes a normal distribution.

$z = 1.64$ which forms the critical value.

Compute the value of a test statistic, which is the observed value obtained from the survey.

$$\begin{aligned} & \sqrt{\frac{p(1-p)}{n}} \\ &= \sqrt{\frac{0.743(1-0.743)}{120}} \\ &= 4.0 \text{ per cent} \end{aligned}$$

At a 95 per cent level of confidence (or 0.05 significance level) $z = 1.96$. Consequently the deviation from the sample proportion is 7.8 per cent (1.96×0.04). This means that at least 66.5 per cent of the respondents believe that a positive relationship exists between the managerial skills of small business owners and business development in South Africa.

Decide whether to reject or accept the null hypothesis:

The results indicate that 74 per cent of the respondents believe that there is a positive relationship between the managerial skills of small business owners and business development in South Africa.

Therefore reject the null hypothesis

The conclusion is that there is a positive relationship between the managerial skills of small business owners and business failure in South Africa.

6

Recommendations

6.1 Improving managerial skills

Managerial skills are required to organise the physical and financial resources needed to run a business. The level of managerial skills and business knowledge are among the most important indicators of how well an entrepreneur can perform important tasks and activities related to the functioning of a business. Government's involvement in managerial training focuses on basic literacy, numeracy and communication skills with a developmental rather than a business focus. This study suggests that training should also focus on administration, financial management and marketing skills. Training should be more practical and less formal and classroom-based, and should also include follow-up practical courses. Small business owners would then be better equipped to make better-informed decisions, and to steer their business away from known pitfalls.

6.2 What small business owners lack

South Africa has too few people with small business managing qualities, which contributes to the poor performance of the South African economy because only a few people succeed as small business owners. Deficiencies in the internal microenvironments of businesses are the major cause of small business failures. Cause for failure centres largely on lack of managerial skills, poor management behaviour and lack of financial knowledge.

To promote small businesses' ability to exploit economic opportunities, a support structure should be designed to address these shortcomings. These support structures should be as comprehensive as possible, including training in management and business skills, systems for financial support, assistance with the marketing of products and services, and counselling on running a business.

6.3 How to address the problem

Educators in South Africa should be aware of the relative importance of the problems identified in this study, and discussions thereof should form an integral component of training or mentorship programmes. Environmental scanning and planning should receive more attention in syllabi. The development of financial acumen and planning skills should also be seen as crucial elements to be offered in any business course. This study indicates that the need for managerial training is greatest among small business owners from previously disadvantaged communities. The results confirm that a lack of managerial skills is the main cause of business failure in South Africa

References

- 1 BATEMAN, T.S. & SNELL, S.A. (1996) *Management: Building Competitive Advantage*, Third Edition, Irwin: Chicago.
- 2 BOWLER, A.; DAWOOD, M.S. & PAGE, S. (1998) *Entrepreneurship and Small Business Management*, Juta: Pretoria.
- 3 CENTRAL STATISTIC SERVICE. (2002) "Development of SMMEs". <http://www.statssa.gov.za/Statistical-releases.htm> (Accessed 15 May 2002).
- 4 DEPARTMENT OF TRADE AND INDUSTRY. "List of small business ventures in South Africa". S.a. www.thedti.gov.za (Accessed 12 March 2001).
- 5 DOCKEL, J.A. & LIGTHELM, A.A. (2002) Factors that contribute to small business survival, Article submitted for publication, UNISA: Pretoria.
- 6 GEM (2002) "Small business development", www.gem.org.za. (Accessed 18 October 05).

- 7 GOVERNMENT GAZETTE. (1998) "Creating jobs, fighting poverty: An employment strategy framework": *Notice 1264*. 397(19040), 3 July 1998. Government Printers: Pretoria.
- 8 KROON, J. & MOOLMAN, P.L. (1999) *Entrepreneurship*, Kagiso Publishers: Pretoria.
- 9 MURPHY, M. (1996) *Small Business Management*, Financial Times and Pitman Publishing: London.
- 10 NAGER, T; SWANEPOEL, E. & VAN DER MERWE, M.A. (2001) *Introduction to Entrepreneurship and Small Business Management*, UNISA: Pretoria.
- 11 NEDERHOF, K. (2002) *Social Research Methods*, Bacon: London.
- 12 PEARCE, J.A. & BYARS, L.L. (2000) *Management*, McGraw Hill: New York.
- 13 WEGNER, A. (1999) *Research methodology*, McGraw Hill: New York.