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SMEs development and failure avoidance in developing countries through public private partnership

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This study examines the current developments of small and medium enterprises (SMEs) in Pakistan and the effectiveness of public-private partnership for SME development. Some important facts are presented. A comprehensive international literature study was undertaken. A questionnaire was developed for small and medium sized enterprises owners and top managers to access the status of their enterprises and also to examine SMEs developmental strategies adopted by them. Linear regression was employed for analysis of the data. The study found that SMEs are of overwhelming importance to developing countries because they account for more than 90% of all firms outside the agricultural sector. The study also found that main constraints faced by small entrepreneurs are lack of finance, low human resource capabilities, and technological capabilities. Finally, the government has been the most important supporting agency for SMEs in Pakistan. However, evidence of the effectiveness of government and private programs to support SME development is mixed and not so encouraging. After analyzing the current SMEs' developmental strategies (adopted by both public and private sectors) the study suggested public private partnership (PPP) as future strategy for SMEs' development in developing countries.

Key words: Small and medium enterprises, public private partnership, developing countries, Pakistan, entrepreneurship.

INTRODUCTION

Small and medium enterprises (SMEs) are essential to the economy of every country, particularly developing economies. For today's competitive and challenging international situations, a really viable and dynamic SME sector is vital for the economic growth of developing countries. SMEs are engine of growth in prosperous and growing economies and play a significant part in creating economic growth. SMEs contribute in developing economies by generating employment, offering advanced and innovative products and services through entrepreneurship and enhance international trade of an economy through diversification. SMEs play a critical role in generating income and improving growth rate in

underdeveloped and developing economies.

SMEs are strategically important in many developing countries, particularly those located in the Asian region. The SME sector consists of more than 90% of all firms outside the agricultural sector in the region (Wattanapruttipaisan, 2003). They are the primary vehicles by which new entrepreneurs provide the economy with a continuous supply of ideas, skills, and innovations (CACCI, 2003). All over the world, SMEs are being supported on the grounds that they make substantial contributions to productivity growth and, consequently, competitiveness and aggregate economic growth. In addition, SMEs are believed to be especially effective job creators and enjoy the reputation of being sources of income, providing training opportunities as well as important basic services for disadvantaged people (UNIDO, 2006).

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Small and medium manufacturing sector in Pakistan, even after worst ever global financial crisis maintained its healthy growth at 7.5% in 2008 to 2009 (Economic Survey of Pakistan, 2008-2009). In Pakistan, SMEs account for more than 95% of the total number of establishments, 80% of employment outside agriculture (SMEDA, 2007).

Across the South Asia, the contribution of SMEs to the overall economic growth and the GDP is high. It is estimated that SMEs contribute 50% of Bangladesh's industrial GDP and provide employment to 82% of the total industrial sector employment. In Nepal, SMEs constitute more than 98% of all establishments and contribute 63% of the value-added segment. In India, SMEs' contribution to GDP is 30%.

SMEs are contributing significantly in Pakistan's economy since its independence. In Pakistan economically active SMEs are approximately 3.2 million which are a source of 78% non-agriculture sector employment and are contributing 30% to GDP (Hussain, 2009). Despite of its greater contribution in Pakistan's economy SME sector is unable to acquire government consideration. SMEs are restricted to main cities and the rural areas not have even essential information about SMEs. The key constraint SMEs facing in developing countries is their isolation, which hamper access to markets, information, finance and institutional support (Mead and Liedholm, 1998; Swierczek and Ha, 2003). Therefore the study investigates the possibility of PPPs to overcome such problems.

The proper definition of SMEs has been the subject of considerable debate. Obviously, it varies from country to country, depending on the purpose for which the definition is used, the overall level of economic development (a large enterprise in Pakistan may be considered a small one in China) and using different criteria like employment or capital invested. Generally, however, in most developing economies the following broad categories would appear to apply:

- a) Micro enterprises: employment level below 10
- b) Small enterprises: employment level from 10 to 49
- c) Medium enterprises: employment level from 50 to 249

UNIDO uses the term 'SME' to refer to firms in these three categories.

SMEs due to their size face problems that make them vulnerable and prevent them from attaining growth. These problems are particularly significant in the areas of human resources development, technological capability, and access to financing. In presence of such problems, many SMEs are unable meet the challenges created due to liberalization and globalization of markets. SMEs on their own are unable to meet such kind of challenges.

In developing countries the full potential of the SME sector is yet to be tapped due to the existence of a number of constraints hampering the development of the

sector. SMEs in developing countries primarily face issues relating to business regulations and restrictions, finance, human resource capabilities and technological capabilities (Asian SME summit, 2009). Developing SMEs in developing countries is an important challenge. The main underlying constraints to their growth are lack of finance, lack of human resource capabilities and lack of technological capabilities. There is generally a lack of awareness in developing countries regarding significance of PPPs. The purpose of the study is, twofold: first, it investigates into the constraints that SMEs face in developing countries; second, it suggests how PPP can help to remove the constraints to SMEs development. Therefore, the study investigates the current situation of PPP and forward policies to enhance public private cooperation in developing countries for SMEs development. The study, therefore, serve to all the stakeholders for improving the various aspects of SME development in Pakistan particularly and in developing countries in general.

The remainder of this paper is structured as follows: summary of recent empirical evidence on SMEs' constraints and patterns; followed by discussion of public-private partnership, its need and importance and benefits to SMEs; then we present the materials and methods used in the study, and discuss in detail results of the study; finally, the conclusion.

LITERATURE REVIEW

SMEs are different from large organizations in several characteristics like resource limitations (financial, human and technological), informal strategies, and flexible structures (Hudson et al., 2001; Qian and Li, 2003). As a consequence, SMEs have higher failure rate than large enterprises. This also causes slow growth of SMEs. Every SME has a set of distinctive resources that provides the foundation for its growth and development. The resource based theory explains these resources; these resources are firm's physical capital resources, human capital resources and organizational resources (Barney, 1991). Hitt et al. (2002) described a firm's resources as a key input and categorized them into tangible and intangible resources. Lack of these resources restricts SMEs growth in developing countries. The study particularly analyzes that how lack of three key resources, finance, human capital and technological resource affect SMEs growth and can PPPs be a way for overcoming this lack of resource to SMEs and enhancing their growth and development.

Lack of finance

SMEs growth and development in developing countries is vital, as they play a key role in creating new jobs and

reducing poverty. Adequate financing is necessary to help SMEs set up and expand their operations, develop new products, and invest in new staff or production facilities. However, in developing countries SMEs often run into problems, because they find it much harder to obtain financing from banks, capital markets or other suppliers of credit (OECD, 2006).

Several studies recognized lack of finance as major constraint in SMEs development in developing countries (Ayyagari et al., 2006; Beck et al., 2006; Cook and Nixon, 2000; Minton, 2006; Tambunan, 2008; Zia, 2008). In Pakistan, Bari et al. (2005) described lack of finance as major constraint in SMEs development in Pakistan. SMEs in China are facing greater credit constraints and have limited access to bank loans. Lin (2007) described that over 98% of SMEs have no access to formal financing. According to Shen et al. (2008), SMEs in China obtain only 12% of their capital from bank loans, while their peers obtain 21% in Malaysia and 24% in Indonesia. Lacking appropriate financing channels has become the main hurdle for the development of SMEs. Lin (2007) argues that as SMEs are often labor-intensive enterprises, their ability to absorb labor costs are reduced when they face credit constraints. Therefore, the need is to establish small and medium-sized banks through PPP to deal with the difficulty of accessing bank credit for SMEs.

Low human resource capabilities

A firm's efficiency is also dependent upon the abilities and how-know of the human capital of its employees. This human capital consists of education and training provided to employees. Educated workers are not only more productive, but they have more learning and innovative abilities (Batra and Tan, 2003). Those SMEs which have more capable workers are likely to be more efficient (Hewitt and Wield, 1992; Lucas, 1993). Several studies such as Batra and Tan (2003), Lee (2001), and McElwee and Warren (2000) recognized low human resource capabilities as major constraint in SMEs development in developing countries.

Human resources in SME generally are weak in terms of their knowledge and skills of market analysis, marketing and product innovation as well as business planning and financial management. Therefore, the need is to develop capacity building programmes to improve the entrepreneurial and business management skills of human resources in SMEs and enhance the effectiveness of SMEs. Entrepreneurial competencies may, therefore, be developed by training and education (Gibb, 1986; Romjin, 1989). Firms with a literate and well-educated workforce are thus likely to be more efficient because of their greater capability to absorb and effectively utilize new technology (Hewitt and Wield, 1992; Lucas, 1993).

Low technological capabilities

Technology is the key for developing core competency in industry. Technological innovation is regarded as a tool for strengthening the competitiveness of a nation (Sikka, 1999). SMEs can largely improve their production abilities and profitability by improving employees' technological capabilities. Employees' technological capabilities can be improved in several ways like R&D initiatives, technology and know-how agreements with foreign and domestic firms, international contacts with foreign firms, and production experience or learning-by-doing (Griliches, 1984; Keesing and Lall, 1992; Mairesse and Sassenou, 1991; Pack, 1992; Pitt and Lee, 1981; Tan and Geeta, 1995; Westphal et al., 1979).

New technologies are rapidly emerging, technologies improves efficiency and enables greater production. Technological innovations are a source of profit for enterprises (Dean, 1980; Drucker, 1985). The potential benefits of modern technology and technological capabilities to SMEs are well known. According to Morse et al., (2007) technological capabilities benefit SMEs in several ways. Technologies enhance SME efficiency, reduce costs, and broaden market reach, both locally and globally.

Several studies (Lee, 2001; Romijn, 2001; Yusuf et al. 2003) recognized low technological capabilities as major constraint in SMEs development in developing countries. Unfortunately, absence of technological capabilities hinders and discourages SMEs from fully grabbing the benefits of new technologies, including, among others, lack of knowledge, resources and training. Public and private sector cooperation can play a critical role in addressing these concerns.

PUBLIC-PRIVATE PARTNERSHIP

Public-private partnerships (PPPs) represent cooperation among public institutions and private enterprises which intend to develop infrastructure networks and at the same time providing public services. The EU defines PPPs as a kind of collaboration linking public establishment and business world that intend to provide finance, structure, renewal, management or repairs of an infrastructure or intend to provide a service (Bovis, 2010).

On the other hand, the UN defined PPPs as new ways employed by the public institutions to form agreements with the private sector, who share their resources and their capability to accomplish projects within allocated budget and time, whereas the public sector maintain the task to make available such services to the public in a manner that assists the public and bring economic growth and upgrade the quality of life (Bult and Dewulf, 2007). Although there is no perfect definition of PPP concerning SME sector, but in the light of the preceding discussion we proposed the following definition for SME sector:

public-private partnership — for SMEs is an approach to addressing SMEs growth problems through the combined efforts of public, private, and development organizations.

There are three main kinds of PPPs, the concession; the contractual PPP and the institutional PPPs (Van, 2007). However, for SMEs growth and development in Pakistan the application of institutional PPPs can be more beneficial. As the institutional type of PPPs consist of instituting a new unit administered together by the public and private partners. Whereas, the job of such cooperative units is make certain the availability of money and the provision of a public services or an infrastructure project for the advantage of the public.

Governments due to the current internationalization of economics and politics are indulged in more interaction with the business world (Yanez et al., 2008). PPPs are a popular source of developing business sector in developing countries. PPPs have now become a defining characteristic of developmental policies. However, many developing countries governments are currently not committing themselves to this approach. PPPs bring public and private sectors together in long term partnership for mutual benefit. PPPs enable the Government to tap into the disciplines, incentives, skills and expertise which private sector SMEs have developed in the course of their normal everyday business. PPPs also help governments to release the full potential of the people, knowledge and assets in the public sector. Further PPPs enables the Government to deliver its objectives better and to focus on those activities, fundamental to the role of Government, which are best performed by the public sector - procuring services, enforcing standards and protecting the public interest.

In Pakistan and other developing countries, sustainable growth of SMEs can be achieved through public-private partnerships, where the government delivers the minimum standard of quality for products and services, the private sector brings skills and core competencies, while government, donors and businesses jointly bring funding and other resources. Such collaborations will be especially productive in promoting poverty alleviation through micro-finance, enhancing SMEs growth through partnerships as has been the case with polio eradication in Pakistan.

PPP is the most efficient and effective mechanism in number of ways. PPP create a sense of co-responsibility and co-ownership for the promotion of small enterprises. Through PPP, the advantages of the private sector such as dynamism, access to finance, knowledge of technologies, managerial efficiency and entrepreneurial spirit, are combined with the social responsibility, network of contacts, environmental awareness, local knowledge, and job generation concerns of the public sector.

PPPs are initiated for the formation of business research centers and industrial parks, or other institutes to provide human, financial and technical help for small enterprises. Such institutions are usually financed and

operated by both public and private sector.

Need and Importance of public-private partnership

Generally, several governmental officials, private enterprises, electronic and print medias and research scholars consider PPPs as useful and even a vital solution system for development in various areas (Flinders, 2005; Hertzberg and Wright, 2005; Mullin, 2002). The transfer of governmental systems at international level has put PPPs to the front position of growth and development methods (Newman and Verpraet, 1999; Stoker, 1999). PPPs usually assist development, availability of services and ensuring wise decisions systems through discussion and consultation between the international and the domestic mutually dependent stakeholders (Sagalyn, 2007; Nzimakwe, 2006; Hajer and Wagenaar, 2003; Goldsmith, 2001). Certainly, PPPs are co-operations between the private and public actors that are considered by the different stakeholders as largely supportive gains than can be accomplished by functioning individually or in conflict (Flinders, 2005; Stoker, 1999).

At times, the aim of a PPP could be to attain the goals of may be a specific economic growth, or PPPs can be formulated to influence current extensive progress goals like joint services provision, urban development or to enhance urban economy's competitive ability (Mullin, 2002; Watson, 1999).

Today, mankind is confronted with multifaceted worldwide dilemmas, like typical weather variations, poverty, or insufficient public services, have a mounting influence on businesses (World Economic Forum, 2005). One of the main issues our top leaders are facing at present is to discover innovative methods to utilize the innovative capacities, technical knowledge, networking expertise, and problem-solving abilities to deal with societal and environmental setbacks upsetting the civic world in corporation with public and not for profit organizations.

PPP is an approach to cooperation that contributes to the development of SMEs and economic advancement of developing countries through the vitality of the SME sector. Supporting the SME sector of developing countries has the potential to stimulate economic growth, reduce unemployment, accelerate poverty reduction, and improve living standards in developing countries. Unless economic activities in the SME sector advance, employment opportunities and incomes will remain limited, as a result, poverty will persist.

SME contribution in terms of tax revenues is also extremely important in developing countries. These taxes strengthen government's capacity to provide administrative services such as education, health, medical care, and welfare for societal development. In order to respond to international competitive environment which becomes more severe in today's economic

globalization, the competitiveness of local SMEs in developing countries needs to be improved. This improvement is not possible only through private sector's efforts. Governments in the developing countries also need to contribute and help SMEs in private sector to improve their competitiveness. To achieve the objective of improving competitiveness, a public private mixed approach like PPP is needed. PPP provides support for SMEs capacity development in a developing country and assistance that brings about competitiveness, intending for economic growth that benefits not only the entrepreneurial group but also the entire society of a developing country.

Many of the developing countries have not developed policies and systems to foster the SMEs development. The lack of technical skills and management know-how on a business-level has impeded the birth and growth of businesses. To overcome these obstacles, formulation of SME development policies and capacity development of persons in the public as well as private sector who formulate and implement the policies appropriately are essential.

Benefits of public-private partnership

PPPs can be benefited several ways in developing a well establish SME sector. First, PPPs can unite diverse actors' knowledge and skills in formulating effective decisions as well as results in developing effective strategies and policies (Lowndes and Sullivan, 2004). Secondly, PPPs can employ different diverse partners' particular resources and can devise improved problem solving techniques further successfully and competently than a single partner (Cohen, 2001). Lastly, employing wide-ranging methods to undertake complicated problems, PPPs can decrease the unintentional costs of narrowly identified, single-sided solutions (Keast et al., 2004). The other benefits of PPPs to SME sector development are numerous, especially for the developing countries. These include:

1. Sharing of each other's competence.
2. Cost of product development.
3. Faster product development.
4. Facilitation of product acceptability by consumers.
5. The efficient use of resources.
6. Availability of modern technology.
7. Better project design and implementation.
8. Improved operations combine to deliver efficiency and effectiveness.
9. Increases accountability and incentivizes performance.
10. Maintenance of required service standards.
11. Improves access to finance.

Hypothesis development

In developing countries, PPPs can promote stronger ties between public and private sector, intermediary

institutions, and research organizations, and hence they can exert some impact on growth and development of SMEs. Hence, we propose that:

H₁: Levels of partnerships between public and private sector are positively associated with SMEs growth and development (as defined in H1a, H1b and H1c).

H_{1a}: Levels of partnerships between public and private sector have positive influences on availability of finance for SMEs.

H_{1b}: Levels of partnerships between public and private sector have positive influences on improving technological capabilities for SMEs.

H_{1c}: Levels of partnerships between public and private sector have positive influences on improving human resource capabilities of SMEs.

MATERIALS AND METHODS

On the basis of literature review, the tentative model is represented in Figure 1. The figure indicates the relationships between different SMEs development factors and PPPs. It supposes that there are positive relationships between improving availability of finance, improving technological capabilities, improving human resource capabilities with PPPs and SMEs growth and development. Moreover, it reveals that partnerships between public and private sectors will have positive influences on SMEs growth and development.

Study design and data sources

The aforementioned three important constraints in growth and development of SMEs in Pakistan, viz. lack of access to finance, lack of human resource capabilities and lack of technological capabilities are the main constructs. Each construct was consisted of five corresponding measures. The measures are adjusted and applied to the specific context of Pakistani SMEs. The items of constructs are assessed with a 5-point Likert scale, with "1" being "very low" and "5" being "very high". The questionnaire was pre-tested for validity to a panel of experts in the related field.

The data were collected via a survey approach by personally managing questionnaires to 200 SMEs owners and managers, which were randomly sampled from SMEs located in the Faisalabad and Gujranwala regions of Pakistan. A follow-up visit was conducted to increase the response rate. After the second survey, 73 questionnaires were received, in which were 72 valid, with a response rate of 36%.

Measurement

In present study, respondents were asked to indicate the extent of public and private sector partnerships required for growth and development of SMEs (including areas like finance, human resources, and technological resources), and the items of constructs are assessed with a Likert scale ranging from 1 to 5 with the following equivalences, "1: very low"; "2: low"; "3: neutral"; "4: high"; "5: very high". The higher the score, the greater degree that the PPPs.

The sample

Sample selected was a mix of micro, small and medium enterprises.

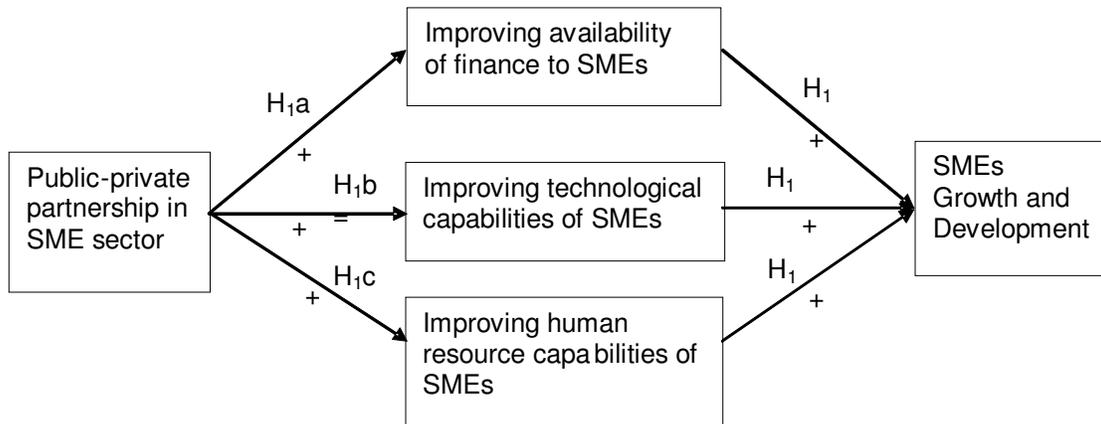


Figure 1. Conceptual model.

Around 87% of respondents were male, with the largest group for genders falling within the 20 to 30 age range. All respondents were workers in Pakistani SMEs. All respondents were educated to degree level, with 38% having achieved a master degree. In addition, Table 1 displays comprehensive profile of the respondents.

RESULTS AND ANALYSIS

The results in Table 2 indicate that if the SMEs are provided with the necessary supporting needs and abilities, like finance, technology and human resources, it would facilitate the SMEs in sustainable growth and development. Means and standard deviations for all the variables were calculated in order to get an idea about the direction of the respondents’ perceptions. Table 2 indicates the mean values and standard deviations for the studied variables. A low standard deviation for all the variables indicates reliability of the data and less variation in respondents’ perceptions. Also all mean values above three indicates the significance of the variables.

Each of the SMEs developmental factor’s mean scores was used to produce a correlation and linear regression analysis corresponding to our hypothesis. The results were used to find that data either support hypothesis or not. A majority of the respondents agree that PPPs have a major impact on every advancement or growth be it technology or otherwise. The SMEs’ growth rate is lower, probably due to lack of finance, technological capabilities, human resource capabilities and lack of effective PPPs in these areas as has been evident.

Overall, data supports hypothesis H1a, H1b and H1c. The results in Table 3 indicates that the relationship between improving availability of finance to SMEs and PPPs is the most significant, with improving technological capabilities of SMEs and PPPs being the next most important relationship. All the SMEs development related variables showed statistically significant correlation with PPP. These results concerning significance of H1a, H1b and H1c simultaneously support our research hypothesis

Table 1. Respondents’ profile.

Characteristics	N	Percentage
Age (years)		
20 -30	09	12.5
30-40	22	30.6
40-55	41	56.9
Gender		
Male	62	86.1
Female	10	13.9
Education		
Masters or above	26	36.1
Graduation	46	63.9
Type of organization		
SMEs	72	100

H₁. In other words, existence of such partnerships tended to increase SMEs growth and development. Indeed, it may be more beneficial for managers to learn how to develop PPPs that attempt to overcome obstacles created by lack of resources, such as finance, technology and human capital.

DISCUSSION

On the basis of a sample of 72 SMEs, this paper has empirically explored the relationships between public-private partnerships and growth and development of SMEs in Pakistan. The findings indicate that there are significant positive relationships between PPPs, and growth performance of SMEs, of which financial partnership

Table 2. PPPs assessments, mean and standard deviations.

Assessment	N	Mean	Standard deviations
Improving Availability of finance to SMEs and PPPs	72	3.97	0.786
Improving technological capabilities of SMEs and PPPs	72	3.87	0.710
Improving human resource capabilities of SMEs and PPPs	72	3.68	0.784

Table 3. PPP and SMEs growth and development: summary of regression analysis predicting SMEs' growth and development.

Variables	Adj. R ²	β
Improving Availability of finance to SMEs and PPPs	0.91	0.923*
Improving technological capabilities of SMEs and PPPs	0.73	0.841*
Improving human resource capabilities of SMEs and PPPs	0.64	0.826*

*p < 0.01.

is the most significant. Despite the progress so far, it is being widely recognized that public and private sectors need to capitalize on mutual strengths to accelerate the process of SMEs development and increase productivity so that the promised benefits reach all the stakeholders. During the past few years, several partnerships have been developed within and between public and private sectors with the objective of achieving these goals. While some of the PPPs have been able to deliver the anticipated results in the form of improved SMEs performance, others are yet to achieve the desired goals. In fact, successful partnerships in SME sector especially between public and private sectors are still rare because of several constraints. Some important constraints are different objectives of each sector, mutual mistrust, and negative perceptions.

The study highlighted some of the policy areas relevant for the success of SMEs where public-private cooperation appears to be the most suitable mechanism for support. It is generally accepted that technology provides growth in output and tangible improvements in efficiency and productivity. For this reason, access to appropriate technology, together with an effective technical and HR assistance programme, is vital for the development of small enterprises. But, as without financial resources, it has proven difficult to develop such programmes. The inability of SMEs themselves to access adequate technological and managerial resources, together with the modest efforts of governments, indicate the need for a PPPs.

RECOMMENDATIONS

Based on the aforementioned analysis, some policy recommendations and implications are given as follows:

these policy recommendations are vital for SMEs development not only in Pakistan but also other developing economies.

1. Both public and private sector should try to develop an overall conducive environment to entrepreneurship, innovation and SMEs growth. Promoting access to finance through regulatory changes; developing cooperation between public-private sectors financial institutions, and effective access to financial services, working and development capital, including innovative financial instruments to reduce the risks and transaction costs of lending to SMEs.
2. Government measures to promote SMEs should be carefully focused, aimed at making markets work efficiently and at providing incentives for the private sector to assume an active role in SME finance. Where necessary, banking systems should be reformed in line with market-based principles.
3. Governments should also act to improve awareness among entrepreneurs of the range of financing options available to them from officials, private investors and banks.
4. Micro-credit and micro-finance schemes play an important role in developing countries and efforts should be made to boost their effectiveness and diffusion.
5. Developing PPPs in education sector to increase the availability of skilful human capital, which is essential for SMEs growth and prosperity. Further enhancing cooperation between public and private sector educational and research institutions will also help improving technological capabilities of SMEs.
6. Develop an environment that supports the growth and dissemination of innovative technologies for and by SMEs to take advantage of the knowledge-based economy.

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