

## MODELLING KEY OBSTACLES HINDERING THE BUSINESS PERFORMANCE OF SMALL AND MEDIUM ENTERPRISES WITHIN THE MANGAUNG METROPOLITAN AREA IN SOUTH AFRICA

Benedict Motsamai Kareli<sup>\*</sup>, Eugene Tafadzwa Maziriri<sup>\*\*</sup>, Tinashe Chuchu<sup>\*\*\*1</sup>

<sup>\*</sup>Regenesys Business School

165 West St, Sandown, Sandton, 2031, South Africa

<sup>\*\*</sup>Department of Business Management, College of Business and Economics (CBE), University of Johannesburg  
PO Box 524, Auckland Park, 2006, South Africa

<sup>\*\*\*</sup>Division of Marketing, School of Business Sciences, University of the Witwatersrand  
1 Jan Smuts Avenue, Braamfontein 2000, Johannesburg, South Africa

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**Abstract:** SMEs play a crucial role in South Africa's economic growth, contributing to production capacity and job creation. This study focused on understanding the obstacles hindering SMEs and specifically examined the impact of financial, management, corruption, and infrastructure obstacles on SME performance in the Mangaung metropolitan area. Data was collected through an online survey from 240 SME owners/managers using a non-probability convenience sampling method. The results, analyzed using SPSS and SmartPLS, revealed that financial, management, corruption, and infrastructure obstacles have a negative effect on SME performance in the Mangaung metropolitan area. The findings have theoretical implications for entrepreneurship research and provide insights for SME managers to improve their entrepreneurial endeavors. The study also has policy implications, suggesting the need for revised credit access policies with lower interest rates for SMEs. Overall, this research contributes new knowledge to the entrepreneurship and small business management literature in the African context, which has been under-researched in academia.

**Keywords:** job creation, corruption, infrastructure obstacles, business performance, SMEs

**Abstrak:** UKM memainkan peran penting dalam pertumbuhan ekonomi Afrika Selatan, berkontribusi terhadap kapasitas produksi dan penciptaan lapangan kerja. Studi ini berfokus pada pemahaman hambatan yang menghambat UKM dan secara khusus mengkaji dampak hambatan keuangan, manajemen, korupsi, dan infrastruktur terhadap kinerja UKM di wilayah metropolitan Mangaung. Data dikumpulkan melalui survei online terhadap 240 pemilik/pengelola UKM dengan menggunakan metode non-probability convenience sampling. Hasilnya, dianalisis menggunakan SPSS dan SmartPLS, mengungkapkan bahwa hambatan keuangan, manajemen, korupsi, dan infrastruktur berpengaruh negatif terhadap kinerja UKM di wilayah metropolitan Mangaung. Temuan ini memiliki implikasi teoretis terhadap penelitian kewirausahaan dan memberikan wawasan bagi para manajer UKM untuk meningkatkan usaha kewirausahaan mereka. Studi ini juga mempunyai implikasi kebijakan, yang menunjukkan perlunya revisi kebijakan akses kredit dengan tingkat suku bunga yang lebih rendah bagi UKM. Secara keseluruhan, penelitian ini memberikan kontribusi pengetahuan baru pada literatur kewirausahaan dan manajemen usaha kecil dalam konteks Afrika, yang selama ini kurang diteliti di dunia akademis.

**Kata kunci:** lapangan kerja, korupsi, hambatan infrastruktur, kinerja bisnis, UKM

<sup>1</sup> Corresponding author:  
Email: [tinashe.chuchu@wits.ac.za](mailto:tinashe.chuchu@wits.ac.za)

## INTRODUCTION

Small and medium-sized enterprises (SMEs) are vital contributors to economic growth, particularly in developing economies (Ibrahim, Roslin & Mohamed, 2022). They play a significant role in economic activity in many economies (Burgstaller & Wagner 2015), including emerging economies (Abor & Quartey, 2010). SMEs are recognized as essential job creators, accounting for nearly two-thirds of jobs in Europe (Gama & Geraldes, 2012). They also foster innovation and entrepreneurship in markets (Bishop, 2018). However, SMEs face challenges as they compete with larger entities in the same markets (Bishop, 2018), highlighting the competitive nature of their business environment. Researchers have expressed positive feedback regarding focusing on small and medium-sized enterprises (SMEs) to promote economic growth and poverty alleviation. Studies in Kenya, Ghana, and Nigeria have examined the performance of SMEs in poverty reduction (Agyapong, 2010; Okpara, 2011). SMEs, including self-employed individuals and micro-enterprises, are recognized as playing a crucial role in poverty reduction, as they often employ individuals from the lowest income groups (Brainard et al. 2005). In the context of South Africa, SMEs contribute significantly to the country's GDP, aligning with the views of scholars who highlight their role in economic growth, job creation, innovation, and reducing poverty and inequality (Mafundu & Mafini, 2019; Mahadea & Kaseeram, 2018). Therefore, SMEs are crucial for improving living standards and ensuring societal stability (Cant, Wiid & Meyer, 2016).

Entrepreneurship has been a subject of extensive research, particularly in the context of developing economies, emphasizing the significance of entrepreneurial small and medium-sized enterprises (SMEs) (Amezcuca et al. 2013; Pamacheche, Chinomona & Chuchu, 2016). However, despite their importance in economic development, entrepreneurs face numerous barriers that hinder their survival and growth. Small business growth is particularly challenging in developing countries, with higher failure rates than in developed nations (Arinaitwe, 2006).

Therefore, this study explores the principles of the human capital theory. The concept of human capital, first introduced by Mincer (1958), has been a subject of debate, emphasizing the importance of human capital in business (Amin, 2018). In South Africa,

small and medium-sized enterprises (SMEs) success is significantly influenced by their human resources (Amin, 2018). According to the human capital theory, individuals who invest in education and training are likely to earn higher incomes (Jones, Macpherson & Thorpe, 2010). Therefore, considering the human capital theory, factors such as education level, field of education, previous entrepreneurial and business experience, and business skills can shape the type of venture undertaken.

This study explores and applies principles of the human capital theory. The concept of human capital, first introduced by Mincer (1958), has been a subject of debate, emphasizing the importance of human capital in business (Amin, 2018). In South Africa, small and medium-sized enterprises (SMEs) success is significantly influenced by their human resources (Amin, 2018). According to the human capital theory, individuals who invest in education and training are likely to earn higher incomes (Jones, Macpherson & Thorpe, 2010). Therefore, considering the human capital theory, factors such as education level, field of education, previous entrepreneurial and business experience, and business skills can shape the type of venture undertaken.

The slow development rate of SMEs in the Mangaung metropolitan area is a concern, as highlighted by Cant, Wiid, and Kallier (2015), who attribute it to a lack of aptitude, education, and capacity. In addition, Fatoki (2014) emphasizes that ineffective foundations, political instability, and everyday violence have a negative impact on SME survival. Dauda and Nyarko (2014) identify various obstacles hindering SME growth, including lack of financial resources, management experience, unfavourable location, non-conducive laws and regulations, poor infrastructure, corruption, low product/service demand, and external economic conditions. This research aims to address the gaps in the literature and provide insights into how financial, management, corruption, and infrastructure challenges affect the performance of SMEs in the region. In light of the abovementioned problem, the study investigates the challenges SMEs face in achieving optimum business performance.

This study addresses the existing gap in the literature by examining how financial, management, corruption, and infrastructure obstacles impact the business performance of small and medium-sized enterprises

(SMEs). Additionally, it contributes to the field by conducting quantitative analysis on this topic, with results that can be valuable for policymakers who are cognizant of the obstacles hindering SME performance in the economy. Consequently, policymakers can utilize the findings of this study to formulate enhanced policies aimed at supporting SMEs. The growth of SMEs can lead to job creation, poverty reduction, and improved living standards for both SME owners and their employees. Furthermore, this study will serve as a valuable resource for other scholars and researchers seeking to expand and advance this area of research. Therefore, this study's main objective is to determine the impact of financial, management, corruption and infrastructure obstacles on SME business performance within the Mangaung Metropolitan area in South Africa.

## METHOD

The target population of this study was SME owners or managers within the Mangaung metropolitan area. The historical evidence method was used as a comparative analysis, as Berg, Lune and Lune (2004) noted, to determine the required sample size. Data collection in the field was conducted over two months using an online survey. This research sample of 244 SME owners/managers was based on prior similar research Asah, Fatoki and Rungani (2015) used 300, Ogujiuba (2021) worked with 439, while Ncube and Zondo (2022) and Ogujiuba (2021) utilised samples of 127 and 156 respectively. Accordingly, a sample size of 244 was recommended for this study. Non-probability sampling using a convenience sampling technique was applied. The convenience sampling method was deemed not to compromise the quality of research because the sample comprised numerous SMEs facing similar challenges or conditions in a competitive market environment (Malhotra, 2019). The convenience sampling strategy was deemed appropriate due to its cost-effectiveness and timeous impact.

The questionnaire comprised questions about the respondents' demographic factors such as gender, age of the SME owner/manager, type of industry in which the business operates, age of the business, and level of education of the SME owner/manager. The scales for the present study were adapted from prior related research and tailored to fit the context of the present study.

The scale of obstacles, name, financial, management, corruption, and infrastructure was taken from Okpara and Wynn (2007) and Olawale and Garwe (2010), while that of business performance was taken from Atud (2017). This study's conceptual framework and hypotheses development is presented in the following section. A conceptual model was established to direct the empirical study on the basis of a synthesis of the convergent literature linked to the research variables, as illustrated in Figure 1.

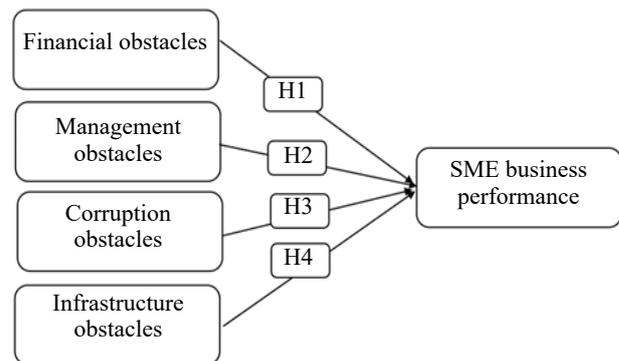


Figure 1. Conceptual framework

## Financial Obstacles and Business Performance

The performance of entrepreneurial small and medium-sized enterprises (SMEs) heavily relies on their financial resources, as they facilitate the opportunity for business expansion (Mohammed & Bunyaminu, 2021; Wang, 2016). Several studies have indicated that challenges related to funding, such as inadequate capital and financing, have a detrimental effect on the growth of entrepreneurial SMEs. These challenges hinder their development (Beck et al. 2005). The primary barriers for SMEs in securing loans from external sources include higher transaction costs associated with smaller loan amounts, lack of information, and difficulty meeting collateral requirements set by creditors (Beck et al. 2005). (Mishra et al. 2014). Overcoming these obstacles through improved access to finance, financial literacy, and supportive policies can enhance the performance and contribution of SMEs to economic development. Thus, the following hypothesis was formulated:  
H1: Financial obstacles have a detrimental effect on the performance of SMEs within the Mangaung metropolitan area

## Management Obstacles and Business Performance

The effectiveness of entrepreneurial small and medium-sized enterprises (SMEs) is influenced by the skills of their managers (Khan & Burki, 2020). Efficient management is crucial for organizational performance (Diniso & Chuchu, 2017). Several management-related issues, such as financing concerns, human resource challenges, leadership, technological issues, and a lack of expertise, have been identified as significant barriers to the development of organizations, particularly small enterprises. Inadequate record-keeping and a lack of managerial skills are highlighted as major reasons for the failure of SMEs, according to Tushabomwe-Kazooba (2006). The expansion of SMEs is negatively affected by a dearth of management capabilities, as indicated by Lussier (1996) and Mahadea (1997). Additionally, a lack of effective record-keeping and decision-making processes can result in a lack of transparency, hinder financial planning, and compromise overall business performance. Addressing these management obstacles through training programs, mentoring, and acquiring relevant expertise can enhance SMEs' performance, foster growth, and improve their competitive position in the market. Hence, the following hypothesis has been formulated:

H2: Management obstacles have a detrimental effect on the performance of SMEs within the Manganung metropolitan area

## Corruption Obstacles and Business Performance

Corruption has detrimentally impacted entrepreneurial small and medium-sized enterprises (SMEs) due to complex registration processes and insufficient anti-corruption measures (Williams et al. 2017). Budak and Rajh (2014) identify corruption as the most significant barrier to conducting business. Developing countries like Pakistan are particularly affected by widespread corruption, negatively impacting SMEs and their operations (Barkemeyer et al. 2018). The Global Competitiveness Report published by the World Economic Forum (2007) highlights corruption, government inefficiency, and bureaucratic hurdles as the primary barriers to SME success in Pakistan. Combating corruption through effective anti-corruption measures and promoting a transparent and ethical business environment is crucial for fostering SME success and contributing to overall economic development. Therefore, the following hypothesis has been formulated:

H3: Corruption obstacles have a detrimental effect on the performance of SMEs within the Manganung metropolitan area

## Infrastructure Obstacles and Business Performance

Infrastructure conditions play a vital role in determining the performance of entrepreneurial small and medium-sized enterprises (SMEs), and a nation's infrastructure is a crucial factor in either enhancing or hindering SME growth (Džafić et al. 2011). Stam (2015) supports the notion that infrastructure significantly predicts business performance. SMEs rely on infrastructure such as roads, energy, telecommunications, and other essential services for their development (Rehman et al. 2019). Conversely, the lack of adequate infrastructure has a detrimental impact on the revenue generation of enterprising SMEs (Obokoh & Goldman, 2016). In South Africa, power and energy infrastructure pose significant challenges for SME growth, with an inadequate transportation system costing the country approximately 6% of its GDP. Therefore, the following hypothesis has been formulated:

H4: Infrastructure obstacles have a detrimental effect on the performance of SMEs within the Manganung metropolitan area

## RESULTS

### Respondent Profile

Most of the respondents in the survey were between the ages of 26–35 years (80 respondents, 33.33%). It was followed by those aged 36–45 years (63 respondents, 26.3%), 18–25 years (57 respondents, 23.8%), 61 years and above (28 respondents, 11.7%), and 46–60 years (12 respondents, 5%). Regarding the industry in which the small and medium enterprises (SMEs) operate, the highest percentage (38.8%) of the 240 respondents work in the service industry (93 respondents). It was followed by the manufacturing industry (71 respondents, 29.6%), the construction industry (59 respondents, 24.6%), and the agriculture industry (17 respondents, 7.1%). Regarding the age of the businesses, 32.5% of the respondents (78 respondents) have businesses that are seven years and above, while 30.4% (73 respondents) have businesses that are 4–6 years old. Additionally, 23.8% (57 respondents) have businesses that are 1–3 years old, and 13.3% (32 respondents) have businesses that are less than a

year old. Regarding the level of education of the SME managers, 56.3% of the respondents (135 respondents) have secondary education, 23.3% (56 respondents) have no formal education, and 20.4% (49 respondents) have tertiary education.

### Statistical analysis procedure

The investigators used the Statistical Package for Social Science (SPSS) version 27 to evaluate the data about the demographic profile of the respondents. On the contrary, the latest software version of SMART-PLS 3.2.7 was used to analyse the proposed conceptual model. The statistical analysis performed in this study includes measures such as (1) measurement model – testing of reliability analysis and validity analysis, and (2) structural model analysis examining the path coefficients between observed coefficients.

### Measurement model analysis

The measurement model points out the associations among the constructs and the indicators: reliability, convergent validity, and discriminant validity.

### Convergent Validity

The first procedure applied in the measurement model analysis is the examination of convergent validity. Construct validity is the extent to which a research instrument (or tool) measures the intended construct (Heale & Twycross, 2015). Convergent is examined using standardised factor loading, composite reliability (CR), and average variance extracted (AVE). Furthermore, the AVE of latent constructs should exceed 0.50 (Hair Jr, Sarstedt, Hopkins & Kuppelwieser, 2014), and the accepted composite reliability values for each latent construct should be 0.70, 0.80 or above (Aguirre-Urreta, Marakas & Ellis, 2013). The initial specification of the measurement model shows that management obstacles (MO3) were below the 0.7-factor-loading threshold. As a result, that item was dropped, and the model was re-specified. The final results of the convergent validity analyses are presented in Table 1.

Table 1. Convergent validity of the measurement model

	Factor Loading	Composite Reliability	Average Variance Extracted
Financial obstacles (FO)		0.881	0.713
FO1	0.845		
FO2	0.818		
FO3	0.869		
Management obstacles (MO)		0.883	0.605
MO1	0.683		
MO2	0.640		
MO4	0.822		
MO5	0.859		
MO6	0.858		
Corruption obstacles (CO)		0.912	0.839
CO1	0.907		
CO2	0.925		
Infrastructure obstacles (IO)		0.856	0.665
IO1	0.813		
IO2	0.861		
IO3	0.771		
Business performance (BP)		0.873	0.580
BP1	0.718		
BP2	0.766		
BP3	0.817		
BP4	0.798		
BP5	0.701		

## Discriminant Validity

The second part of the measurement model analysis is the discriminant validity assessment. Discriminant validity refers to the extent to which a construct differs from one another empirically (Hamid et al. 2017). The heterotrait-monotrait ratio (HTMT) (Hair et al. 2021) techniques were used to assess discriminant validity.

### a) Heterotrait-monotrait ratio (HTMT) technique to confirm discriminant validity

HTMT is one of the latest methods used for examining discriminant validity in partial least squares structural equation modelling as stated by Henseler, Ringle and Sarstedt (2015). The various simulation tests conducted by Henseler et al. (2015) such as partial least squares, the Fornell-Larcker criterion and the examination of cross-loadings are the dominant approaches for evaluating discriminant validity. By means of a simulation study, we show that these approaches do not reliably detect the lack of discriminant validity in common research situations. We therefore propose an alternative approach, based on the multitrait-multimethod matrix, to assess discriminant validity: the heterotrait-monotrait ratio of correlations. We demonstrate its superior performance by means of a Monte Carlo simulation study, in which we compare the new approach to the Fornell-Larcker criterion and the assessment of (partial confirm that the HTMT criterion performs better than the common approaches to discriminant validity assessment, such as the Fornell-Larcker criterion and (partial) cross-loadings, as these techniques are sometimes not capable of spotting a lack of discriminant validity. The HTMT technique uses either of two methods to evaluate discriminant validity: (a) as a criterion or (b) as a statistical test (Yusoff et al. 2020). Assessing HTMT as a criterion includes comparing it with a stated threshold. If the value of the HTMT is above this threshold, it can be said that there is a lack of discriminant validity (Henseler et al. 2015) such as partial least squares, the Fornell-Larcker criterion and the examination of cross-loadings are the dominant approaches for evaluating discriminant validity. By means of a simulation study, we show that these approaches do not reliably detect the lack of discriminant validity in common research situations. We therefore propose an alternative approach, based on the multitrait-multimethod matrix, to assess discriminant validity: the heterotrait-monotrait ratio of correlations.

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## Hypotheses Testing

The results of the PLS-SEM of the structural model analysis are presented in Table 3 and depicted in Figure 2.

## Financial Obstacles and Business Performance

The analysis of the results revealed that financial obstacles have a positive and significant impact on the business performance of SMEs ( $\beta = 0.192$ ,  $p=0.002$ ); therefore, H1 is empirically supported. Entrepreneurial SMEs have difficulty obtaining finance from banks because they lack loan collateral. The findings of this study are consistent with previous research conducted by Okpara and Wynn (2007), indicating a similar outcome. Additionally, the results align with the findings of Hussain et al. (2018), who discovered that financial literacy and reduced monetary costs positively impact the growth of entrepreneurial SMEs. The literature also supports this study's findings. Mishra et al. (2014) highlighted that firms require funding for investment purposes, and the absence of comprehensive financial records hinders SMEs' ability to obtain necessary funds, contributing to their perception of riskier than larger firms.

Table 1. Convergent validity of the measurement model

	Business performance (BP)	Corruption obstacles (CO)	Financial obstacles (FO)	Infrastructure obstacles (IO)	Management obstacles (MO)
Business performance (BP)					
Corruption obstacles (CO)	0.814				
Financial obstacles (FO)	0.732	0.600			
Infrastructure obstacles (IO)	0.673	0.445	0.641		
Management obstacles (MO)	0.589	0.474	0.496	0.621	

Table 3. Summary of the results of the hypotheses testing

Hypotheses	Path coefficient	T Statistics	P Values	Decision
H1 Financial obstacles → Business performance	0.192	3.048	0.002	Accepted
H2 Management obstacles → Business performance	0.096	1.988	0.007	Accepted
H3 Corruption obstacles → Business performance	0.543	9.326	0.000	Accepted
H4 Infrastructure obstacles → Business performance	0.197	2.787	0.005	Accepted

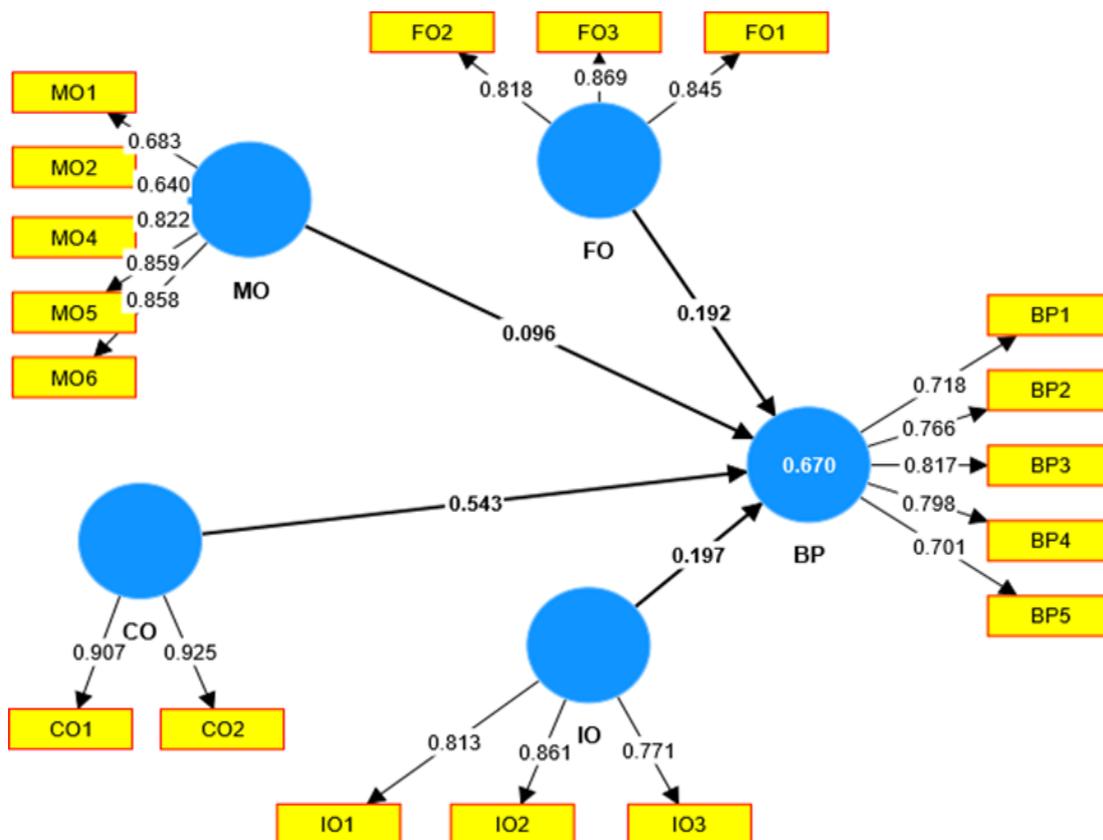


Figure 2. Structural model analysis with path coefficients and R2 estimates

## Management Obstacles and Business Performance

The analysis of the results revealed that management obstacles have a positive and significant impact on the business performance of SMEs ( $\beta = 0.096$ ,  $p = 0.007$ ); therefore, H2 is empirically supported. These results are consistent with the idea that managerial skill deficiencies are the principal hindrance to business performance. Due to a lack of management experience and expertise, entrepreneurial SMEs perform poorly and fail (Tushabomwe-Kazooba, 2006). Bad management skills, such as those in bookkeeping, marketing, inventory management, and resource management, are the root of poor business performance. These challenges have led to the closure of companies and play a substantial role in business failure. The research by Khan and Burki (2020) further emphasizes managerial skills' influence on entrepreneurial SMEs' performance. This finding is supported by existing literature, as highlighted by Lussier (1996) and Mahadea (1997), who observed that a deficiency in management skills has a detrimental effect on the growth of SMEs.

## Corruption Obstacles and Business Performance

Empirical evidence was also found in this research that corruption obstacles have a positive and significant impact on the business performance of SMEs ( $\beta = 0.543$ ,  $p = 0.005$ ); therefore, H3 is empirically supported. The fact that corruption has an impact on SMEs' growth and development is one of the main issues with it. This study's results align with those of Hashi and Krasniqi (2011), who discovered that SMEs with an entrepreneurial spirit do poorly when corruption exists. This finding is corroborated by previous studies, as indicated by Budak and Rajh (2014), who highlighted that corruption is the primary obstacle to conducting business. Similarly, the results of this study are consistent with the findings of Barkemeyer et al. (2018), which revealed that corruption is prevalent in developing countries like Pakistan, adversely affecting SMEs and their operations.

## Infrastructure Obstacles and Business Performance

This study also discovered that infrastructure obstacles have a positive and significant impact on the business performance of SMEs. Therefore, H4 is accepted ( $\beta = 0.197$ ,  $p = 0.005$ ). The cost and performance of SMEs are highly impacted by the state of the infrastructure, which has become a significant problem for South Africa's

entrepreneurial SMEs. The research conducted by Obokoh and Goldman (2016) aligns with the findings of this study, as both studies demonstrate that inadequate infrastructure has a negative impact on the profitability of entrepreneurial SMEs. These results are consistent with existing literature, as noted by Kubičková et al. (2017), who highlighted that infrastructure-related challenges pose a more significant problem for SMEs operating in rural areas.

## Managerial Implications

Managerial implications emerged from the findings. Firstly, the study established that financial obstacles hindered the performance of SMEs. It implies that policymakers and captains of industry should make every effort in identifying and addressing the financial hurdles that SMEs face in entering and remaining relevant in a market. It could involve financial incentives in the form of tax breaks for established corporations that support SMEs. Another implication arose from the observation that corruption hinders business performance. It could be handled at both the government and corporate levels, with the government enforcing tighter controls on officials responsible for supporting SMEs and corporations implementing more severe punishments on corrupt individuals. It could act as a deterrence to corruption.

## CONCLUSIONS AND RECOMMENDATIONS

### Conclusions

This research study provides valuable insights into the challenges faced by small and medium-sized enterprises (SMEs) in the Mangaung metropolitan area of South Africa. The findings demonstrate that financial obstacles, management obstacles, corruption obstacles, and infrastructure deficiencies have a detrimental impact on the business performance of SMEs. These results highlight the need for policymakers and stakeholders to address these obstacles to support the growth and development of SMEs. The research contributes to the academic field of entrepreneurship by enhancing our understanding of the relationships between finance, management, corruption, infrastructure, and business performance. The findings offer theoretical implications and insights that can guide future research. Furthermore, the study has important implications for policy development. The current policies on credit

access can be re-evaluated, focusing on reducing interest rates for SMEs. By addressing the identified obstacles, policymakers can create a more conducive environment for SMEs to thrive and contribute to the region's economic growth. Overall, this research adds new knowledge to the existing body of literature on entrepreneurship and small business management in the African context. It sheds light on SMEs' unique challenges in the Mangaung metropolitan area and emphasizes the importance of supporting their entrepreneurial endeavours.

## Recommendations

Based on the literature analysis, and more specifically, in light of the empirical research findings, the following recommendations are offered. It is recommended that the Government of South Africa should support SMEs by providing relief measures and lower collateral demands for credit finance. Reducing loan costs and enhancing financial literacy skills for SME executives are also recommended to promote their activities. Also, maintaining low inflation and lowering interest rates can positively impact SMEs' performance, while anti-corruption efforts should continue. Improving infrastructure, especially the road system, electricity rates, and telecommunications, is essential for SME growth. Moreover, offering management training and workshops on record-keeping, marketing, and accounting will enhance the overall effectiveness of entrepreneurial SMEs. Encouraging guidance from established companies and hiring competent employees are also crucial for SME success.

This study has some limitations that must be considered, even though it has significantly contributed to various fields. Future research should continue exploring and increasing knowledge in small business management. With a moderately small sample size, the findings cannot be summarised decisively, even though various statistic questions were utilised to decide how extensive the sample of the target population should be. In future research, a larger population of SMEs should be examined. An examination of SMEs from different provinces, for example, the Eastern Cape province of South Africa, where poverty is at its zenith, would be advantageous. As this research was quantitative, future research could utilise triangulation techniques to avoid this bias. A further limitation is that a non-probability convenience sampling technique was employed in the study. As a result, even though several demographic

questions were used to determine how representative the sample was of the defined target population, one should be cautious when generalising the results of this study over the entire population. Finally, it is imperative to note that the abovementioned limitations do not necessarily refute the contributions of this study but open further avenues for future research.

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