

# FACTORS AFFECTING THE GROWTH OF SMALL AND MEDIUM-SIZED ENTERPRISES

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**Abstract:** *Today, the role of Small and Medium-sized Enterprises (SMEs) in economic development, industry and innovation in the field of business, Gross Domestic Product(GDP) and entrepreneurship is clear to all people; in a way that Global Entrepreneurship Monitor(GEM) measures the rate of entrepreneurship in countries based on the rates of new business births and deaths. These businesses which account for 80 percent of the world's economic growth do not undergo all the stages of life cycle and a high percentage of them fail during the early years after establishment.*

*During the previous decade, SMEs' failure in transforming into established businesses has been one of the major concerns. Thus the aim of this narrative and issue review is to study the factors affecting SME's from various researchers' points of view and to provide a comparative table based on similarities and differences in order to summarize the previous studies and finally provide a trifurcation schematic integrated model given the new point of view to facilitate the simplification of factors affecting the growth of SMEs.*

**Keywords:** *SMEs, Entrepreneurship, Growth, Comparative Approach*

## 1. INTRODUCTION

SMEs are the best resort for entrepreneurial activities (Moghimi and Ahmad pour Dariani 2008) and it requires them to be able to undergo their life cycle and to be competitive against large established corporations in the respective industry, and do not lose their growth and competitiveness power shortly after establishment and avoid liquidation. However, most new small businesses are more disadvantaged than their large established competitors and are more prone to high failure rate (Lee, Kelley, Lee, & Lee, 2012).

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During the past decade, SMEs' failure in turning into large corporations or multinational companies (MNCs) in regional and global level have been one of the major concerns. However, the growth model of SMEs has been less studied in the literature (JK Li and Hua Tan 2004). In fact, the growth of SMEs is a complex process. This process is influenced by internal factors, i.e. firm-specific features, as well as external factors, i.e. industry-specific or macro-economic factors (Bullock, Cosh, Fu, Hughes, & Yang, 2004).

Davidson believes that all factors in the growth of small and medium-sized businesses can be classified into three categories determining the capability, need and opportunity (Davidson & Wiklund, 2006). Some researchers believe that the company's growth is determined based on the population ecology, which means that the environment sare variable in terms of dimensions such as dynamics, heterogeneity, hostility and munificence, and these external factors may determine the growth of companies more than the incentives and strategic actions of managers (Carroll & Hannan, 2000; Davids son & Delmar, 1997, 2001; Jovanovich, 1982). Given that some companies survive and continue their activities, the question is: ' what factors can help the growth of small and medium-sized companies?' In fact, given the dispersion of factors influencing growth, researchers seek to study the concept of growth in SMEs, growth parameters, factors affecting the growth of the SMEs from different viewpoints and SMEs growth paths, using an overview of about 50 works related to the growth of SMEs, and to portray the factors affecting the growth of SMEs in the form of a trifurcation model.

## **2. THE CONCEPT OF GROWTH IN SMES AND ITS INDICATORS**

Growth is a phenomenon which necessarily happens over time. Therefore, a company's growth must be studied over time, and the predictors' recognition and evaluation precedes the assessment of such outcomes as changes in size. Considering change-in- amount, growth can be assessed using a range of various indicators including sales, recruitment, assets, physical output of market share (Davids son, 1991). For some companies, growth is manifested in sudden increase in sales, without considerable changes in assets or recruitment, while for other types of companies; it results in balanced growth in assets, sale and recruitment. The set of standard versions of all three indicators the oretically shows the growth concept. If only one indicator is used, the results will be weak and probably wrong. Instead, the underlying theory predicts that specific indicators are related to the growth in sales and market share, while other indicators are relevant to the impact of growth on employment and profit.

In this case, the key is to analyze growth indicators separately. If only one indicator is used and the plan is multi-industry or inter-industry, then there is a consensus that growth of sales should be the preferred option. According to Barkham, Gudgin, Hart and Hanvey(1996) this is an indicator that is used by the owner-managers of small and medium-sized businesses. This indicator reflects short and long term changes and is easily achievable. In addition, researchers such as Barkham et al. (1996) stated that the growth of sales is the most common performance indicator among entrepreneurs. Growth process probably begins due to an increased demand for products or services. This means that an increase in sales will result in the acquisition of additional resources, such as employees or machines. In calculating the market share, the concept of "market" may be unclear. The difference in market share may be irrelevant to small companies, and the comparison of share for companies in different markets can be untenable. The value of assets is different based on the amount of capital of industries, and evaluating the companies whose key asset is knowledge is difficult (Delmar et al. 2003). On the other hand, there is a widespread desire to hire new recruits. From this perspective, the growth of employment and employees is another major aspect of growth. In the process of rationalization, it is possible that employees are replaced by capital reserves. In other words, to some extent, there is an inverse relationship between capital reserves and personnel growth. Therefore, assets are another important aspect of growth. Measuring growth based on assets is often problematic in the service sector, which is mainly an accounting issue.

In the selection of appropriate indicators, in addition to the experimental nature, theoretical considerations are also necessary, and the appropriateness of each of these dimensions is contingent and depends on the analysis unit. For a growth-oriented entrepreneur, enterprise is the wealth accumulation cycle. In fact, when the individual is the unit of analysis, the growth of assets may become a priority. When entrepreneurs plan to use sales growth as an indicator of performance, this aspect is as attractive as individual as the unit of analysis. Recruitment-based growth may be secondary in this case. However, what is important is that the aim is almost never the growth of staff (recruitment) alone (Davidson & Wiklund, 2006).

Davidson et al. have identified four theoretical perspectives that are categorized as growth factors or processes. They include resource-based view, motivational perspective, strategic compliance and configuration perspective. In resource-based view, the focus is on the company as a set of resources and activities based on which the company can work. So, in this

view, growth refers to the development of business activities which will be possible by a unique composition or arrangement of resources. The motivational perspective to companies' growth focuses on the individual and his/her actions. From the perspective of strategic compliance, a strategic option may be reasonable if it leads to the growth of overall business activities. Configuration perspective deals with the process of growth. It focuses on managerial problems and how they are dealt with during the growth process through development stages (Davidson & Wiklund, 2006, p. 46).

Wiklund integrated three theoretical perspectives in his model: resource-based perspective, motivational perspective and strategic compliance. In this model, strategy as an entrepreneurial orientation (EO) was operationalized. It is assumed that resources, motivations, and environmental features have an indirect impact on growth through strategic adaptation, while entrepreneurial orientation is directly associated with growth. The results showed that all variables listed above affect growth. However, in empirical evaluation, motivation and environment were attributed to direct impacts coupled with their impact through strategy. Subsequent analyses by Davidson showed that the entrepreneurial orientation performance occurs over time. Hence, strategy has the strongest and most direct impact on growth, which can be an important attachment to Davidson's conclusions (1991). While Davidson and Wiklund's models embrace many factors and mediated effects, they do not include interactive/mutual effects which are important in recent researches (Davidson & Wiklund, 2006, p. 56).

## **2.1 Factors affecting SMEs' growth from the perspective of the industrial economy, industrial capital and governance structure**

An approach in industrial economy literature is developed based on the size and the age which emphasizes on the extreme skewness of growth rate patterns. This approach considers that only a number of companies grow constantly and rapidly. The results suggest that the universe is characterized and described by industries that - during maturity stage - are full of several large companies and an extensive range of smaller ones. Such a distribution can be created by the company's growth models that assume growth as random. In this model, past growth does not influence future growth. Also, some companies are successful and some are not.

Only sustainable growth is consistently successful. A version of this process, 'the law of proportional effect', expresses that the size of company in the future is the size of current period plus a random variable. The mean

and variance of the company's growth rate are independent of the firm size and they are also not fixed in the growth of the company. Generally, studies show that although many random factors are involved in the growth of small businesses, law of proportional effect is not executed effectively. In particular, small companies may grow systematically compared to the rest of companies.

The new theory of growth suggests that investment in human capital plays a major role in promoting growth and competitiveness. In addition to physical capital and labor supply, growth is a function of investment in human capital. Education and training increase the absorption capacity of companies, as the costs of research and development facilitate innovation and benefit from external consultations and other activities that have access to new ideas such as knowledge transfer and overflow, cooperation and exports. Management and governance structure are key factors that shape a company's growth process. When a small company starts to grow, management capacity requirements to deal with complex strategic and operational managerial tasks also increase along with the development of its products. Therefore, the competency of management and SME's management structure can be a key effective factor in the growth of SMEs (Table 1).

**Table 1.**  
**Perspectives and Assumptions Regarding Growth Factors**

<i>Approach</i>	<i>Factors affecting growth</i>	<i>Assumption</i>	<i>Perspective</i>
Internal/external	Random factors	Growth randomness	Industrial economy perspective
Internal	Education and training	Growth is a function of investment in human capital	Human capital perspective
Internal/external	<ul style="list-style-type: none"> <li>• adopting the structure</li> <li>• decentralized ownership</li> <li>• Business consultancy and support by government</li> <li>• macro-economic environment</li> <li>• management competency</li> </ul>	Sustainable growth requires appropriate management structure	Management and governance structure perspective

To realize sustainable growth, it is necessary to adopt appropriate management and organizational structures that are appropriate for implementing strategy. In addition, management and governance structure may affect strategic decisions such as exports, innovation, cooperation and education, which are important factors in firm's involvement in acquiring competitive advantage. It is also stated that the tendency to depreciate ownership and to adopt decentralized ownership structure is desirable for SMEs growth, so that it results in more application of external financing. Thus a variety of managerial, ownership and organizational variables are used in the analysis. It has been said that SMEs' access to external financing is a major constraint to the irgrowth, and growth potential can only be realized if a company has adequate financial resources to support the development process. In addition, it is possible that SMEs have specific problems in their judgments about the quality or effectiveness of education, or the fear that if they teach others, they will easily involve their employers. Moreover, they may not have the resources required for effective access to sufficient information in order to choose the best business practices. Business consultation and support from the government can be important ways to improve SMEs' performance by bringing external knowledge concerning SMEs' development issues. Finally, the market demand and competitive pressure affect company's growth potential. Also, the industry that the company belongs to as well as the macroeconomic environment may affect changes in demand and growth patterns and the activities of competing companies (Bullock, Cosh, Fu, Hughes, & Yang, 2004).

In a study conducted in Pakistan, factors affecting growth, marketing, management skills, finance, government support and education were identified (Abrar-ul-haq, MohdJali, andMdNurul Islam 2015). In a research conducted by Cassia and Colombelli in 2010,these factors included proactivity, risk-taking status and investment to grow (Cassia and Colombelli 2010). Also, any changes in sales or recruitment are attributed to the variability of innovation, risk-taking and the age of the firm (Palalic and Busatlic 2015).

On the other hand, other researchers showed that organizational structure (formalization, centralization and separation), business strategy (cost leadership strategy and focus strategy), supply structure (supplier power and technological confusion) and government policies (financial, tax, customs and export incentives) are among the factors related to the growth of small and medium-sized businesses in the city of Ardebil (Lotfi, Nayebzadeh, and Dehgan Dehnavi 2014).Furthermore, another research

showed that SMEs growth in Algeria is restricted by a number of interrelated factors, including environmental factors, which are beyond the control of SMEs, and internal factors. External factors include legal frameworks, access to external financing and human resource capacity, and internal factors include entrepreneurial characteristics, management capacities, marketing skills and technological capacities (Benzazoua Bouazza, Ardjouman, and Abada 2015). Likewise, cash flow and debt, the amount and intensity of research and development and labor productivity are regarded as the factors influencing the growth of SMEs (Mac a~s Nunes, Gonc alves, and Serrasqueiro 2013). Perren (1999) identified four groups of factors affecting the growth of small businesses: the owner's growth motivation, expertise in managing growth, access to resources, and demand. According to the mixed model of Ghoshal (2002), Davidsson (2006), factors affecting the growth of SMEs are: entrepreneurial judgment with the ability of entrepreneurial knowledge, growth motivation and recognition opportunity, as a need, and organizational capability with the ability of accumulated capacity and resources, environmental opportunities and resources, and economies of scale and economies of growth, as a need (Prenyi, Selvarajah and Muthaly, 2008). It may be thought that growth is a standard. However it is not true. Most companies start small, live small and die small, without ever being on a significant growth curve. One of the main reasons is that most new businesses (startups) are imitative businesses in mature industries and serve local markets. As a result, they do not have much growth potential. Regardless of the potential, it is also very important to recognize that most business owners have ambitions and a great desire to grow their companies. But is it the tendency of managers to grow that matters, or the external forces that determine the growth of the company based on the population ecology?

Environments are variable in terms of dimensions such as dynamics, heterogeneity, hostility and munificence, and these external factors may determine the growth of companies more than managers' motivations and strategic initiatives. For example, it has been shown that high-growth companies are mostly in more dynamic industries (Carroll & Hannan, 2000; Davids son and Delmar, 1997; Jovanovich, 1982). While in highly innovative industries the rate of failure is also high for newcomers, Audretsch(1995) showed that for those companies that seek to survive and also grow in the early years, the rate of failure is even higher in the following years. Companies grown in stagnant industries often grow in niche markets which seem to be similar or related to Penrose's (1959) argument about opportunities for small businesses to enter and grow in what he calls'

interstices' of the economy. While the positive impact of dynamics (increase in dynamics, in this case) has been approved, Wiklund(1998) found the weak negative impact of environmental hostility (and not the impact of heterogeneity). He said it is likely for other environmental conditions related to the aspects to be contradictory, so that the overall dimensions can fluctuate towards zero or any other directions (depending on the specific context).

For instance, environmental munificence may not only facilitate growth capacity building, but may also attract more newcomers who compete for the market potential for the growth. It is said that in a symmetric markets, entrepreneurial opportunities that will exist in a market are more likely to generate demand (for products in related areas). Also, skewness indicates that the market is fragmented into small untapped segments whose development seems difficult for the individual companies. Thus the evidences show that growth is broadly determined externally.

Consequently, there are some evidences to suggest that owner-managers' growth motivation, goals and communicated vision have direct impact on the company's growth, as does the company's strategic orientation. The reasonable conclusion is that growth, to a considerable extent, it a matter of willingness, however we can not ignore facilitating factors and fundamental barriers in the environment. Also the extent to which companies have control over their own destinies are different from a company to the other and in different environments. For example, the image generated by DImar & Davidsson's(1997) research is that companies defined as high-growth companies find their path to achieve their growth targets almost regardless of environmental conditions, while it seems that the growth of most companies fluctuates up and down with economic development.

A severe downturn and the revival of 'other companies' first reduces and then increases recruitments. As long as companies' growth is defined on such a basis, it is not surprising that the curve for 'high-growth companies' is higher on the growth axis and never shows negative values (Davidsson, Achtenhagen, & Naldi, 2000).

## **2.2 Growth paths for small and medium-sized businesses**

### ***Natural growth VS. Acquisitions:***

In the smallest companies, almost all the growth is organic / natural. Larger companies, based on the overall employment growth, have in fact withdrawn from organic conditions. McCann (1991) states that dominance of



internal venturing among young and relatively inexperienced companies, as well as companies who barely have the resources to grow through acquisitions, is not attractive., Kraemer and Venkataraman (1997) empirically focused on companies that had some initiatives at the beginning, and found that they are more likely to be funded internally than through acquisitions and strategic alliances. Typically entrepreneurial growth is considered as an organic growth which is defined as the internal development through extending existing operations and internal processes and product innovation. On the other hand, researchers have reported that acquired growth creates long-term entrepreneurial benefits that might not be generated through organic growth or greenfield (Vermeulen and Barkema(2001), Wiklund and Shepherd (2005).In fact, under certain circumstances, acquired growth can be a response to growth of supplies, strength and simplicity. Acquisition can revive a company and improve its ability to predict or provide adequate response to changing external conditions.

Cultural and managerial stimulation and mobility as a result of growth acquisition and learning and subsequent integration eliminate comprehensive rigidity and weakness, resulting in an organization which is more appropriate for pursuing entrepreneurial activities. Researchers believe that these positive results are only attainable when growth acquisition is accompanied by developing its capabilities, namely accumulation, storage and use of new organizational knowledge (Salvato et al., 2007).

### ***Internationalization***

Internationalization is another path of growth which is often based on unions and networks. Many studies clearly have established the links between networks and firms' growth(DonckelsandLambrecht, 1995; Hansen, 1995; Jarillo, 1989).The relationship between networking and internationalization is based on the establishment and maintenance of relationships needed with partners, customers, suppliers and governments (Welch and Welch 1996).Internationalization is no longer an alternative, but is an essential prerequisite for growth of small businesses. This is also true for the geographical expansion. Researchers interested in international entrepreneurship mainly focus on what is called 'International New Ventures' (INVs), or 'high-growth new ventures" (Salvatoetal. 2007).

### **3. DISCUSSION**

The growth of small and medium-sized businesses is a complex process. This process is influenced by internal factors, i.e. specific features of the company,

as well as external factors, i.e. industry specific factors (Bullock, Cosh, Fu, Hughes, and Yang 2004). The reasonable conclusion is that growth, to a considerable extent, is a matter of willingness, however we can not ignore facilitating factors and fundamental barriers in the environment. Also the extent to which companies have control over their own destinies are different from a company to the other and in different environments. (Davidsson, Achtenhagen, & Naldi, 2000) Experts in this field have suggested various views about the factors influencing the growth of small and medium-sized businesses, which have been briefly collected in Table 2.

**Table 2.**  
**the summary of the factors influencing the growth**  
**of small and medium-sized businesses**

<i>Researchers</i>	<i>The factors influencing the growth of small and medium-sized enterprises</i>
Bullock et al, 2004	Internal factors (company-specific features, such as competency management, investment in human capital) External factors (industry-specific factors and governance structure)
Perdavidson, 2006	Finance, business operations, strategic choice and individual motives of owner-manager
Carroll & Hannan, 2000	Population ecology theory: the environment and its characteristics (dynamics, heterogeneity, hostility and munificence)
Davidson, Achtenhagen & Naldi, 2000	Growth motivation of owner-manager and the communicated vision
Davidson & Wiklund, 2006	Ability, need and opportunity
Wiklund, 2006	Entrepreneurial orientation
Kutllovci, 2012	Strategy, strategic management, and adopting a vision
Bartlett & Ghoshal, 2000	Clear strategy, desired leadership and eagerness to learn
Ansoff, 1965	Business plan model
Hodgetts and Kuratko, 1998	The number of innovations
Eugene et al. 2003	The owner's ability (to remain an entrepreneur while adopting managerial attributes)
Gibb and Dyson, 1984	Strategy and decision making models
Salvato et al., 2007	Learning, developing formal tools to support growth (financial management, accounting and operations control), internalizing lessons learned

Table 2 Contd...

Man, Lau & Chan, 2002	Internal factors and individual characteristics of the entrepreneur
Abrar-ul-haq et al., 2015	Marketing, management skills, finance, government support and education
Cassia & Colombelli, 2010	proactivity, risk-taking and investment to grow
Palalic & Busatlic, 2015	Variability of innovation, risk-taking and the firm's age
Lotfi et al.,2014	Organizational structure, business strategy, supply structure, government policies
(Benzazoua Bouazza, Ardjouman, & Abada, 2015)	legal frameworks, access to external financing, human resource capacities, entrepreneurial characteristics, managerial capacities, marketing skills and technological capacities
Wakee, Van Der Veen & Eurlinges, 2015	Brand awareness

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The following table sporadically describes the factors each of which analyze growth of small and medium-sized businesses from a different viewpoint. These factors include marketing, management skills, finance, government support and training (Abrar-ul-haq, MohdJali and MdNurul Islam 2015), proactivity, risk-taking status and targeted investment (Cassia and Colombelli 2010), variability of innovation, risk-taking and firm's age (Palalic and Busatlic 2015). On the other hand, other researchers showed that organizational structure, business strategy, supply structure and government policies (Lotfi, Nayebzadeh, and Dehgan Dehnavi 2014), business activities itself, business owner-manager's growth motivation (Perdavidson2006), entrepreneurial orientation ((Wiklund 2006,) strategy and strategic management, business environment, number of innovations, and etc. are factors that are associated with the growth of small and medium-sized businesses.

In one of the previous studies, brand awareness was emphasized as a feasible and profitable growth path after the new venture establishment and entry into foreign markets (Wakkee, Van Der Veen, and Eurlinges 2015). Each source has its importance at various stages. Tangible resources, such as cash and physical resources are necessary for start-ups, while intangible resources are the priority in the maturity stages and success. In order to gain competitive advantages, SMEs should completely develop their inimitable

and unique resources, such as brands, technology, culture and reputation (Fang Li 2010).

SME susedifferent forms of growth: geographic expansion both domestically and internationally, launching related and unrelated new products, improving products, clients' retention and attracting new customers (Barbero Navarro, Casillass, and Barringer 2012). Empirical researches indicate that company's growth is determined not only by traditional features such as size and age, but other firm-specific factors, such as indebtedness, internal financing, future growth opportunities, process and product, innovation and organizational changes, also affect SMEs' growth (Mateev and Anastasov 2010).

The researchers sought to categorize these factors based on a new perspective in the form of three branches: structural, content (behavioral) and contextual (environmental). Organization branch represents all physical and inhuman elements, factors and conditions of the organization that regularly shape the physical and substantial form of the organization. The content (behavior) means human in human relations in organization, which forms the core content using interconnected behavioral forms, informal relations and specific patterns. Contextual branch means all conditions and environmental factors that are external to the organization, surround the organization and constitute the main system or super-systems of organization (Mirzaee, 1376).

#### **4. CONCLUSION**

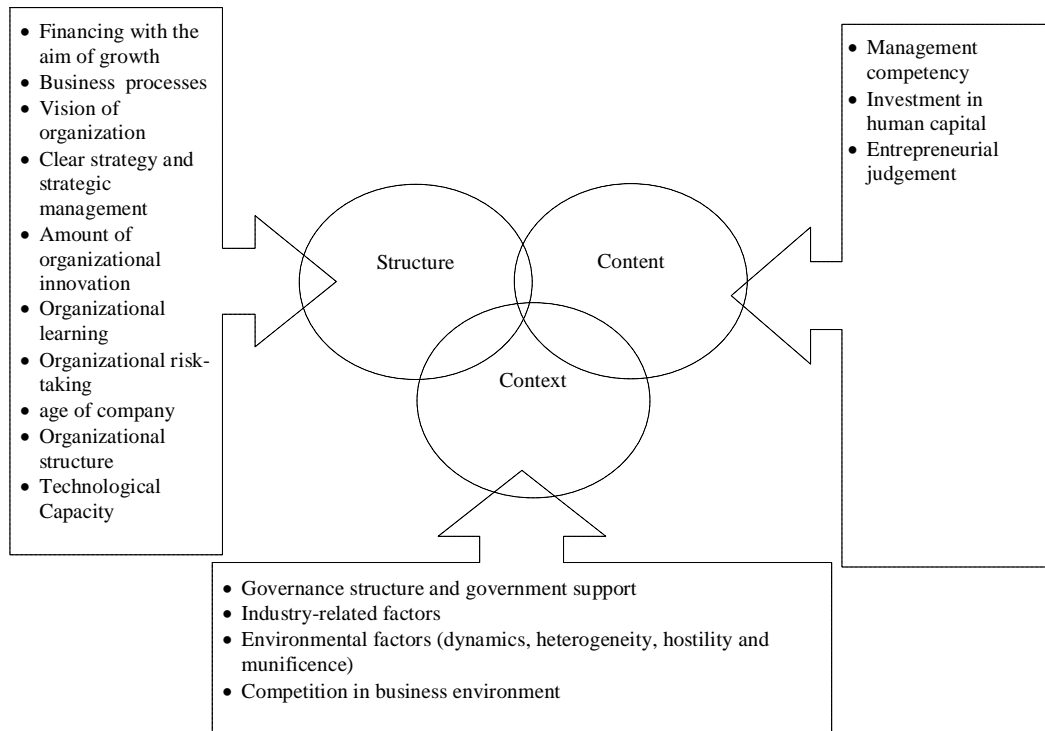
This study aimed to investigate the factors influencing the growth of small and medium-sized businesses using a comparative approach in the form of a coherent summary. An overview of the literature on the growth of small and medium-sized businesses and the factors affecting it showed that growth is a complex process with two fundamental meanings: One is change in amount when the company grows from a smaller size to a larger one, and the other one refers to the growth as the process of organizational change that leads to change in amount and other kinds of changes. Even if we are limited to one of these views, growth is still a heterogeneous phenomenon, and there will be a variety of networks for that, and the recent activities are not only carried out by increasing the volume of activities, but by vertical integration or related and unrelated diversification, including organic growth or

acquisition or strategic alliance that may be related or unrelated to the geographic expansion of internationalization, to measure which several indicators are considered such as sales, employment, assets, physical output and market share, though an indicator cannot always be considered as a preferred criterion in all small businesses.

What is important in the selection of appropriate indicators is theoretical considerations and empirical nature. The appropriateness of each of these dimensions is contingent and depends on the analysis unit. However, researchers believe that many factors influence the growth of small and medium businesses that are highly diverse. According to the established assumptions and factors in the growth of small and medium businesses, there are a lot of factors in the schools of industrial economics, education, management and governance structure. Levy and Powell (2005) believe that five factors affect the growth of small and medium-sized businesses. These factors include market, independence, personal influences, flexibility and innovation (Levy and Powell 2005). Other factors include the variability of innovation, risk-taking and the age of the company, organizational structure, business strategy, supply structure and government policies, business activities, growth motive of owner-manager and entrepreneurial orientation. Given the conclusion of researchers, we conclude that all the factors mentioned above are included in one of the three following factor:

1. Structural factors: business processes, vision, clear strategy, the amount of innovation, organizational learning, organizational risk-taking, age, organizational structure, technical capacities
2. Behavioral factors: investment in human resources, management competence, entrepreneurial judgment (knowledge of entrepreneurship, opportunity recognition and growth motivation, proactivity)
3. Contextual factors: governance structure and government support, industry-related factors, environmental characteristics (dynamics, heterogeneity, hostility and munificence), competing in the environment (Figure 1).

Figure 1. Factors affecting the growth of SMEs



This article contributes to the background of the factors determining SME growth. It is also an instrument to adjust the SMEs' Growth Appraisal System, because in the growth evaluation process, the first step is to determine the factors influencing growth. Also, these three identified factors can be a signal for policy-makers to promote and support SMEs in the path of growth.

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