

ECONOMIC RECESSION AND THE ACTIVITIES OF SMALL AND MEDIUM SCALE ENTERPRISES: A REVIEW

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ABSTRACT

The aim of this paper is to expose literature on economic recession and performance of Small and Medium Scale Enterprise in order to discuss the relationship between both variables and to identify the gap for further recommendation. Data was sourced through searches for peer-reviewed journal articles on the internet using the search term “economic recession. The review was based on empirical and selected journal; this is to make the review as comprehensive as possible. The review revealed that economic recession affects small and medium scale enterprise. However, a number of strategies are available to help them navigate the condition. Most of these strategies involve the use of resources which SMSE generally lack. The paper proposed that the adoption of economic recession will determine the direction and strength of the relationship between economic recession and performance SMEs. This paper has practical implication for owners/managers of SMEs in Nigeria in view of the current state of the economy.

Keywords: Economic recession, Performance, and SMEs.

INTRODUCTION

According to (SMEDAN, 2013) the sector plays an important role in employment creation, generating gross domestic product (GDP), achieving new product and process advances, and making a significant contribution to export. However, the sector is very vulnerable to the risk of economic recession as a result of the lean resources controlled by the firms. SMEs are usually reserved by factors like restricted access to financial, human, technological as well as managerial resources (Bouletidis et al, 2014). It is amazing however that, their small size, lean resources, owner/ managed status which were hitherto a source of problem becomes an advantage in times of economic recession. These characteristics make them flexible and easily adapt to changes in the economy and therefore recover faster than large firms.

Economic recession is a general collapse in the economy and it affects SMEs in many ways, from a fall in performance measures like sales volume, profits, growth, number of employees and so on (Cowling, Liu, Ledger & Zheng, 2015; Dolenc, Grum & Laposrsek, 2012; Lucky & Manai, 2012; Pradhan, 2011) to an outright liquidation and closure in the long run (Chukwu, Liman, Enudu & Ehiagbe, 2015; Yap, Mahmood & Chong, 2014). During recession firms must change the way they operate in order to adjust to the changes in the business environment. According to Pearce and Michael (2006), SMEs can survive and thrive during economic recession by adopting strategies like investing in multiple markets and in different

geographical locations, implementing turnaround plans, and upholding marketing initiative. However, these strategies require the use of financial, human and managerial resources which SMEs have very little.

The impact of the recession on firms' performance and how firms should react has been described as an "unexplored research stream" as well as the "least developed research stream in all of management strategy and organizational science" (Bromiley, Navarro, & Sottile, 2008 p.207). Furthermore a review of extant literature reveals that there is a dearth in research on the relationship between economic recession SMEs performance. Research on this phenomenon is relevant in the Nigerian context and will be beneficial to understand the effect of recession and the strategies adopted by firms to navigate the difficult condition in view of the current state of the economy. Calls for further studies (Kaytaz & Gul, 2014; Latham & Braun, 2004; Srinivasan, Lillen & Sridhar, 2011) provide opportunity for researchers to contribute to the study as equally noted by Nuiama, Idris, Al-Ferokh and Abu Joma, (2014).

The objective of the current research is to review the literature on the relationship between economic recession and performance of SMEs and with the aim of identifying research gap and propose a model that includes real variable. The paper is organized in various sections from the literature review, methodology and concluded with discussion, conclusions, and suggestions for future research.

THEORETICAL FRAMEWORK

The theoretical support for this paper originates from the review of the literature and the contingency theory. In literature a negative link has been found between economic recession and SMEs similarly literature review reveals a number of strategies SMEs adopt to improve performance during economic downturns. This posture involves being innovative, proactive and taking some degree of business risk. The relationship between economic recession and performance has been found to be stronger for firms operating in uncertain business environment (Covin & Slevin, 1989; Krause, et al, 2012) than for those operating in an environment (Covin & Slevin, 1989; Ezirim & Nwokah, 2009).

Contingency theory holds that the relationship between two variables depends on the level of a third variable (Rauch et al, 2009). The contingency theory is based on the idea that similarity among variables is critical for obtaining optimal performance (Lawrence & Lorsch, 1967) in addition studies have shown that performance can be improved by associating some important variables of SMEs (Neman & Covin, 1993).

REVIEW OF RELATED LITERATURE

Economic recession refers to a downturn in the economy, evidence of which can be seen in form of rising prices of goods and services, governments inability to meet its obligations, exchange rate instability, diminishing macroeconomic variables such as gross domestic product (GDP), per capita income, and export performance as well as rising unemployment rate (Farabiyi, 2016). The national bureau for economic research (NBER) defines a recession as a significant decline in



economic activity spreading across the economy and lasting for a few months, normally visible in real GDP, real income, employment, industrial production and wholesale-retail sales (NBER,2008). Several recessions have occurred in the history of the world.

For instance in the 1930s there was a great depression in the United State, also the depression in Germany after the Second World War, and the recent global financial meltdown caused by the collapse of the US housing market and the Eurozone crisis. Surely, the world economy has experienced different cycles at different times.

SMALL MEDIUM SCALE ENTERPRISES IN NIGERIA

There is no universal definition for the concept; the definition of MSMEs in Nigeria is shaped along number of employees and assets (excluding land and building). However, where there is a disagreement on the classification between employment and asset criteria, the employment-based criteria will take precedence (SMEDAN, 2013) this is because asset-based classification can be affected by inflation. The SMEs plays significant role in the economic development of countries worldwide. In Nigeria, the sector serves as a vehicle for transforming the economy.

They make significant contributions through generation of gross domestic product, and they contribute to exports and increase local value addition and technological advancement (SMEDAN, 2013).

SMEs in Periods of Economic Recession

Studies have shown that SMSE suffers during recession than large businesses, the irregular effect is caused by the lean nature of the firms, they are inhibited by limited financial, human, managerial and technological resources, which reduce their ability to navigate easily during economic downturns (Bouletidis, & Triantafyllopoulos, 2014).

Other studies have shown that their lean size and resources, their flexibility and the owner/ manager operated nature of SMEs become beneficial during economic crisis and are able to fine-tune resources and take on strategies that are capable of sustaining them. Decisions like cost slashing or increase investments during periods of economic recession, enable MSMEs to recover faster than large firms (Kitching, Smallbone & Xheneti, 2009; Skorvagova & Pasztorova, 2014).

Different strategies have been proposed to help MSMEs survive and thrive during economic downturn. Literature reveals that the effect of recession on MSMEs can be viewed from a perspective; of ‘vulnerability’ which is the external shock such as recession in the business environment that makes MSMEs risky (Kitching et al, 2009). The limited resources they control and can access hinder their ability to make adequate adjustments and changes to react to the new conditions resulting in reduced performance.

However, the strategies that can help firms navigate economic recession are described in the literature as pro-cyclical and counter-cyclical. While pro-cyclical strategies involve actions such as reduction in purchases, cutting down on production and personnel expenses,

countercyclical strategies, on the other hand, involves increase in investment during times of economic recession (Conti, Goldszmidi, & Vasconcelos, 2015).

Business Performance

From what is found in literature it seems that there is no consensus on the most appropriate measure of the construct business performance. Scholars have adopted objective or financial measures (Walker, 2001). Traditionally business performance is measured in terms of objective or financial terms such as increase in turnover, profits, return on investment and increase in number of employees. However the use of nonfinancial, subjective or lifestyle measures are becoming popular especially with regard to small businesses, these measures are job satisfaction and ability to balance domestic and work responsibilities. The financial measure is more appropriate in measuring business performance, however such data is difficult to obtain especially from SMSEs since business owners/ managers are unwilling to release such information. An alternative is to use subjective measures but subjective measures depend on the self-evaluation of the owner / manager of the business and the specific objective and motivation of the owner/ manager which may differ from one owner to another, this tends to make subjective measures less reliable (Wiklund & Shepherd, 2005).

Scholars agree that considering only one measure may be misleading in view of the differences in objectives and motivation of owners of SMEs. Therefore, in order to achieve more accuracy in measurement of performance the construct must be treated as a multidimensional construct and the integration of both objective and subjective measures offers greater advantages (Walker, 2001; Wiklund & Shepherd, 2005).

ECONOMIC RECESSION AND PERFORMANCE

The relationship between economic recession and SMEs performance is not straightforward. A review of existing literature reveals inconsistencies in findings, some studies found a negative relationship (Chukwu, Liman, Enudu & Ehiaghe, 2015; Dolenc, Grum, & Larposek, 2012; Fapohunda, 2012; Little, Mortimer, Keene & Hendersen, 2011; Lucky, & Minai, 2012; Sahin, Kitao, Cororaton & Laiu, 2011; Yap, Mahmood & Chong, 2014). While a few studies found a positive relationship between the two constructs (Chaston, 2012; Cowling, Liu, Ledger & Zhang, 2015). (Baron & Kenny, 1986,).

Baron and Kenny (1986,) opined that expectedly weak or inconsistent relation between an independent and a dependent variable in studies in relation to a particular phenomenon. As (Baron & Kenny, 1986, Baron and Kenny (1986,) defined the quantitative variable such as (sex, race, class) and qualitative variable such as (Level of reward) that affects the direction and strength of the relations between an independent and dependent variable". For this reason this study intends to contribute to the study of economic recession and SMEs.



Economic recession and SMSEs Performance.

A review of literature on the relationship between SMEs and performance indicates an aggregate positive relationship between the two constructs (Covin & Slevin, 1991; Lumpkin & Dess, 1996; Rauch et al, 2009; Wiklund & Shepherd, 2003).

However, the positive relationship between economic recession and SMEs performance has been found to hold more mostly when operating in uncertain business environment such as during an economic crisis than for those operating in a benevolent environment (Covin & Slevin, 1991; Ezirim & Nwokah, 2009).

A number of strategies have been suggested by previous researchers such as investing in multiple markets and in different geographical locations, others are developing turn around plans, and maintaining marketing initiatives (Pearce & Michael, 2006), however these strategies require the use of financial, human and managerial resources which SMEs are known to be constrained by (Bouletidis, & Triantafyllopoulos, 2014).

Based on theoretical backing and evidence found in literature this study argues that SMSEs the relationship between economic recession and performance.

Hence this study extends existing research by making the following propositions to summarize the relationship one might expect from economic recession, and SMEs performance. Proposition 1 there is a negative relationship between economic recession and performance of SMEs.

PROPOSED CONCEPTUAL FRAMEWORK

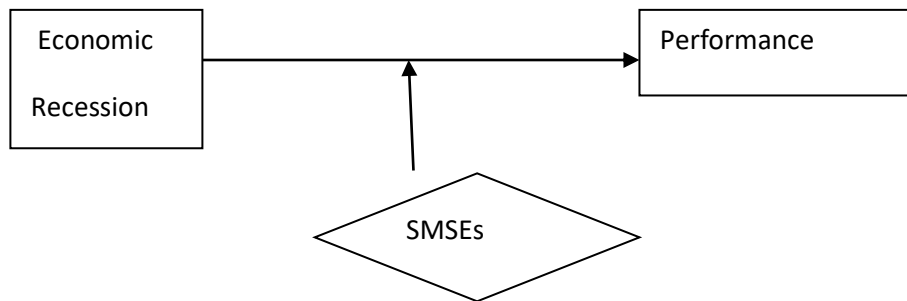


Figure 1: Source: Chong, G.H. (2008).

METHODOLOGY

The review focuses on the concepts of economic recession and performance and covers relevant literature on the topic. Data were obtained through searches for peer-reviewed journal articles on the internet using the search terms “economic recession and SMEs performance.

The review covers empirical studies published in peer-reviewed journals. Selection of articles for the review was not limited to any specific journal this is to achieve comprehensiveness and robustness of the sample. Only empirical studies on the relationships between the two variables of interest were included while non-empirical studies were excluded



from the review. Using this method the researcher obtained a suitable number of samples for the review.

DISCUSSION

The purpose of the paper was to conduct a review of the literature on economic recession and performance of SMEs with a view to analyzing the relationship between economic recession and performance. Also to identify research gap and recommend new research area. Studies on the effect of economic recession and firm performance have generally suggested that there exist a negative relationship between the two variables (Chukwu, Liman, Enudu & Ehiaghe, 2015; Dolenc, Grum, & Larposek, 2012; Fapohunda, 2012; Little, Mortimer, Keene & Hendersen, 2011; Lucky, & Minai, 2012; Sahin, Kitao, Cororaton & Laiu, 2011; Yap, Mahmood & Chong, 2014). In terms of measures of Performance the most affected are profits, sales volume of SMEs. Although, there is a long run a positive relationship between economic recession and SMEs performance (Chaston, 2012; Cowling, Liu, Ledger & Zhang, 2015). This indicates that SMEs can experience improved performance during periods of economic recession. While a mixed result was reported by others that are positive relationship for some SMEs and negative for others (Kitching, Smallbone & Xheneti, 2009). On the other hand some scholars argue that the direction of the effect of economic recession on performance of SMEs in the economy (Conti, Goldzmid, & Vasconcelos, 2015; Lee & Nhu, 2009; Pradhan, 2011). These researchers argue that the strategies adopted by SMEs can be of advantage in recession.

A review of the literature suggests that there are considerable variation and inconsistencies in the reported relationship between economic recession and SMEs performance, also a number of factors have been suggested that can affect the direction and/or strength of the relationship. Scholars reported different strategies and factors that determine performance. (Chaston, 2012), competitive strategies of low cost, differentiation and focus strategy (Lee & Nhu, 2009), Proactiveness and innovativeness (Kraus, et al 2012). All the studies reviewed focused on SMEs and two studies focused SMEs performance (Lee & Nhu, 2009, Little, Mortimer, Keene & Hendersen, 2011).

CONCLUSION

This review focused on empirical studies on the relationship between economic recession and performance of SMEs. The paper presented definitions and explanation of key conceptual issues and empirical findings.

The review is only limited to empirical results, however in view of the gap found in literature and the inconsistencies in reported findings; this paper suggests SMEs variables are to test both direct and indirect relationship between economic recession and performance of SMEs that are innovative, proactive and take high risks are likely to be less affected by economic recession and increase in their performances. It is hoped that this paper will contribute to knowledge on issues concerning strategies adopted by SMEs during economic recession; it is also expected to have practical implication for owner/ managers of SMEs in Nigeria.

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