

Impact of External Business Environment on Organisational Performance of Small and Medium Scale Enterprises in Osun State, Nigeria

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Abstract

The paper examined the impact of external business environment on organizational performance of Micro, Small and Medium Scale Enterprises in Nigeria. It also reviewed literature on MSMEs, business environment and organizational performances. Secondary sources of data were utilized for the study. The findings from reviewed literature showed that the external business environment (economic, political, legal, socio-cultural environment, demographic, natural, technological, global and financial environment) have influence on MSMEs operators in Nigeria. It was also discovered that there exists relationship between SMEs and the environment in which it occurs. The study concluded that SME operators should understand all these types of external business environment and their implications on organizational performance of their business activities in order to identify opportunities and threats to their businesses and update their knowledge, understanding and skills to meet the predicted changes in realm of their enterprises.

Keywords: MSME operators, external business environment, organizational performance, scanning, socio-cultural environment.

INTRODUCTION

The environment within which the business operates is very important for running small and medium scale enterprises. For instance, where there is a change in the government policies, the business has to make the necessary changes to adapt it to the new policies.

Similarly, a change in the technology may render the existing products obsolete, for instance the flat televisions (LCDs & LED) have made the black and white televisions out of fashion. Again a change in the fashion or customers' taste may shift the demand in the market for a particular product e.g. the demand for locally made wears and shoes have reduced the sales of foreign wears and shoes.

All these factors are beyond the control of the business. A business environment comprises of such factors as infrastructural, legal, natural, financial, cultural, economic, social and political environments. These environmental forces have been found to be capable of either impeding or facilitating entrepreneurial activities in any economy. The World Bank is of the opinion that improvement in the enabling environment leads to greater levels of investment by the private sector, more wealth, job creation and poverty alleviation (Adeoye, 2013). The relationship between business and its environment is one of mutuality; that is, the environment exerts pressure on the business while the business, in turn, influences some aspects of its environment. The above picture, therefore, presents the need to examine the effect of business environment on the organizational performance of SMEs, which is the focus of this write-up.

LITERATURE REVIEW

Meanings of Small and Medium Scale Enterprises

Different scholars have given different definitions to SMEs. Some attempt to use the capital asset while others use skill of labour and turn-over level. Others define SMEs in terms of their legal status and method of production. Storey (1994) argues about the danger of using size to define the status of firm by stating that in some sectors all firms are regarded as small, while in other sectors of the economy, there are possibly no firms which are small.

However, in July, 2001, micro-small and medium enterprises (MSMEs) in Nigeria were defined by National Council on Industry as follows:

1. **Micro/ Cottage Industry:** An industry which has a total cost, including working capital (but excluding cost of land) of not more than N1 .50 million with a maximum of 10 employees.
2. **Small-Scale Industry:** An industry with a labour size of 11-100 workers, or total cost of not more than N50 million, including working capital but excluding cost of land.
3. **Medium Scale Industry:** An Industry with a total cost of over N50 million but does not exceed N200 million, including working capital but excluding cost of land.

4. Large Scale Industry:An industry with a working capital of more than N200 million and a work force of over three hundred workers but excluding cost of land.

European Commission (EC) (2003) defines Small and Medium Enterprises (SMEs) as enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding 50 million euro or an annual balance sheet total not exceeding 43 million euro. Consequently, the EC definition is too all embracing to be applied to a number of nations. It is clear from the various definitions that there is no general consensus over what constitutes an SMEs. Definitions vary from industries to industries and from countries to countries. From Nigeria context, we can define SMEs as entities engaged in economic activities, irrespective of their legal forms. This definition has taken into consideration economic activities engaged in by business organizations such as sole proprietorships, partnerships, cooperatives, associations, family firms etc.

Apart from the foregoing, Small and Medium Enterprises (SMEs) occupy a place of pride in virtually every country or state. Because of their (SMEs) significant roles in the development and growth of various economies, they (SMEs) have aptly been referred to as “the engine of growth” and “catalysts” for socio-economic transformation of any country. SMEs represent a veritable vehicle for the achievement of national economic objectives of employment generation and poverty reduction at low investment cost as well as the development of entrepreneurial capabilities including indigenous technology.

SMEs operate within environment which according to Adidu&Olanje (2006) is an aggregate of all conditions, events, circumstances and influences that surround and effect the business organization. Business organizations must interact with those forces that influence its decisions, directions, actions, size, health and profitability in the environment.

Agboli and Ukaegbu (2006) state that SMEs do not operate in vacuum; they affect and are affected by environmental conditions. Therefore SMEs irrespective of their objectives must take into consideration, these environmental opportunities and constraints.

Environment

The word “environment” is derived from the French word and “Environ” which means “surrounding”. Our surrounding includes biotic factors like human beings, plants, animals, microbes etc. and abiotic factors such as light, air, water, soil among others.

According to UBC Net Tutor Commerce (2008), environment is the sum total of conditions that surrounds us at a given point of time and space. It is comprised of the interacting systems of physical, biological and cultural elements which are interlinked both individually and collectively. It states further that environment is the sum total of conditions in which an organism has to survive or maintain its life process. It influences the growth and development of living forms.

Pannerseelvan and Rarmarknshnan (2005) define environment as the universe of a biotic and other physical elements as organized into dynamic system. These systems are ecological systems or ecosystems which represent the integration of living (biotic) and non-living (abiotic) elements in the environment.

Thus, environment refers to anything that immediately surrounds an object and exerting a direct influence on it. It consists of the interacting systems of business physical and cultural elements which are interlinked both collectively.

What is Business Environment?

According to business dictionary (2013), business environment can be defined as the combination of internal and external factors that influence a company's operating situation. The business environment can include factors such as: clients and suppliers; its competition and owners; improvement in technology' laws and government activities; markets, social and economic trends. Fernando (2011) regards business environment as external forces, factors and institutions that are beyond the control of the business and they affect the functioning of a business enterprise. These include customers, competitors, suppliers, government and the social, political, legal and technological factors etc. Ask.com (2013) also defines business environment as the physical and operational factors, both internal and external, that affect the flow of activities in a business. They include; customers, competitors, suppliers, distributors, industry trends, substitutes, regulations, government activities, the economy, demographics, social and cultural factors, innovations and technological developments. A business is influenced by the environment in which it operates and the success of any business is dependent on its ability to adapt to its environment. The complexity of this reality for business owners is compounded by the fact that there are many different environments that each business operates in (IBS, 2013).

Blurtit (2013) also regards business environment as those conditions and forces which are external to the business and are beyond the individual business unit, but they all operate within it.

On the basis of the above definitions, the features of business environment can be summarized as follows:

- (a) The sum total of all factors external to the business firm and greatly influence their functioning.
- (b) Factors and forces like customers, competitors, suppliers, government and the social, cultural, political, technological and legal conditions.

Features of Business Environment

Business environment has the following features:

- (a) Business environment is the sum total of all factors External to the business firm and that greatly influence their functioning.
- (b) It covers factors and forces like customers, competitors, suppliers, government and the social, cultural, political, technological and legal conditions.
- (c) The business environment is dynamic in nature, which means, it keeps on changing.
- (d) The changes in business environment are unpredictable. It is very difficult to predict the exact nature of future happenings and the changes in economic and social environment.
- (e) Business environment differs from place to place, region to region and country to country. Political conditions in Nigeria differ from those in South Africa. Taste and values cherished by people in Nigeria and France vary considerably.

Importance of Business Environment to SMEs

There is a nexus between the business and its environment. This nexus helps in strengthening business enterprises to use its resources more effectively. According to Chidambaram (1999), business environment is very important to SMEs in the following ways:

- (a) **Determining opportunities and Threats:** The interaction between the business and its environment would identify opportunities for and threats to the business. It also helps the business enterprises for meeting the challenges successfully.

- (b) **Giving Direction for Growth:** The interaction with the environment leads to opening up new frontiers of growth for the business enterprises. It enables the business to identify the areas of growth and expansion of their activities.
- (c) **Continuous Learning:** Environmental analysis makes the tasks of managers easier in dealing with agro-business enterprises challenges. The managers are motivated to continuously update their knowledge, understanding and skills to meet the predicted changes in realm of business.
- (d) **Image Building:** Environmental understanding helps the business organizations in improving their image by showing their sensitivity to the environment with which they are working.
- (e) **Identifying Firm's Strength and Weakness:** Business environment helps to identify the individual strengths and weaknesses in view of the technological and global developments.

The Nigerian Business Environment

The relationship between business and the environment has been given attention in the last few decades. The Nigerian business environment has been evaluated and addressed by several scholars and several suggestions have been recommended but there has been no visible change. The Nigerian business environment is multifaceted, complex and dynamic in nature and has a far-reaching impact on the performance and growth of the entrepreneurship business. The World Bank is of the opinion that improvement in the enabling environment leads to greater levels of investment by the private sector, more wealth, job creation and ultimately more poverty reduction.

The Nigeria government has initiated several programmes that are geared towards the mobilization, training and supporting initiatives that will promote financial literacy and entrepreneurship development. Despite all these, the efforts seem abortive; this can be linked to environment, some of which are external environmental factors which are analyzed below.

External Business Environment

The concept of external environment is for every kind of business operation. External environment is an attempt to understand the outside forces of the organizational boundaries of SMEs. External environment can provide both facilitating and inhibiting influence on organizational performance. Duncan (1972) views external business environment as the totality of factors outside an organization

that are taken into consideration by an organization in its decision making. These factors depend largely on the complexity and dynamism of the environment (Duncan, 1972; Dess& Beard 1984). Thus, external business environment has been classified as being stable when it does show any changes, unstable when it shows relative changes and dynamic when it shows changes continuously (Aguilar, 1967).

4.21 Types of External Business Environment

The types of external business include:

- 1. Economic Environment:** According to Adeoye (ibid), the survival and success of each and every business enterprises depend fully on its economic. Managers in the business enterprises should be worried about the trends in the economic conditions in their decision making. This is defined by factors such as: (i) Gross Domestic Product (GDP)(ii) Government fiscal and monetary policies (iii) Unemployment rate (iv) Exchange rate(v) Inflation rate (vi)Capacity utilization.
- 2. Political Environment:**Mark and Nwaiwu (2015) submit that not only the political environment poses direct risks to small and medium scale enterprises. They also posited that regulatory changes have the potential to promote or inhibit market competition, social risks often have political bases and responses and political mismanagement can turn natural or human-made events into catastrophes. According to Okeyo (2014), the implication of political environment to a business enterprises is that the risk emanating from it is a measure of likelihood that political events may complicate its pursuit of earnings through direct impacts (such as taxes or fees) or indirect impacts (such as opportunity cost forgone).
- 3. Legal Environment:** According to Adeoye (ibid), legal environment consists of the laws regulations and procedures of a country which SMEs are anticipated to comply with in the course of their operations. These laws may facilitate successful business conduct as well as constitute handicaps to successful performance. Furthermore in carrying out their business operations, agro business, enterprises are required by law to pay taxes, value added tax, capital gain tax, education tax, import duties, excise duties among others.
- 4. Socio-cultural Environment:** Socio-cultural environment in broad terms consists of both the social system and the culture of a people. It refers primarily to man created intangible elements which affect people's behaviour relationship, perception and way of life, and their

survival and existence. In other words, the socio-cultural environment consists all elements, conditions and influences which shape the personality of an individual and potentially affect his attitude, disposition, behavioural decisions and activities. Such elements include beliefs, values, attitudes, habits, forms of behaviour and life styles of persons as developed from conditioning (Adeleke et al, 2003). Akpor-Robaro (2012) maintains that social cultural environment, in relation to business enterprises can be defined as consisting of all the elements of the social system and culture of a people which positively or negatively effect and influence business enterprise emergence, behaviour and performance and entrepreneurship development in general.

5. **Demographic Environment:** This refers to the size density, distributions and growth rate of popular. These factors have direct bearing on the demand for agricultural products for instance a country where population rates is high and children constitute a large section of population, then there is more demand for baby food products. Similarly the demand of the people of cities and towns like Lagos, Ibadan, and Port-Harcourt are different from the demand of the people of rural areas. Thus an agro business enterprise owner keeps a watch on the changes on the demographic front and reads them accurately in order to land opportunities knocking at its doorstep.
6. **Natural Environment:** The natural environment includes geographical and ecological factors that influence the business operations. These factors include the availability of natural resources, weather and climatic condition, location aspect, top a graphical factors etc. Business is greatly influence by the nature of natural environment. For example, sugar factories are set up only at those places where sugarcane can be grown. It is always considered better to establish manufacturing unit near the sources of input. Also, government's policies maintain ecological balance, conservation responsibility on the business sector (Shaikh, 2010).
7. **Technological Environment:** Technological environment has impact on the two decision take by SMEs. Technological change can involve:
 1. **New process of production:** News ways of doing things which rises productivity of factors inputs; for example around 80% of technological change has been processing agricultural technology innovation.

2. **New products:** For example Led Indoor Crop Cultivator, Air Seeder or Plow, Sprayers, Grain header harvester and Rotary tiller etc. are direct result of agricultural technological innovations for agricultural products (Zubair, 2013).
8. **International Environment:** Adeoye (Ibid) refers to international environment as all those elements on the international scene, which can help or inhibit the decision and operations of the business enterprise. Changes in the economic, social, technological, political and public issues affect the operations of agro-enterprises. This is because most companies depend on imported raw materials, technology and other services or export their goods and services overseas.
9. **Financial Environment:** UGC NET Commerce (ibid) ascertains that business finance is concerned with making decisions about the investments in the business. It includes bond markets, forex markets, stock markets, commodity markets. OTC markets, Real estate markets, and cash or spot markets. All these markets play an important role in raising finances for the companies and at the same time give profits to the investors.
10. **Social Environment:** The social environment of business includes social factors like customs, tradition, values, beliefs, poverty, literacy, life expectancy rate etc. The social structure and the values that a society cherishes have a considerable influence on the functioning of business firms. For example, during festive seasons there is an increase in the demand for new clothes, sweets, fruits, flower etc. Due to increase in literacy rate the consumers are becoming more conscious of the quality of the products. Due to change in family composition more nuclear families with single child concepts have come up. This increases the demand for the different types of household goods. It may be noted that the consumption patterns, the dressing and living styles of people belonging to different social structures and culture vary significantly.
11. **Competitive Environment:** These are those firms that market products that are similar to, or can be substituted for, a business' product(s) in the same geographical area. The four general types of competitive structure are monopoly, oligopoly, monopolistic competition and perfect competition.

Organizational Performance

Organizational performance is one of the most important variables in the management research and arguably the most important indicators of the small and medium scale enterprises.

Although the concept of organizational performance is very common in the academic literature, its definition is difficult because of its many meanings. For this reason, there isn't a universally accepted definition of this concept. In the 1950s organizational performance was defined as the extent to which organizations, viewed as a social system fulfilled their objectives (GeorgopoulosTannenbaum, 1957). Performance evaluation during this time was focused on work, people and organizational structure. The years 1980s and 1990s were marked by the realization that the identification of organizational objectives is more complex than initially considered. Thus, organizational theories that followed supported the ideal of an organization that achieves its performance objectives based on the constraints imposed by the limited resources (Lusthaus&Adrien, 1998). In this context, profit became one of the many indicators of performance. Lebens&Euske (2006) provide a set of definitions to illustrate the concept of organizational performance:

- Performance is a set of financial and non-financial indicators which offer information on the degree of achieving of objectives and results.
- Performance is dynamic, requiring judgment and by using a causal model that describes how current actions may affect future results.
- To define the concept of performance is necessary to know its elements characteristic to each area of responsibility.
- To report an organization's performance level, it is necessary to be able to quantify the results.

Conclusion and Recommendations

There is no doubt, based on the empirical study discussed in this paper, that all the types of external business environment (economic, political, legal, socio-cultural, demographic, natural, technological, global, financial, social and competitive) have significant impact on organizational performance of small and medium scale enterprises. It is also realized that there exists relationship between SMEs and the environment in which it occurs.

The study concluded that SME operators should be understand all these types of external business environment and their implications on organizational performance of their business activities in order to identify opportunities and threats to their businesses and update their knowledge, understanding and skills to meet the predicted changes in realm of their enterprises.

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