

# The Small and Medium Enterprises' Contributions to Ongoing Economic Developments in Somalia

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**Abstract:** Entrepreneurship is necessary to raise living standards and promote economic expansion. It is widely believed that small and medium-sized firms are essential for modernization, economic expansion, job creation, and revenue generating. The research focuses on how SMEs may assist Somalia in generating economy progress and job opportunities. A previous study was utilized, and to understand variables, the study employs a quantitative method and a descriptive research design. 201 people made up the sample size that was based on a judgment or intentional sampling technique. The researcher prepared the questionnaire to collect data, and Excel 2010, the SPSS statistics program was used to edit, compile, and tabulate it. Ultimately, in order to increase validity and reliability, researcher fixed some errors and anomalies. According to the study, the main obstacles for SMEs in Somalia are a lack of funding, inadequate management abilities, and specific government policies. The study also showed that the region's developing small and medium enterprises are negatively impacted by nations' inadequate strategy on imported goods, international charity and unrestricted competitiveness. This study came to the conclusion that granting SMEs in Somalia accessibility to capital through banks and large corporations, providing them with sufficient skills, understanding, and enacting strong strategy for their development that will improve them.

**Keywords:** SMEs, Economic, Entrepreneurs, Somalia

**JEL Classification:** O10

## 1. Introduction

The pursuit of economic superiority and growth is shared by developed and developing nations. Poor institutional systems, inadequate capital development, and inadequate infrastructure have all been identified by some scholars as contributing to the decrease in growing countries. New theories based on academic research have demonstrated that the entrepreneurship factor is integral to the economic miracle that third world nations so desperately need (Olutuase, 2014).

Countries seeking long-term economic growth must give special priority to the SMEs firm sector, which has the ability to generate employment, boost community innovation, diversified output, promote indigenous entrepreneurs, and connect with huge corporations. SMEs are critical to the development of any economy and act as industrial development accelerators (Aruwa & Suleiman, 2004).

Somalia is considered as the world's least developed countries, with high rate of unemployment. But still there is a progress alongside with state building, also many diasporas and entrepreneurs are coming back in the country, creating opportunities for young people and contributing huge investing in the country's economy (GDP growth). The majority of Somali SMEs are family-owned, those small and medium enterprises has contributed hugely to the ongoing economic developments in Somalia.

## **2.The Literature reviews**

### ***2.1. Concept of Small Medium Enterprises (SMEs)***

#### ***Definition:***

World bank (2021) Small and medium-sized enterprises (SMEs) are independent, non-subsidiary businesses with fewer than a certain number of employees. This figure varies by country. As in the European Union, the most common upper limit for designating an SME is 250 employees. However, some countries limit 200 employees, whereas the United States defines SMEs as businesses with fewer than 500 employees.

SMEs are less likely than big companies to receive bank loans; instead, they rely on personal funds or cash and family to start and initially run their businesses. According to the International Finance Corporation (IFC), 65 million enterprises, or 40% of structured micro, small, and medium enterprises (MSMEs), have an unfulfilled financing need of \$5.2 trillion per year, which is 1.4 times the current global MSME lending level. Pacific and East Asia account for the greatest percentage of the entire worldwide economic deficit (46%), pursued by Europe and Central Asia (15%) and Latin America and the Caribbean (23%). The volume of the gap differs substantially through one location to another. The Caribbean and Latin America, the Middle East, and North Africa have the highest proportions of the finance gap compared to potential demand, at 87% and 88%, respectively. Approximately half of all formal SMEs do not have access to proper credit. When micro and informal enterprises are included, the financing gap grows even more extensive.

## 2.2. The Importance of SME in Developing Countries

OECD (2004) The concept of SME and entrepreneurship development was introduced into the growth and development landscape as early as the late 1940s, when governments implemented targeted policies (grants, subsidized credits, special tax treatment, etc.) and established small business or SME support agencies. (e.g., publicly funded SME agencies were set up in 1948 in Japan, 1953 in the USA, 1954 in India, 1966 in Tanzania, 1976 in Turkey).

Berry (2007) The size and significance of the small medium enterprise sector vary by country, as with any other component of an economy. For the last few decades, there has been a growing recognition of its role in industrial countries, which has been more obvious in developing countries since the 1970s. SMEs are essential to almost all economies in the world, but especially to those in developing countries. There is considerable interest in SMEs in developing countries. There are probably two main reasons for this. One is the belief that SMEs development may prove to be an effective antipoverty program. The second is the belief that SME development is one of the building blocks of innovation and sustainable growth. Of course, these two reasons are linked because most international evidence says that growth and actual poverty reduction go hand in hand. If SMEs development helps growth, more than likely it helps reduce poverty as well (Warner, 2001: 61)

Güttler, (2001:89) SMEs contribute substantially to a stable economic environment and the development of the economy. To achieve stable economic development, the business of SMEs must be supported. They need financial and consulting services that help them overcome difficulties during the start-up phase or carry out their everyday business activities.

Berry, (2007) Developing countries without significant SMEs sectors (often referred to as having a "missing middle" in their firm size structure) tend to have not only capital and income concentrated in larger firms, but also a "labor elite" in that sector, able to bargain for wages much higher than elsewhere in the economy. With the economy's capital stock almost entirely consumed by large firms (usually as a result of capital market imperfections), there is little remaining capital to be distributed among the many workers who large firms do not hire; this results in a large micro-enterprise sector, with the SMEs sector squeezed out due to a lack of capital.

The equilibrium wage in the micro–enterprise sector is meager, and capital incomes are low there as well. In short, income is very unequally distributed. When the SME sector is large, these extremes in the distribution of both capital income and labor income are avoided.

OECD (2004) Furthermore, SMEs contribute to employment and income generation, and export revenues in developing countries. However, to tap into the potential of SMEs for development and poverty reduction, transition and developing country governments, development partners, and SMEs.

They need to address several challenges:

- The domestic SME/private sector should grow by:
  - establishing new and innovative businesses, and
  - graduating as many informal enterprises as possible into the formal sector.
- Small and medium–sized enterprises (SMEs) must become more competitive and productive in their home markets.
- At least a portion of these nationally competitive SMEs must achieve a level of competitiveness that will allow them to integrate into global value chains via trade (exports and internationalization) and investment, including FDI linkages.

### **2.3. Small & Medium Enterprises in Somalia**

One of the least underdeveloped nations in the world, Somalia also has one of the highest unemployment rates. However, both human and financial resources have not been appropriately developed or prepared as a result of protracted civil turmoil and a lack of institutions. According to studies, small and medium–sized enterprises help developing nations like Somalia improve their economies. On the other hand, Somalis find it difficult to cope with the humanitarian aid that developed nations continue to provide. Idris (2016) claims that properly managed humanitarian aid can have a significant positive impact on the economy, including encouraging local business regeneration, job creation, and rising government tax revenue. However, it can also lead to price inflation, reduce the supply of goods, weaken local businesses, and even hasten their closure.

According to reports from the Somali Humanitarian Fund (SHF), each year, millions of dollars in cash or in–kind from donors are given to Somalia. However, due to poor management and a lack of priorities, these money are hurting Somalia's economy rather

than enhancing it. These enormous resources can be used to build infrastructure, create jobs, and provide capital for small businesses, among other things. According to a 2015 World Bank study by Randa, Whimp, Abdullahi, and Zacchia, two-thirds of Somalis aged 14 to 29 and 70% of Somalis under the age of 30 are unemployed; therefore, investing in small and medium-sized firms will increase employment growth, security, and living standards. Dalmar, Ali, and Ali (2017) also recommended that the government take into account measures that support foreign debt and make use of it to boost domestic investment.

There is no clear definition of the term small and medium enterprise, and the available definitions focus on the number of employees and the firm's sales revenues. In fact, the term "SMEs" varies significantly across different countries around the world. In Kenya, for example, SMEs are organizations that employ between 10 and 15 people and make between K.sh. 500,000 and K.sh. 5,000,000 in sales income, according to the large and small business (MSE) statute (2012). The term "SMEs" refers to a wide range of businesses that operate in many economic areas.

Minister of commerce and industry in Somalia (2020), states that in Mogadishu the capital city of Somalia, over 87 are formerly registered and recognized SMEs that operate as manufactures and in service sector of the economy. However, the given number could be higher than that, there are many SMEs that has not been formally registered.

Abdirahman (2017) it is estimated that the SMEs sector in employ about 80% of the labor force in Somalia while significantly contributing 1.2 % of gross domestic products (GDP) of the country.

According to Ahmed et al (2018), most of Small and medium Enterprises suffer resource constraints that make it challenging for them to own capabilities that would boost their degree of operational efficiency. According to Kasie et al. (2013), SMEs play a critical role in the growth of Somalia's economy by creating job opportunities. Well-performing SMEs are seen to provide high-quality products and create more jobs, thereby raising the living standards of the communities in which they operate.

#### **2.4. Job creation**

Small and medium-sized businesses (SMEs) are acknowledged as answers for economic growth, modernization, job creation, income generation, and scientific advancement in the majority of sophisticated economies (Acs & Audretsch, 1990; Bhutta, Rana & Asad,

2008). According to Kadiri (2012), the phrase "small and medium-sized enterprises" (SME) is frequently used in the business world because this industry helps to create jobs, advance a country, reduce poverty, and advance the economy. More job opportunities are offered by small and medium-sized firms than by large and global corporations. Alif (2021) SMEs and startups place a greater emphasis on job creation among young people than large corporations. As a young country, Somalia has an opportunity to use SMEs to engage a new generation of young men and women entrepreneurs, potentially contributing to economic growth and significant reductions in unemployment.

### **2.5. Wealth creation**

Entrepreneurs help themselves, and their collaborators achieve a stable income source through profits and help individuals increase their purchasing power by investing their resources, whether natural or financial. It is possible to generate domestic income and boost economic growth over time by supporting and encouraging more startups.

### **2.6. Better standard of living**

Small and medium-sized enterprises (SMEs) in fragile states can play a critical role in providing the country with innovations and technologies to improve people's lives. In Somalia, for example, the advancement of mobile banking services is assisting the government and international NGOs in accelerating community development, particularly in rural areas.

### **2.7. Challenges faced by SMEs**

Small and medium-sized firms undoubtedly contribute significantly to economic expansion. However, both developing and developed nations are concerned about the failure rate of small and medium-sized firms. According to several surveys, 80% to 90% of SMEs fail within 5-10 years (Ahmad, Abdul Rani & Mohd Kassim, 2010; Kuratko & Hodgetts, 2004).

Owners of small and medium-sized businesses face challenges due to changing economies, a diverse array of technology, expertise, and resource shortages (Gummesson, 1994). Small and medium-sized businesses are critical for economic growth and development, as well as job creation. To thrive in the global economy, small and medium-sized businesses require precise management. Successes in entrepreneurship will demonstrate how poverty levels can be reduced and people's lives in the world's developing economies can be improved.

Small and medium-sized enterprises (SMEs) face a variety of challenges both globally and domestically. According to the SMIDEC (2012) study report, these challenges include competition from other producers, increased global competitive, limited capability to meet the challenges of market globalization and liberalization, low productivity and quality output, limited capacity for knowledge acquisition and technology management, limited access to capital and finance and the infancy of venture funds in initial or mezzanine financing, a lack of skills for the new environment, and general shortfalls.

### **3. Methods and Materials**

To understand variables, the research employed a style of descriptive analysis within a quantitative structure. The study's focus was on young people and entrepreneurs in Mogadishu. The Purposive or Judgmental Sampling method was used to select a sample size of 201 individuals because the potential scope was so broad. Using a non-probability technique called judgmental sampling, the researcher selects from the population the individuals he believes are most likely to have the needed or accurate information (Etikan & Bala, 2017). Additionally, the method is frequently regarded as having a great level of validity and reliability, in addition to bias elimination.

An inquiry was created by the researcher to collect data. The main benefits of choosing a data gathering inquiries are which is less expensive, takes less time, and enables respondents to answer honestly and anonymously, making it simpler to gather the necessary data. The researcher used a pretest to account for any potential questionnaire errors and determine how long it would take to complete. Pre-testing entails evaluating the questionnaire to determine whether or not the questions are pertinent. A small group of respondents conducts pre-testing to weed out superfluous questions from the questionnaire (Bashir Ahmed, 2021).

### **4. Discussion of the Findings**

#### **4.1. Population Results**

At this stage will concentrate the gender, age, educational backgrounds and level of income of our study's participants. It's significant since it demonstrates that the information was gathered from those who were closest in relation. The results indicate that practically all of the ideal research participants were contacted with our inquiry.

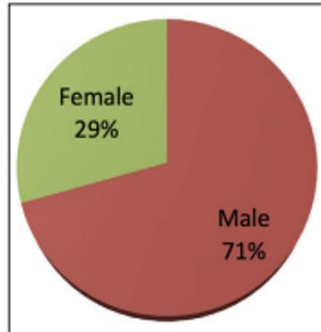


Figure 1. Gender

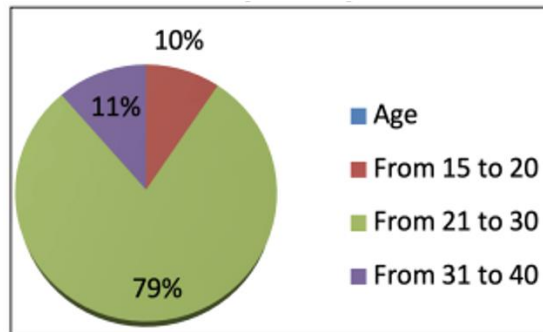


Figure 2. Age

Men made up 71% of the study's participants, while females made up the leftover 29%, as seen in Picture 1. This is understandable considering that in Somalia, men predominate in the workplace, schooling, and other spheres of society. Chart 2. illustrates, on the contrary side, that the majority of our participants were between the ages of 21 and 30, indicating that the research was primarily concentrated on the youth, who are disproportionately affected by unemployment and are critical to the nation's economic progress.

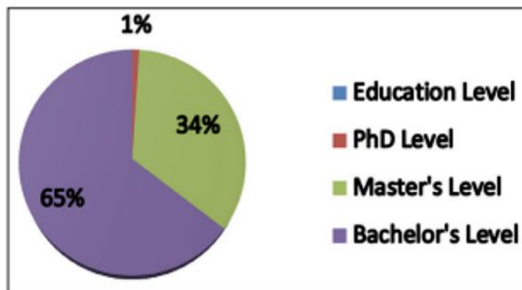


Figure 3. Education Level

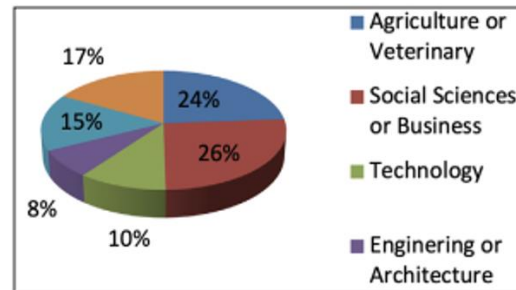


Figure 4. Field of Education

According to the findings, over half of the participants were either students or unemployed, with 45 percent earning less than \$200. Data demonstrates the youngster's lower earnings level, which might impede them from developing further.

#### 4.2. Study findings

The results of the study's inquiry asking respondents about the limitations and obstacles facing small and medium-sized businesses are shown in the section after that. These findings will aid Somalia if SMEs businesses are supported, and they demonstrate whether such businesses can support the country's faltering economy and lower the



country's increasing jobless number. Additionally, they demonstrate what share-holders may act by promoting businesses and other SMEs.

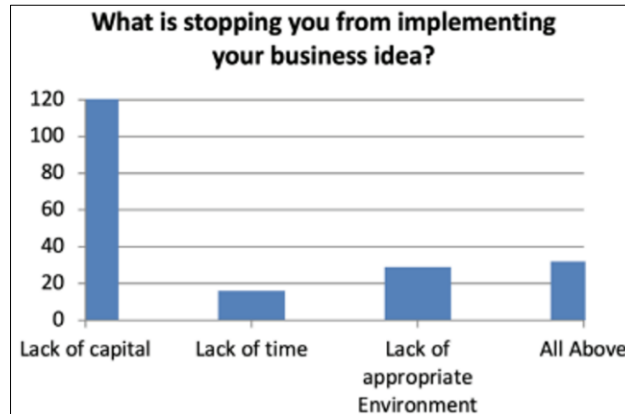


Figure 5. Challenges of SME in Somalia

Research shows one of the major obstacles facing SMEs businesses is a limitation of finance and financial access (Singh & Belwal, 2008).

The majority of the responses to queries indicate that our respondents were eager to launch their own firms, but a lack of funding was the main barrier to their success.

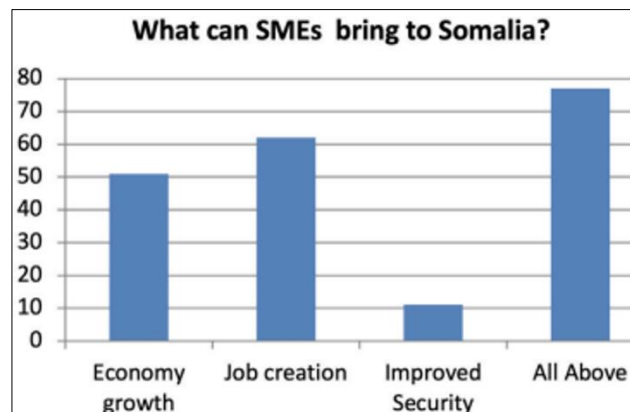


Figure 6. What SMEs Can Bring to Somalia

Research further highlights the significance of small and medium-sized businesses for economic growth, particularly in emerging nations. SMEs are widely recognized for their part in promoting commercial booming and the generation of jobs. SMEs may assist the economic thrive and create jobs, according to our respondents.

Small and medium-sized businesses can succeed or fail depending on the talents and abilities of the business owners. Entrepreneurs also struggle when they lack knowledge, abilities, or a strong social network (Marshall & Oliver, 2005). The main reason why new SMEs in South Africa fail is a lack of preparedness and education (which is a subset of human capital) (Herrington, Kew & Kew, 2009). According to Martin and Staines (2008), the main causes of new companies failing include a lack of management knowledge, experience, and human qualities. Similar to this, our research demonstrates that one of the major challenges for aspiring business owners in Somalia is a lack of managerial skills.

The respondents say that help for SMEs should come from the government, banks, and big businesses. A functioning government should put huge investment into the emerging small businesses. A business revolution will have a greater possibility of occurring if banks and large corporations have access to capital, experience, and talents. Banks and large corporations make it difficult for entrepreneurs to secure loans, make investments, or secure finance. Respondents affirm that in order to obtain loans or financing, banks and big businesses require SMEs to present IDs, guarantors, or mortgages.

## **5. Conclusion**

For the Somali people to survive, entrepreneurship is vital. Somalia needs to put more effort into growing small businesses as one of the least developed nations in the world if it wants to reduce its reliance on foreign aid. Establishing numerous SMEs businesses, specifically for youngsters, is the suitable option to combat financial downturn, shoddy safety, and rising unemployment. According to the data, supporting small and medium-sized businesses could improve the national economy and increase employment.

Lack of funding, inadequate management abilities, and specific government policies, as many of our study participants noted, are major obstacles for Somali's SMEs. The study discovered that the region's developing SMEs are negatively impacted by nations' weak strategy on imported goods, international aids, and unrestrained rivalry.

Respondents concur that SMEs in Somalia will be improved by the government implementing successful strategy increasing SMEs through facilitating accessibility to capital via banks and big businesses. The respondents also brought up the point that giving young people the right education and training would help them build better futures for their families, the nation, and themselves.

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