

Social Capital, Charismatic Leadership and Performance of Small and Medium Size Enterprises in Western Part of Kenya

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Abstract: Small and Medium Size Enterprises (SMEs) play an important role in the economic development of a country. However, existing research in Kenya indicate that their survival rate is low. To address the constraints of SMEs performance, most practitioners and scholars have suggested the use of innovation, technology, knowledge management, human capital and intellectual capital. Indeed, there is little research on how social capital can improve the performance of SMEs. Further, the role of charismatic leadership and social capital in SME performance remains largely unexplored. Therefore, the main objective for this research was to investigate the moderating role of charismatic leadership on the relationship between social capital and performance of SMEs. The specific objectives of this study were: to investigate the effect of social capital indicators on SME performance and to examine the moderating role of charismatic leadership on the relationship between the social capital indicators and SME performance. The study employed explanatory research design and data was collected using a structured self-administered questionnaire. It targeted the top managers of 5,100 SMEs in the four Counties in Western Kenya. Stratified sampling was used to determine the sample size of SMEs from both service and manufacturing sectors and then simple random sampling was done to select the SMEs. In total, a sample of 357 was used in the study. A pilot study was carried out in Kisumu County. Instrument reliability was tested on the pilot study and all the instruments yielded a Cronbach's Alpha above 0.6. Data was coded, entered into SPSS 20 program and analyzed using descriptive and inferential statistics. Factor analysis was done to ensure content, construct and discriminant validity. Hierarchical multiple regression model was used to test the hypotheses. The results reveal that the social capital indicators; social network ($\beta=.104$, $p\text{-value}=.024$), trust ($\beta=.106$, $p\text{-value}=.026$) and co-operation ($\beta=.202$, $p\text{-value}=.002$) had a positive and significant relationship with SME performance hence hypotheses 1, 2 and 3 were not supported. The study further revealed that charismatic leadership moderates the relationship between social network and SME performance ($\beta=-.1073$, $p\text{-value}=.016$) thus hypothesis 5 was not supported. However, charismatic leadership does not moderate the relationship between; trust and SME performance ($\beta=-.134$, $p\text{-value}=.140$) and; co-operation and SME performance ($\beta =.188$, $p\text{-value}=.122$) thus hypotheses 5 and 6 were supported. In conclusion, social capital of a top manager plays a significant role in SME performance and that the charisma of the manager in relation to social network only, influences SME performance. The findings are therefore invaluable to the SME sector in relation to development of social capital of the managers which play a significant role in firm performance. Further recommendation from the study is that firms should take a proactive approach towards promoting, building and maintaining social networks coupled with trust and co-operation among their structures. The findings informs practitioners both in the public and private sector to factor in social capital particularly social network coupled with charismatic leadership attributes when sourcing for managers to efficiently run SMEs.

Keywords: Social capital, charismatic leadership performance of SME's, western part of Kenya.

1. INTRODUCTION

There is no universal definition of Small and Medium sized Enterprises (SMEs). Definitions vary from country to country. The World Bank (2002) has also defined SMEs as Micro enterprises having 1–9 employees; small scale enterprises 10–49 employees and medium 50–249 employees. In Kenya, SMEs are defined as businesses in both formal

and informal sectors, classified into farm and non-farm categories employing 1-100 workers. Worldwide, SMEs are recognized as engines of growth and development and they are the backbone of the economy in many successful developed nations all over the world. The enterprises cut across every sector of the economy. It includes general trade such as wholesale and retail, services, farm activities and manufacturing. SMEs have emerged as a vibrant and dynamic component of the economy by virtue of their significant contribution to Gross Domestic Product, industrial production and exports (Dunne & Hughes, 2003). In the world over, SMEs, are largely recognized as engines of growth and development and are the backbone of economy in many successful developed nations (Zhou and Luo, 2007). According to World Bank (World Bank, 2002) SMEs have such a crucial significance in the development of an economy that they can't be ignored hence their development should form one of the objectives of any country (World Bank, 2002). In Finland, for instance, more than 99% of all firms are SMEs, firms with fewer than 250 employees, constitutes more than one half of all firms, if measured by the number of personnel (61%) or by turnover (51%) (Federation of Finnish Enterprises, 2002). In Nigeria, the 2012 Enterprise Baseline Survey revealed an existence of 17 million Small and Medium Scale Enterprises, employing 32.41 million persons and contributing about 46.54% of Nigeria's Gross Domestic Product in nominal terms. In Malaysia, SMEs contribute about 38% to the country's GDP (World Bank, 2014). In general, the SME sector can thus contribute to the GDP of high income countries by as much as 51 percent and the middle and low income countries SMEs can produce up to 39% and 16% respectively of local GDP (World Bank, 2014).

SMEs in the Kenyan Context:

The importance of SMEs has been emphasized in all development plans in Kenya since independence in 1963. Active participation in this sector by the government began in 1992 when the government developed Sessional Paper No. 2 on Unemployment where the government identified its primary challenge as its ability to find ways to help accelerate the expansion of SMEs as a strategic avenue of job creation in Kenya (GoK, 1992). In the 1986 Sessional Paper No. 1 on Economic Management for Renewed Growth, the government acknowledged the increasing importance of the informal sector in economic development with respect to employment creation, particularly in the face of the economic crisis and structural adjustment policies that were prevailing at that time (GoK, 1986). In 1989, the government published a document entitled, "A Strategy for Small and Medium Enterprises (SMEs) Development in Kenya: Towards the year 2000. The document focused on the constraints the sector was experiencing. Sessional Paper No. 2 of 1992 on Small enterprises and Jua Kali Development in Kenya set out a policy framework to enhance assistance to individual entrepreneurs and small scale enterprises. SMEs cut across all sectors of the Kenyan economy and provide one of the most prolific sources of employment creation, income generation and poverty reduction. According to the Sessional Paper No. 2 of 2005 substantial funds have been spent to implement Government policies and programs, and to build institutions specifically aimed at promoting the SME Sector since independence. The sector is considered as one of the major contributors to the Kenyan economy by providing income and employment to a significant proportion of the population. Available data show that about a decade ago, SMEs in Kenya employed 3.2 million people and accounted for 18% of national GDP (Woldie *et al.*, 2008). According to the Kenya Economic Survey 2014, employment within the SME sector increased from 9.2 million persons in 2010 to 10.5 million persons in 2013 accounting for 75.3 percent of the total persons engaged in 2013. In view of this, Kenya government has put a lot of emphasis on the growth of this sector and as a result, in 2013, SMEs contribution to GDP rose up to about 70% (Kangai, 2014). However, this sector has continuously remained stagnant in terms of growth and expansion. As vital as they are, SMEs have low survival rate, less than a third of their business survive transition from first to second generation ownership and those that do, about half do not survive the transition from second to third generation ownership (Bowman, 2006). In Kenya, their survival rate is deteriorating with alarming rate (Kangai, 2014). These firms have continued to experience many constraints like poor access to markets and financial services, lack of innovativeness, poor access to information, unfavorable policies among others that have inhibited the realization of their full potential. This therefore implies the need for intervention and more research on various concepts of their business and operations to enhance their performance.

Statement of the Problem:

In the global economy, SMEs are largely recognized as engines of growth and development and are the backbone of the economy in many developed nations (Zhou, 2007). SMEs play significant role in the economic development by creating employment, wealth creation, poverty eradication and creation of new firms (Musimba, 2012). In Kenya, the sector contributed about 70% of GDP in 2013 (ROK, 2014). In Kenya, despite having several SMEs startups, there is a high rate of collapse and most enterprises are short lived and barely survive third anniversary. Sessional paper No. 2 of 2005 shows that despite the significant role by the SMEs, they have continued to experience many constraints like poor access

to market and financial services and unfavorable policies. These have inhibited the realization of its full potential. Kirigo (2010) indicated that no detailed study has addressed the relationship between social capital and the performance of SMEs and the impact of social network on the overall growth of small enterprises. A study by Musimba (2012) concludes that the survival and performance of a firm are influenced by the firm's ability to utilize social capital. This is alluded to the fact that connections and relationships and networking both at home and abroad are crucially important for SMEs seeking to export or invest. The relationship between social capital and leadership is documented in literature, but there is limited understanding of the dynamic nature of this relationship and lack of sufficient evidence to support an assertion that social capital significantly influences leadership styles or vice versa. Hence, with the shared nature of social capital and leadership attributes, some researchers and theorists visualize charismatic leadership as a societal process. And while there is scanty empirical evidence on how social capital affect SME performance (Lawrence, 2008; Cooke & Clifton, 2010); Stam *et al.*, 2013; Kangai, 2014), the role of charismatic leadership in this relationship has not been studied. This study, therefore, endeavored to examine the effect of social capital on SME performance and the attendant moderating role of charismatic leadership.

General Objective of the Study:

The objective of this study was to investigate the influence of social capital on performance of SMEs and the moderating role of charismatic leadership among SMEs in Western Kenya.

Specific Research Objectives:

To examine the relationship between social network and performance of SMEs

Research Hypotheses:

H₀; There is no significant relationship between social network and performance of SMEs.

2. RESEARCH DESIGN

The study employed explanatory research design. The design was therefore used to determine the relationship between the variables in the model.

Target Population:

The study targeted SMEs in the Western Part of Kenya. The region has about 5100 SMEs operating in a formalized organizational structure, mostly concentrated in the region's urban center and heterogeneous in nature (Kakamega County; Industrialization, Trade and Enterprise Development Office, 2014). The SMEs are mostly in the manufacturing and the service sector with the latter constituting about 70%; (Kakamega County; Industrialization, Trade and Enterprise Development Office, 2014).

Sample Size:

From a target population of approximately 5,100 SMEs, a formula by Fisher (2007) was used to calculate the sample size as follows; $n = z^2 pg/d^2$

$$n = \frac{(1.96^2)(0.5)(0.5)}{(0.05)^2}$$

$$n = 384$$

Where;

n=the desired sample size

z= the standard normal deviation at the required C.I=1.96

p=proportion in the target population estimated to have characteristics of interest=0.5

q=1-p=0.5, d=the level of statistical significance set = 0.05.

Because the target population is less than 10,000, the following formula has been used to determine the actual sample size;

$$nf = \frac{n}{1+n/N}$$

$$nf = \frac{384}{1+384/5100}$$

=357.1096, rounded to 357

Where;

nf=required sample size when population is less than 10000

n=required sample size when population is more than 10000=384

N=estimated population=5100

Therefore, 357 was the final sample size that was studied.

Stratified sampling targeting both the SMEs in the service and manufacturing sector was used to select respondent SMEs to participate in the study. The strata included county, Type/Nature of SME and sample size.

Simple random sampling was then used to select respondents from each stratum thus ensuring that that each respondent had an equal chance of participating in the study.

Data collection Instruments and Procedure:

Data was collected using valid and reliable data measurement tools as summarized in table 3.2 below.

Table 1: Data Collection Tools

Variable	Type of Data	Data collection tool
Social capital	Quantitative	Putnam’s Social Capital Questionnaire(Lene and Gert, 2000)
CharismaticLeadership	Quantitative	Conger and Kanungo’s “C-K” Charismatic LeadershipQuestionnaire.((Conger and Kanungo, 1994, 1998; Conger, Kanungo, Menon, and Mathur, 1997).
Performance of SME	Quantitative	Firm Growth Questionnaire, an extension of Santos and Brito (2012) Questionnaire

Source: researcher (2015)

3. DATA ANALYSIS, PRESENTATION AND INTERPRETATION

Data was collected from dully-filled questionnaires from the field, coded and entered into a computerized SPSS 20 program, verified, and missing data were deleted. The individual item scores in the social capital elements, performance of SMEs and charismatic leadership surveys were recorded. Demographic data were also coded and recorded accordingly. There was a total of 89 items coded. Data analysis was done using both descriptive and inferential statistics. Assumptions underlying the multivariate analysis were conducted using descriptive and correlation analysis. To test the relationship of variables in regression analysis, correlation analysis was done using Pearson’s Product Moments correlation. Variables depicting a high level of correlation may indicate multicollinearity. Scale reliability and validity were assessed using Cronbach’s coefficient alpha. Factor analysis was used as a variable reduction technique. Descriptive statistics such as mean, frequencies and percentages were computed to summarize data into meaningful forms. The study hypotheses were tested using multiple regression analysis.

Results on Correlation Analysis:

Correlating the variables the results indicated that there was a statistically significant positive correlation between the predictor variables and SME performance; social network (r=.119, p<.001). The correlation between social network and charismatic leadership was found to be statistically significant but negative (r=-.131, p<.001).

4. SUMMARY AND DISCUSSION OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

Summary of Findings:

The main purpose of this research was to test the effect of social capital on performance of SMEs and examine the moderating role of charismatic leadership on the relationship between social capital and performance of SMEs. The study tested a total of six hypotheses of performance of SMEs. The first set of hypotheses relates to the theory of social capital indicators. This set tested hypotheses one, two and three which examined the influence of social network, trust and co-operation on performance of SMEs. The second set of hypotheses tested the moderating effect of charismatic leadership on the relationship established in the first set of hypotheses. The results provide good support for the effects of social capital indicators on SME performance thus hypotheses 1, 2 and 3 were not supported. Hypothesis 4 was also not supported confirming that charismatic leadership has a significant moderating effect on the relationship between social network and SME performance. The results of the study advanced knowledge on the empirical evidence of the importance of social capital on firm performance. It was also established that charismatic leadership only significantly moderates the relationship social network and SME performance and not the other indicators of social capital (trust and co-operation).

Discussion of Findings:

The study results found that social capital variables exerts statistically positive effect on SME performance, thus supporting existing researches and theories. The theory of social capital hypothesizes that, networks of relationship grant access to resources, especially information benefits not available to non-members of the network and that social capital is a resource that facilitates production. The findings also support existing researches by concurring for instance, with Cooke & Clifton, (2010), who sought to establish the extent to which social capital affects the performance of technological SMEs in the UK. The research found statistically significant association between use of social capital and the other performance measures (growth, quality standards), but innovation provided the clearest results.

Effect of Social Network on Performance of SMEs:

This was objective 1 in the study that sought to determine the direct influence of social network on SME performance. The results indicate that social network significantly influences SME performance. The findings suggested that by having social and economic bonds, SME actors are likely to enhance their resource mobilization and leveraging capacities which in turn can significantly improve their performance.

Conclusions of the Study:

This research addressed the gap in the literature by examining the relationship between social capital and SME performance by incorporating a moderating effect of charismatic leadership on such relationship. Charismatic leadership moderated the relationship between social network and SME performance, an indication that charisma is very important in social networking. Generally, charisma is an important factor in academia and popular culture when it comes to leadership but it seems based on this study, charisma does not moderate the relationship between a C.E.O's trust; and co-operation and SME performance. In conclusion therefore, social network of a top manager coupled with charisma can significantly improve SME performance. However, charisma might not play a role in the manager's trust and co-operation on SME performance.

Recommendation of the Study:

From the findings, several recommendations emerge which can broadly gouged into policy recommendations and recommendations for extension of theory and practice.

Policy Recommendations:

The results shows that social capital is critical to performance of SMEs; that it helps to get things done and helps in the attainment of an SMEs objectives. This research suggests that broad and strong business networks provide a great vehicle for market expansion, and allow for extracting more benefits in terms of resources, opportunities, risk-reduction and mutual support. The findings are therefore invaluable to the SME sector in relation to development of social capital of the managers which play a significant role in firm performance. In view of that, the study recommends that firms take a proactive approach towards promoting, building and maintaining viable social networks coupled with trust and co-operation within their structures in order to derive maximum benefit from it.

Recommendation for Extension of Theory and Practice:

The researchers in strategic management should expound on this study so as to contribute to the extension of the Community field theory of social capital, theory of firm performance and Weber's theory of charismatic leadership. The study successfully extends knowledge in firm performance by introducing charismatic leadership as a moderator variable. Practitioners in the SME sector need to factor in social capital when sourcing for managers to efficiently run the SMEs. Particularly, consider individuals with social network coupled with charisma. Finally, entrepreneurs and managers should recruit more resource-rich ties into their personal networks.

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