

## Challenges Faced by Small Businesses in Registering Companies in Rural Kwazulu-Natal

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**Abstract:** The research investigated challenges faced by small businesses in registering companies in rural KwaZulu-Natal province of South Africa. uMzinyathi District Municipality in KwaZulu-Natal was used as a case study, representing the rural context of the province investigated. A sample of ten small businesses within the uMzinyathi Small Business Forum which represents all local municipalities of the district, together with stakeholders such as the Small Enterprise Development Agency (SEDA), the Department of Economic Development, Tourism and Environmental Affairs (EDTEA), the Small Business Unit staff members and a consultant who deals with the registration of companies were selected, using purposive sampling to collect data. The key findings of the study indicated that small businesses in rural areas are affected by many challenges which differ from their urban counterparts. These include socio-economic conditions, lack of small business support institutions and local government related challenges as a result of their being in rural areas. The research findings were critical for establishing effective service delivery interventions that could improve small business development and enhance the participation of small businesses in local initiatives within rural areas.

**Key words:** Small businesses, business development, registration, rural areas, South Africa, government

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### INTRODUCTION

Small businesses are increasingly becoming a major feature of economic development policy in developed and developing countries, because of their contribution to employment creation improving of the socio-economic conditions of poor communities (Ndabeni, 2008; Okon and Edet, 2016). South Africa also recognises the growing and important role played by small business in economic development. This has been emphasised and demonstrated by the formulation of a number of policy initiatives that are already in place in South Africa encouraging and supporting the development of small businesses.

The KwaZulu-Natal Provincial Growth and Development Strategy (PGDS) put job creation as the number one strategic goal and the development of small enterprises as one of the priorities of the KZN Province. The strategy commits the province to promoting Small Medium and Micro Enterprises (SMMEs), entrepreneurial and youth development in which a number of new small businesses are expected to be registered and established in an endeavour to reduce unemployment rate in the

province. However, it also undertakes to reduce red tape and regulation burdens that often inhibit small businesses from contributing to the economic growth.

The district which was used to investigate challenges of small businesses in rural KZN was the uMzinyathi district municipal area which is one of the 10 districts within the KwaZulu-Natal province. According to, KZN Provincial Spatial Economic Development Strategy (PSEDS) (2004), the district has four local municipalities, namely, eNdumeni, Nquthu, Msinga and Umvoti municipalities which have distinct development features. Endumeni has a strong coal-mining industry and has been associated historically with the towns of Dundee and Glencoe. Cattle and crop farming are currently key features of the economic landscape. Nqutu is located to the east of Endumeni, the town of Nqutu being the main rural centre. The predominant land use within the municipality is traditional settlement. Msinga is generally viewed as one of the municipalities with the highest poverty levels in South Africa. Tugela Ferry is the only significant rural centre serving the population of nearly 200000 people in the municipality.

Umvoti is the southernmost municipality of the district and has a strong agricultural economy with timber being the major product of the region. Out of four local municipalities within the uMzinyathi District, only eNdameni is an urban area: three municipalities are rural municipalities with tribal authorities dominating the area. Communities living in these areas are largely previously disadvantaged and relatively dispersed with limited service delivery (KZN PSEDS in 2004). uMzinyathi District which is in KwaZulu-Natal was selected due to its rural context.

Rural entrepreneurship is considered as one of the solutions to poverty and migration while augmenting development employment in rural areas. Small businesses in rural areas are experiencing worse challenges than those in urban areas, owing to the locations of their businesses (Dejardin and Fritsch, 2011). If the regulation entry persists and conditions of rural areas are not dealt with the National Development Plan goals of stimulating entrepreneurship may be difficult to achieve. A need therefore arises to investigate reasons, despite government efforts for a persistent failure of small businesses in rural areas. It is of paramount importance to job creation and economic growth of the country that small businesses be able to start up and maintain momentum.

The KZN Department of Economic Development, Tourism and Environmental Affairs (EDTEA) as the department mandated to grow the economy of the province is tasked with developing new businesses in order to stimulate entrepreneurship. Furthermore, it must encourage communities to participate actively in the economy by taking advantage of local economic opportunities in their areas, especially in rural areas. This therefore includes the facilitation of registration of new business companies.

The objectives of the research were to: understand challenges facing rural entrepreneurs; examine the registration process in rural areas and develop strategies to stimulate entrepreneurship and participation by rural communities in the local economy.

Various research studies such as Djankov *et al.* (2002), Renski (2009) and Stel *et al.* (2007) have been conducted locally and abroad, dealing with new business formation. However, these studies mainly deal with business formation and regulations affecting small businesses at a broader level without necessarily examining the environment within which the businesses are placed. This study examined regulation challenges that affect the formation of businesses, specifically in the rural context.

The study aimed at investigating challenges faced by small businesses in registering companies within rural KZN. The study was focused specifically on uMzinyathi as a rural municipality of KwaZulu-Natal.

The following objectives were identified:

- To analyse process efficiency in company registration
- To identify challenges for small businesses in rural areas when registering new companies
- To establish whether small businesses are using opportunities offered by LED in their areas; and
- To improve company registration processes in rural areas

**Small businesses in the rural context:** Governments around the world have come to recognise the vital role that is played by small enterprises in helping to achieve industrial and economic development objectives. In many countries, enterprise development is perceived as the strengthening element for the integration of small firms with potential for growth and expansion into the mainstream economy which leads to accessing value-chain-system opportunities for modern industries (Morales-Nieto, 2008).

Pemberton and Goodwin (2010) recognised that in developing economies, small businesses provide a balance between supply and demand in the job markets, creating competition between businesses that leads to the more efficient utilization of resources. Developing countries are characterised by rural settings which have high levels of poverty by comparison with well-developed countries and they have identified rural business development as a priority and an important issue on their agendas.

Pooe and Mafini (2012) re-affirm this by pointing out that in many rural settings, business development is an important driver of economic growth which results in job creation innovation, entrepreneurship, skills development and infrastructure development, inter alia. The development of small businesses in emerging countries which have rural settings is hampered by several challenges including burdens associated with business company registration regulations and compliance. Challenges include being able to obtain credit and access to electricity and public services (Kapteyn and Wah, 2016).

Siemens (2010) stresses that the value of the small business sector is recognised in economies world-wide, irrespective of the economy's developmental stage. Small businesses represent an important vehicle by which to address the challenges of job creation, economic growth and equity in many countries. Throughout the world, it has been noted that small businesses are playing a critical role in absorbing labour, penetrating new markets and generally expanding economies in creative and innovative ways.

Fray (2010) describes Local Economic Development (LED) as the collaboration between communities, businesses and governments at local level to restructure economic situations with the view to stimulating economic growth which will create jobs and reduce poverty. He further highlights that the purpose of LED is to take advantage of local resources in building the economy which will change the quality of lives of people at a local level.

Wille *et al.* (2011) point out that business registration is increasingly recognised as an important gateway for small businesses to enter the formal economy. Formal registration of businesses increases their chances of rights benefits such as access to government services, fair treatment under law and limited liability when their businesses become insolvent. Registered businesses also have growth opportunities through improved access to finance and potential clients in the private sector and to government institutions. Formalization also involves increased obligations including compliance with tax laws as well as regulatory and information disclosure requirements (Wille *et al.*, 2011).

In terms of the World Bank (2013), South Africa has made some progress in business reforms aimed at stimulating and encouraging the participation of small business within the economy. The findings from the study conducted by the World Bank indicated that South Africa was better than all the other BRICS countries in terms of the entrepreneurial regulatory framework.

The rural development frame work in 1997 indicates that almost three quarters of people below the poverty line in South Africa are living in rural areas. It defines rural areas as having the following two characteristics: sparsely populated areas in which people farm or depend on natural resources including villages and small towns that are dispersed through these areas and areas that include large settlements in the former homelands which depend on migratory labour remittances as well as government social grants for their survival and typically have traditional land tenure systems.

Recognise the positive effect of LED on the establishment of new businesses in which communities participate in the economy and the development of their areas. However, the formation of new business and its sustainability is influenced by the population density and the level of employment in the area which are needed for product demand and human resources supply. Employment tends to be concentrated more in urban areas than rural areas which slows the pace of growth of small businesses established in rural areas.

The state of development found in different areas affects and influences the dynamics of entrepreneurship that may be established. The local economic development

level is influenced by interconnections between development and the entrepreneurship institutions. These interconnections are also affected by other needs, such as the quality of governance, accessibility and the perceptions of entrepreneurs towards the entire development and the value-chain dynamics (Acs *et al.*, 2008).

## **MATERIALS AND METHODS**

The research sought to understand the challenges faced by rural small businesses when registering their companies. This meant focusing on the human aspect of behaviour and characteristics by investigating individual experiences, feelings, opinions and perceptions (Leedy and Ormrod, 2014). The study therefore employed the qualitative research approach. The chosen method of gathering data was to interview the selected participants and to adopt a semi-structured approach in which the largest part of the interviews was guided by a list of questions and issues to be explored.

Prior to data collection, Siyanqoba Business Forum, located in uMzinyathi District municipal area, the consultant, EDTEA and SEDA's head offices were contacted and informed of the purpose of the research. These entities were purposefully contacted to request their permission to undertake the research within their institutions: permission was granted. Owing to their willingness and particular interest in participating in the study, signed gatekeeper letters granting permission were promptly received from the Siyanqoba Business Forum, EDTEA, SEDA and the consultant.

A total of 15 semi-structured interviews were conducted face to face with participants. The participants were from ten small businesses who had registered their business companies in 2013 and who were also members of a business forum in the uMzinyathi District of Kwa-Zulu Natal; two district managers from the Department of Economic Development Tourism and Environmental Affairs, dealing with small businesses; two managers from the Small Business Development Agencies and one consultant who registers companies in rural areas. This allowed diverse perspectives to be gathered on the research topic. Interviews were conducted in different settings which included offices and municipality boardrooms and which were negotiated with participants and agreed upon.

The sample of respondents who shared their experience in registering their businesses were interviewed in their language which is isiZulu; all the information was translated into English. This ensured that participants felt comfortable and able to express their

**Table 1: Demographic Information: interview respondents**

Respondent	Area of work	Occupation	Gender	No. of years in business
R1	Uthukela	Small business development practitioner	Male	6
R2	Vryheid	Consultant	Male	10
R3	Nquthu	Small business	Female	1
R4	uMzinyathi	Small business development practitioner	Female	5
R5	Amajuba	Small business development practitioner	Male	10
R6	Durban	Small business development practitioner	Male	6
R7	Nquthu	Small business	Female	3
R8	Nquthu	Small business	Female	3
R9	Nquthu	Small business	Male	3
R10	Msinga	Small business	Male	2
R11	Msinga	Small business	Female	2
R12	Msinga	Small business	Female	3
R13	Msinga	Small business	Female	2
R14	Dundee	Small business	Male	4
R15	Dundee	Small business	Female	4

views succinctly. Using the respondent’s own language was important in collecting data, because of the possibility of misunderstanding and losing the real meaning of data when interpreters are used. An interpreter was not used as the main researcher was fluent in both isiZulu and English (Welman *et al.*, 2005).

The duration of each interview session was from about 45 min to an hour. A digital recorder was used to record interviews and all interviews were transcribed. This ensured that all information was still fresh, thereafter being stored on computer to facilitate data analysis. The interviews took place over 2 months, namely, between July and August, 2014. Since, the study was qualitative in nature, the research questions focused on the perceptions, views, ideas and feelings of the respondents in respect of the research topic. Ethical clearance requirements were adhered to. Participants also had to sign an informed consent form.

Table 1 indicates the demographic information of the respondents to the interviews. With regard to the secondary data, literature on LED and the formation of businesses and related documents were reviewed. The secondary data was collected from journals, dissertations, books, newspaper articles, management reports, minutes of meetings and newspaper articles.

Thematic analysis was used. Wellman *et al.* (2005) emphasise the importance of transcribing the responses of the participants for data analysis and noting of new thematic analysis that may arise on the research topic. In qualitative data analysis, responses from participants are analysed and categorised into various themes which are identified and found from the responses to be common (Creswell, 2009).

## RESULTS AND DISCUSSION

**Socio-economic conditions:** The current study findings revealed that rural areas were of different socio-economic conditions with various effects on the registration of business companies and a significant impact on the implementation of LED initiatives and the development of small businesses in the areas. The current study findings share similarities with the study findings by Huiban (2011). Differences between urban and rural areas were observed, owing to spatial location which disadvantages small businesses in rural areas. The research deals with declining socio-economic conditions of the rural areas, albeit competing equally in the global market.

The study also revealed that the socio-economic conditions of rural areas were characterised by a high unemployment rate, a large number of people depending on social grants, a high illiteracy level and the majority of the community living in poverty. The study findings corroborate Naude (2010)’s sentiments that entrepreneurship would assist communities in rural areas to escape poverty and enable them to assist themselves and their families instead of relying on the government.

**LED opportunities:** The study results indicated that the primary focus for small businesses in the uMzinyathi municipal area was to change their lifestyles which could be achieved through accessing government tenders after registering business companies. The study results are contrary to Poee and Mafini (2012)’s view that in many rural settings, business development is an important driver of economic growth which results in job creation innovation, entrepreneurship, skills development and infrastructure development, amongst other developments.

The current study also revealed that small businesses in rural areas were not participating in developmental forums and meetings such as the municipal Integrated Development Plans (IDP) at which LED opportunities are presented through various stakeholders. The study findings are in contrast with Pose (2001)'s view which highlighted that the advantages of LED over traditional economic policies are the involvement of local people in planning their own economic future and their increasing participation in local processes which create locally based initiatives in line with the local comparative advantage of the area.

The results further indicated that the unavailability of infrastructure and communication facilities in the uMzinyathi area was costing their businesses too much in accessing raw material as well as in transporting goods to their clients. Participants indicated the impact of infrastructure development on the area for the sustainability and growth of their businesses. This is consistent with Porter (2000)'s views that infrastructure and communication are important aspects of LED, yet this is overlooked in rural areas. Porter emphasised that some businesses to some extent depend on infrastructure such as transport and communication, to be able to meet demand of supply and customers.

**Local government challenges:** The study findings indicated that the uMzinyathi District municipal area had challenges such as political instability, lack of capacity in LED officials, maladministration and municipal boundaries which incurred costs and made it difficult for small businesses to access services. The current study findings are consistent with the findings by Nel and Hill (2008) and Hoogendoorn and Visser (2010) which highlighted that globalisation and a change in politics brought new trends which afford both advantages and disadvantages to small businesses.

The findings also highlighted that the municipal demarcation process which amalgamated multiple municipalities in some instances, resulted in the loss of institutional capacity and deprived many rural areas of immediate access to services and governance functions. This created barriers in initiating local activities that could have benefited the community. The study found that local government challenges were discouraging and had become hindrances for both large and small businesses in rural areas to be started and to participate in the local economy.

The current study also indicated that there was a shortage of private sector investors in uMzinyathi, owing to their bad image as a result of the maladministration and the political instability of municipalities within the district.

The study results contradict Porter (2000)'s views which emphasised that local municipality affairs are critical as they play a role in marketing the area to benefit its citizens and to attract investors who would create local economic opportunities.

In dealing with local government challenges, the study also revealed that nepotism and political appointments were used to engage staff which resulted in taking LED officials on who did not have the capacity to deal with the LED issues which could have grown the economy of the area. The result of the study was in line with study which indicated that owing to the lack of capacity of LED officials within many municipalities, various municipalities had established development agencies with the view to delegating LED initiatives that would enhance economic growth in the area.

**Inter-collaboration between government departments:**

The study findings showed that in order for communities to establish small businesses and for the private sector to invest in the uMzinyathi area, it was important for various government departments to work together to deal with the infrastructure backlog in order to enhance economic development initiatives for rural small businesses.

The study findings further indicated that accessing water, sanitation and electricity was still difficult for communities of the uMzinyathi District municipal area. This is consistent with the DNT (2012) report which also confirmed the huge backlog curtailing the conducting of business and of infrastructure services such as water, sanitation and electricity in rural areas; this, compared with urban areas in which every household has access to clean water, proper sanitation and electricity.

The findings also indicated that in some parts of the uMzinyathi District it will take an exceedingly long time for communities to participate in LED while basic needs such as water, electricity and proper sanitation are still lacking. People are migrating to better areas where they can obtain their basic needs and can start thinking about satisfying other needs than starting businesses. This study supports the findings of the study conducted by Pinillos and Reyes (2011) which recognises that there is a connection between the development of the area which satisfies basic needs such as housing, water and roads and 'higher order needs' that include achievement and prosperity. Higher order needs may stimulate individual's introspection which results in taking action such as starting a business and accomplishing a sense of achievement and prosperity through business.

**Small business challenges:** The study results showed that small businesses in rural areas have challenges which

are different from their counterparts in urban areas, owing to the location of their businesses. The study findings corroborate the research findings of the (OECD, 2005) report on rural entrepreneurship in 2005 which indicated that there are also policy issues that create challenges for small businesses in rural areas. The current study findings also support the findings by Nieman and Nieuwenhuizen (2009) that entrepreneurs would find it difficult to market their businesses, access finance and grow the businesses if location factors such as political and social stability and the pool of labour and skills are not favourable to external stakeholders.

**Registration process:** The study results revealed that the majority of small businesses view the registration of business companies as a burden imposed by government. The study results also indicated that there were some companies that were doing well in business despite not registering their companies. The study results show a different view from the Wille *et al.* (2011) study which found that business registration is increasingly recognised as an important gateway for small businesses to enter the formal economy. The explanation of these findings is that the formal registration of businesses increases their chance of rights benefits such as access to government services, fair treatment under law and limited liability should the business become insolvent. The findings further indicated that the notion that registered businesses have opportunities to grow through improved access to finance and potential clients in the private sector and government institutions differs from that understood by the current study findings.

The current study findings also indicated that there are many compliance issues such as Black Economic Empowerment (BEE), tax and sector compliances having to be followed when starting a business which become barriers for small businesses in rural areas to register business companies and to participate in the economy. The result of the study is consistent with the research findings by Acs and Storey (2004) that business entry barriers prevent new businesses from entering the market. The current study finding is also supported by the finding of the study conducted by Woodruff (2013). The study by Woodruff (2013) found that the tendency of small businesses to remain in the informal sector is sometimes caused by government which creates many regulation entries that become barriers to starting a new enterprise. The participants in the study suggested a one-stop shop that would deal with all compliance issues when the business is registered without small businesses having to go to various offices.

The current study results indicate the shortage of communication facilities such as post offices and Internet facilities in the uMzinyathi area. The lack of communication facilities has had a significant negative impact on the company registration process for small businesses in rural areas which takes time and becomes costly.

The results indicated that small businesses preferred to register their companies through service providers, even though such entities charged exorbitant amounts, because of their turnaround time in delivering services compared with government departments who take an excessively long time to register business companies. The period taken by government departments to register business companies is associated with inefficiency and the poor quality of services in government institutions. The current study findings have similarities with Williamson (2000)'s study which indicated that there is inefficiency and poor quality of services experienced in government small business support institutions which are protected by regulation in the country and which create challenges to rural communities entering the business sector. Williamson highlights that poor government activities are costing money and are discouraging poor communities from registering business companies. Hence, small businesses revert to private service providers to gain assistance.

The study results reflected that the services of the Companies Intellectual Property Commission (CIPC) have been centralised to the pretoria office which services the whole country. Participants indicated frustration with the inefficiency of and lack of accessibility to the CIPC offices, having no alternative of another office which could process their company registration.

The current study findings are supported by studies conducted by Aidis *et al.* (2012) and McMullen *et al.* (2008). These studies found that in most countries institutions that support the registration of companies are monopolised and controlled by government. In countries in which the institutional environment is weak and monopolised aspirant small businesses who are eager to continue, have to adapt to the systems used by available institutions, irrespective of whether these institutions bring opportunities or limitations as there are no alternatives. The study by Aidis *et al.* (2012) and McMullen *et al.* (2008) also found that monopolistic state company registration institutions do not allow competition nor a comparison process by its users, whereby they have the opportunity of comparing an expected return against alternatives when making a decision to start their businesses and register their companies.

**Small business support institutions:** The current study reveals that business support institutions such as EDTEA, SARS and SEDA were crucial to the development of small businesses within rural areas. However, these institutions were not available in the uMzinyathi district municipal areas and accessibility to them was difficult. The study findings revealed that small business owners within rural areas had to travel to urban areas to access the services of business support institutions, impeding their participation in the economy.

The current study shows that there is a strong need for the visibility of business support institutions in rural areas to stimulate entrepreneurship and to develop small businesses. The study corresponds with the study findings by Acs *et al.* (2008) which stresses that institutions supporting small businesses are critical determinants of economic behaviour and economic transactions which impose both direct and indirect effects on the supply and demands of entrepreneurs.

### CONCLUSION

This study aimed to investigate challenges faced by small businesses in registering companies within rural KZN. The study has focused specifically on the uMzinyathi district as a rural municipality of KwaZulu-Natal. The research demonstrated to a reasonable extent that small businesses in rural KZN are inundated with severe challenges that are related to socio-economic conditions, local government, location, lack of collaboration between government institutions, unavailability of business-support institutions and shortage of business networks.

A policy shift that takes into account the environment of rural areas was identified by the study in addressing challenges faced by small businesses in rural areas. These issues that were highlighted in the study, pertaining to challenges in rural areas, need to be addressed. The status quo is not conducive to a developing economy in which small businesses need to be encouraged to participate in the economy, thereby alleviating poverty and inequality and contributing to reducing unemployment.

The study only explored the challenges of small businesses when registering business companies in rural areas. A quantitative study could be conducted with more small business participants from rural areas: big business could also be included in determining their challenges when registering businesses. Registration of business companies was associated with the participation of communities in LED. Further studies should focus on the impact of the registration of business companies on the economic growth of rural areas.

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