FACTORS INFLUENCING THE ESTABLISHMENT OF SUCESSFUL BUSINESS LINKAGES BETWEEN MICRO AND SMALL ENTERPRISES AND LARGE ENTERPRISES IN KENYA

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ABSTRACT

Business Linkages can be defined as channels through which enterprises influence each other's economic performance. They show the interrelationship among various economic activities through the input-output relationships or the economic value chain. The main purpose of this study was to explore the extent of business linkages between MSEs and large firms in the various major sub sectors in Nakuru town so as to establish the levels and types of linkages between these MSEs and the large firms. The mixed method approach was used where both quantitative and qualitative approaches was adopted. A sample of around 121 MSEs in metal fabrication, chemicals, auto mobile service sector and agro-processing was selected using a multistage sampling technique and divided into strata on the basis of sector involved. Data was collected by use of a questionnaire and analyzed by use of Statistical Package for Social Sciences. Both descriptive and inferential statistics were used in reporting the study findings. Regression analysis was used to express the relationship. The study found that establishment of business linkages between MSEs and large firms was significantly influenced by technology and labour mobility. The study recommended: the formulation of policies to strengthen the coordination of institutions supporting MSE developments networks among MSEs, business linkages attraction measures should give priority to firms operating in sectors where the technological gap with local MSEs is not too high and expensive to adapt and specifically prioritize firms which are more likely to generate substantial linkages and promote the internationalization of the host economy.

Key Words: *Technology, Labour Mobility, Business Linkages, MSEs*

Introduction

Micro and Small Enterprises (MSEs) play a very important role in the economies of many countries and cut across all sectors of the economy providing one of the most prolific sources of employment, and a breeding ground for medium and large industries, which are critical for industrialization. The nature and extent of this contribution by MSEs varies between countries, reflecting differences in economic, social and institutional conditions, and ultimately the competitiveness of the sector. In this context, many transition and developing countries in particular, face a need to promote and strengthen the long term development of the MSE sector, which requires access to market opportunities, as well as to new technology and management know-how, often in a situation of considerable resource scarcity (Demo & Smallbone 2015).

According to Bwisa (2011) businesses must build networks if they are to become more competitive. Networking is a process of creating alliances with people and alliances beyond the immediate boundaries of the venture. It is a process of linking up with the right people to get things done and the difference between a successful and unsuccessful venture often rests in knowing people in the right places. For MSEs, linkages with large firms help Micro and Small Enterprises (MSEs) to learn new and better production methods and can help to increase MSE employment (Carluccio & Fally, 2012). Hirschman (1958) developed the concepts of backward and forward linkages and analyzed their importance for economic growth. He argued that the setting up of an industry brings with it the availability of a new expanding market for its inputs whether or not these inputs are supplied initially from abroad. This enhanced market exerts a backward pressure for establishing industries that supply the new entrants. He calls this process backward linkage effect. Every non-primary activity will induce attempts to supply through domestic production the inputs needed in that activity. Similarly, forward linkage effects are created when one industry uses another industry's outputs as its inputs, every activity that does not by its nature cater exclusively to final demands will induce attempts to utilize its outputs as inputs in some industries (Krammer, 2010).

For their part, large firms often rely on good quality and timely local supplies. Well-developed suppliers can stimulate more investment and help to improve the developmental impact of linkages (Te Velde, 2002). The proximity of customers and of suppliers may generate positive externalities for entrepreneurial clustering, as firms cluster and employees too, local markets grow up. These market size effects foster geographical concentration. The sum of the backward linkage effect and the forward linkage effect gives the total linkage effect, which can be seen as the growth in new industries induced from establishing an industry. Linkages between parent and satellite industries are unlikely to be as important as those formed with larger industries that have a lower probability of forming, multiple industries are likely to have a greater linkage effect when taken together, compared to simply adding up the individual effects, (Buchanana, Quan &, Rishi, 2012). The presence of two or more industries may create enough demand to surpass the threshold required for establishing new industries, whereas the presence of only one of them would not. Taking all of these industries together may provide enough incentive to create yet others. This cumulative effect may explain much of the acceleration of industrial growth seen early on in the development process. (Glass et al, 1999). Linkages can also be defined as channels through which enterprises influence each other's economic performance. Final demand linkages have to do with the incomes generated in the domestic economy by the Enterprise (Lenaerts & Merlevede 2011). Although

most of the net returns to such activity may flow abroad to foreign owners, some incomes will be generated which get spent in the domestic economy where the export industry is located. This spending will create demand for goods and services, some of which may be imported, of course, but some of which may of necessity be locally supplied (UNCTAD, 2010).

Hirschman (1958) suggested that the importance of linkages in an economy could be approximated by the percentage of inputs purchased from other industries for backward linkages and the percentage of output sold to other industries for forward linkages. He further argued that part of the difficulty for underdeveloped economies is a lack of interdependence and linkages, a scenario very common in our economy. Consequently, the development process must commence with industries that cater to final demand. This requirement leaves two possibilities: transformation of either primary goods or semi-manufactures into final products. Since the latter may provide stronger possibilities for linkages, he suggested that governments in such countries should assist industries involved in intermediate activities since these have strong potential for creating both backward and forward linkages.

Linkages between Large Enterprises and MSEs are important in the context of investment for development. The spillovers of know-how and technology from large firm which are usually foreign-invested enterprises to the rest of the business sector is one of the main benefits of FDI to development (Amendolagine et al, 2013). MSEs are found in every corner of Kenya and they have great potential for creating a variety of jobs, while generating widespread economic benefits (Sessional Paper No2 of 2005). The Economic Recovery Strategy Paper for Wealth and Employment Creation (Republic of Kenya, 2003) identified MSEs and in particular jua kali expansion as one of those activities that will assist in economic recovery and growth. In 2014, MSEs accounted for roughly 82.7 per cent of total employment creating 693.4 thousand new jobs and an estimated 18 per cent of GDP (Economic Survey, 2015. Maximizing the economic and social benefits of linkages is an important related challenge. The ultimate benefits of large firms and MSE linkages to the host country depend on the enabling environment for investment as well as the strategies of foreign-invested companies (Ndemo& Smallbone, 2015). Both host and home country authorities can play an important role in encouraging mutually beneficial linkages. They can help overcome information asymmetries, can support MSEs' capacity to engage in linkages and they can encourage large firms to engage in partnerships with MSEs (Lam, 2013).

Statement of the Problem

The various business linkages that the Micro and Small Enterprises (MSEs) can establish with large enterprises are essential factors for their growth and competitiveness. The organization of these linkages is crucial both up-stream with the suppliers and sub-contractors, and down-stream with the distribution and marketing channels (James et al, 2014). The benefits stemming from business linkages crucially depend on density, depth and nature of supplying and buying linkages between the large investors and local small firms (Amendolagine et al, 2013). Closer integration, openness to trade and business linkages are helping firms in developing countries become part of international production networks and global value chains, thereby creating new sources of growth and development worldwide (Ndemo & Smallbone 2015). Evidence shows that linkages expansion and trade liberalization need to be accompanied by a coherent policy framework both at the national and global level, enabling enterprise development and the integration of domestic markets into global markets (UNCTAD, 2010).

Despite the important role played by MSEs in the economy, the sector is plagued by a numerous challenges key among them; limited access to infrastructure, technology, finances, marketing and human resources, gender inequality, limited access to information and limited linkages to large enterprises, among others (Republic of Kenya, 2005), so overcoming the obstacles to linkages between large and small enterprises is of great developmental importance which calls for a suitable support for enterprise and human resource development in the sector in order to drive competitiveness. (Economic Survey, 2015).

Many transition and developing countries in particular, face a need to promote and strengthen the long term development of the MSE sector, which requires access to market opportunities, new technology and management know-how, often in a situation of considerable resource scarcity (Ndemo & Smallbone, 2015). The study therefore sought to assess the factors that influence formation of successful business linkages between MSEs and large enterprises as measured by levels of technology transfer, skills acquisition, improved capacities and efficiency by MSEs.

Study Objectives

The general objective of this study was to establish the factors influencing the establishment of successful business linkages between MSEs and the large firms in Kenya which in turn could lead to the development of MSE sector in Kenya and an enhanced performance by the sector. The specific objectives were:

- To explore the influence of technology on development of linkages between MSEs and large firms.
- To determine the influence of labour mobility on linkages in the MSE sector

Literature Review

Theories of Business Linkages

Clustering theory

This theory explores how interdependence between firms, industries, and public and quasi-public institutions affects innovation and growth in regional agglomerations. It is increasingly focused on the social or cultural dimensions of such interdependence, rather than the more traditional economic or technical relations between firms (Hassink 1997, Malmberg and Maskell 1997). New' trade theories and the 'new economic geography' theories make a number of predictions about the characteristics of the industries we should expect to become geographically concentrated and the characteristics of the countries where these locate. Consistent with new trade theories, empirical studies suggest that geographically concentrated industries are subject to scale economies and have a high proportion of intermediate inputs in final production; and they concentrate in countries that have access to large markets. (Amiti, 1998). The theory further advances the Marshallian externalities by arguing that the home-market effect means that upstream firms are drawn to locations where there are relatively many downstream firms. Downstream firms gain by obtaining their intermediate goods more cheaply through lower transport costs or more intense competition and having a larger variety of differentiated inputs to use in production. Upstream firms located in a region use these backward and forward linkages and produce intermediate goods, i.e. creating forward and backward linkages to customers and suppliers. According Venables, (1996 and 1998) linkages (forward and backward) make it more attractive for firms to set up in the location, and so on in such a set-up the interaction between trade costs, increasing returns to scale and linkages creates the possibility of cumulative causation, leading to the

formation of new centers of activity. Thus these linkages may give rise to an agglomeration of activity.

However, Perroux's (1950) in his theory of abstract economic space states that there is no reason why physical space should necessarily bear any relationship to economic space; enterprise linkages will extend without spatial limit throughout the globe, at least where they are economically justified. Directing one's analysis to particular regions will only provide a distorted picture of the growth and development process. In the framework, Perroux's sated that in order to understand economic growth and change, analysts need to focus on the role of propulsive industries, those industries that dominate other sectors because of their large size, considerable market power, and role as lead innovators. Propulsive industries or even individual firms represent poles of growth which attract, focus, and direct other economic resources (Darwent, 1969). The degree that large firms can use their market power to dictate or perhaps strongly encourage, even assist with technology upgrades and improved manufacturing strategies to their suppliers, such end-market industries might be said to drive, at least in part, overall cluster competitiveness. On the other hand, one can also conceive of market power among some cluster members as exerting a detrimental influence on the overall cluster.

Labour Mobility Theory

Labour mobility models explore the absorptive capacity and catching-up capabilities of local firms and on the geographical proximity to foreign affiliates. According to the absorptive capacity argument of Cohen and Levinthal (1990) domestic firms need to possess a certain level of human capital and technological knowledge in order to understand, assimilate and use incoming spillovers from foreign-affiliates. Domestic firms are better able to catch-up with superior technologies of foreign firms when the technology gap between both parties is not too large (Findlay, 1978). Spillovers may occur through movement of labour, whereby workers trained by or working in multinationals may decide to leave and join an existing or open up a new domestic firm, taking with them some or all of the firm specific knowledge of the multinational (Görg & Strobl, 2002). According to Glass and Saggi (2002) there is a trade-off between technological and pecuniary spillovers to the local economy. In their model spillovers depend on the level of diffusion with examples of workers having knowledge of a portion of technology, or may be unable to fully utilize the knowledge, as well as the number of foreign and domestic firms in the market. Pakes and Nitzan (1983) model argue that scientists and their employers realize that the scientists will accumulate knowledge when conducting research and may get a return to this knowledge by moving to another firm. Therefore, labour contracts are designed to ensure a future wage increase, which leads scientists to accept an initial wage that is below their outside option.

Conceptual Framework

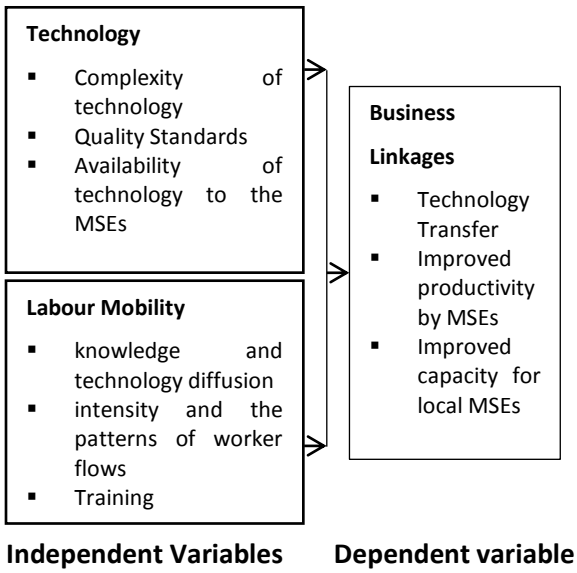

Figure 1: Conceptual Framework

Empirical review

Technology

New external linkages may upset the status quo and that small firms which do not expand their knowledge base within a cluster may struggle to keep up with new developments. The degree which large firms assist MSEs in maintaining quality, price and delivery targets through standards and production compliance measures especially for more complex products can foster upgrading through technology and skills transfer and lead-firms can also provide smaller firms with access to industry best practices, along with hands-on advice such as how to upgrade production capabilities and improve production flows. (James et al, 2014). According to (Carluccio & Fally, 2012) Technological incompatibilities can generate complex interactions between vertical linkages and technology adoption decisions, with important implications for the effects of openness to large firms and FDI in terms of technology adoption, firm selection, output reallocation and welfare. When technology adoption is costly, the effects of foreign entry on domestic firms are not uniform. In this case, foreign entry benefits the best firms and is detrimental to the low-productivity firms.

Successful linkages depend on a firms' ability to absorb external knowledge, combine it with their own proprietorial knowledge and develop new market offerings (Lenaerts& Merlevede, 2011). Small firms may be attractive partners if they possess distinctive technological capabilities but most of them are often hampered by limited management experience and suffer a power imbalance when collaborating with large firms. Relationships between large firms and MSEs are asymmetric not only because of their respective sizes, but also because their power, management, capabilities and organizational cultures differ substantially (UNCTAD, 2010). Positive linkages effects are more likely to happen when the technological gap is small, meaning the host country have the absorptive capacity needed to facilitate the transmission of positive effects. (Amendolagine et al, 2013)

Labour Mobility

Labour mobility constitutes a channel for knowledge and technology diffusion between academia, firms and industries. The intensity and the patterns of worker flows have important implications not only for the labour markets, but also for the productivity growth and overall industrial renewal in general. Worker mobility is a part of the productivity-enhancing restructuring, or the "creative destruction", that has been found to have a crucial role to play in many countries (OECD, 2001). Labour embodies productive intangible capital that is increasingly important as a factor of economic growth and is a very strong factor in the creation of Industry linkages and clusters based on human capital.in fact, industries are linked together based on labour flows (Nikulainen & Maliranta,2009). Labour mobility and human capital acquisition can boost the productivity of local firms. This emerges when domestic firms hire workers that were previously employed by a multinational. These workers might have received some sort of training and are informed about many features of the multinational's production process. If this knowledge can be implemented by local firms, it will improve their productivity. (Lenaerts & Merlevede, 2011)

RESEARCH METHODOLOGY

The mixed method approach was used where both quantitative and qualitative approaches was adopted with the aim of determining the relationship between the entrepreneurial factors

and the successful business linkages (Salkind, 1990). Descriptive research includes surveys and fact-finding enquiries of different kinds and its major purpose is description of the state of affairs as it exists at present (Kodhari, 2004). The cross sectional descriptive design which involves the collection of data in a fairly standardized form from groups of people at a single point in time was adopted because of its salient features which are the capability of describing phenomena or situations and events and obtaining information concerning the factors influencing successful linkages between MSEs and Large firms, it is also easy to design and use and also appropriate as is detailed (Anderson, 2011). The population of interest included the over 23,169 MSEs in manufacturing and service industry in Nakuru County. (NAKURU CIDP- 2013-2017). The sampling frame used was the membership registration list from the Micro and Small Enterprises Authority (MSEA) office in Nakuru of MSEs in manufacturing and service industry from four major MSE clusters; metal fabrication, chemicals, auto mobile service sector and agro-processing in Bondeni and Shabab areas of Nakuru town and was divided into strata on the basis of sector involved. The researcher used multi-stage sampling technique to get the sample. The first stage involved sampling the enterprises in their various associations in Nakuru Town. Stratified random sampling method was used where the researcher divided the sample population into different strata according to their characteristics. The researcher used self-administered questionnaires designed for the MSEs as the main instrument of data collection, comprising of semi structured both open and close ended questions to collect primary data. The questionnaires were structured with fixed set of choices closed questions and unstructured not limiting responses but to provide a frame of reference for respondents to open ended questions (Cooper & Schindler, 2003). For questioning, the researcher prepared a questionnaire which comprised of both closed and open ended questions sent to the respondents and give them complete freedom of response. The questionnaire was pretested to ensure clarity and content validity prior to it being administered. A sample size of 12 respondents was selected. Three respondents from each category were sampled using purposeful sampling to test the questionnaire. All the 12 questionnaires were returned therefore there was 100% response rate. During the pre-test the researcher was able to test the ease with which respondents were able to complete the questionnaire, the clarity and accuracy of the questionnaire instructions (Mugenda & Mugenda, 1999), the length of the questionnaires and the level of redundancy. The researcher verified that the length of the questionnaire was appropriate since all the respondents were comfortable with the time it took to fill them. Most of the instructions given were clear. However, on part C of the Questionnaire, we reframed the questions as most of the respondents said they did not understand them clearly**.**To ensure validity of the questionnaires, content validity was established from the pretest and re-test method that was done before the actual research. The pre-test retest was done in an area within the study location which was not included during the actual research undertaking. Data was analyzed both quantitatively and qualitatively since it's a descriptive study. The study employed a multiple Regression analysis to estimate the causal relationships between factors under study. With the aid of Statistical Package for Social Sciences (SPSS), the research performed multiple regressions analysis on primary data to estimate the beta values of factors and F – test statistics to determine their significance at confidence level of 95%. The results of analyzed data were presented using tables and charts with a brief description thereafter.

RESEARCH FINDINGS

To obtain a comprehensive understanding of the population structure from which the sample was taken, a preliminary analysis was carried. The results showed that the sample was male dominated. The male consisted of 62.7% of the population as compared to 37.3% female. All the respondents who were less than 18 years were employees. While for those aged 31 years and above majority of them were the enterprises owners and only a small percentage of the MSEs do employ managers. Majority of the MSEs are aged 40 years and below. 75% in Agro processing had attained tertiary education, Majority of automotive respondents (45%) had secondary school qualification. Majority (75%) of those in electronics had attained tertiary education. Farm machinery and metal fabrication had the majority having tertiary education and all of the respondents having academic qualification of secondary school and above. MSEs in furniture and manufacturing were operated by people with qualification of tertiary and below; majority been secondary and polytechnic graduates. The researcher further used chi-square to test the association between nature of business and level of education for the respondents. The results reveal a statistically significant association at a confidence level of 95% since the significance level is less than 5% (P.value=0.000 is less that 5%). The number of years of the enterprise existed did not have an association with number of employees as most of the enterprises (77.1%) had 1 to 9 employees and 10-19 employees (16.5%). Those that had existed for more than 15 years had the greatest percentage of 10-19 employees. Only 6.4% of the enterprises had employees ranging from 20-29. Also majority of the entrepreneurs had been in existence for 10 years and below. Most MSEs (82.4%) bought products from large entities before adding value and selling them later. Less than half of the MSEs were also involved in supplying large entities while only 37.3% were involved in subcontracting with other entities.

Factors Influencing Formation of Business Linkages between MSEs and Larger Enterprises

Technology was considered by majority respondents as the factor influencing formation of business linkages most significantly. This was followed by labour mobility.

The influence of technology

Majority of the respondents (42.7%) agreed that technology was of great influence in formation of business linkages between MSEs and larger enterprises. 20.9% agreed that the influence was moderate while 19.1% said that there was only little influence with 17.3% agreeing that technology influence was to great extent. The researcher further analyzed the influence of technological attributes on formation of business.

It is clear that complexity of technology, quality standards set by large enterprises; cost of technology and availability of the technology locally influenced significantly the formation of successful business linkages. On average majority of the respondents agreed that those factors influenced formation of business linkages.

Influence of Labor Mobility on Formation of Business Linkages

The respondents' views on the influence of labor mobility on formation of successful business linkages were obtained and analysed as follows. The influence of labour mobility was regarded as moderate by majority of the respondents (46.4%). 30% of the respondents regarded the influence as of great extent, 21.8% regarded it as of little influence with only 1.8% of the respondents regarding it as of very great extent. The researcher further analysed labour mobility factors. Knowledge and technology diffusion by SMEs was the most

regarded (3.77~4= Agree) labour mobility factor that influenced formation of business linkages. On average the respondents were not sure whether intensity and the patterns of worker flows influenced formation of business linkages the same as offering training formally and informally. The respondents were further asked whether their employees had worked in large firms and whether they were been offered any training. On whether any of the employees had worked in large firms, 65.5% of the respondents had no employees who had worked in large firms, while 34.5% had employees who had worked in large firms. On whether employees attended trainings, 58.7% of the respondents' employees had attended trainings either offered by their employees or other institutions while 41.3% of the respondents had not attended any. Majority of the respondents had received training in general business management from government departments and NGOs. There were some however who had undergone skills upgrading trainings.

Business Linkages

The researcher in a summary evaluated the state of current business linkages comparing the two variables under study: technology and labor mobility. The results clearly showed that majority of the respondents agreed that technology complexity of the large and adaptability by the MSEs affected formation of business linkages. The respondents were neutral on influence of labour mobility and imports and exports on formation of business linkages.

SUMMARY OF RESULTS, CONCLUSION AND RECOMMENDATION

Summary of the Study

Technology

The researcher analyzed the influence of technology and technological attributes on formation of business linkages between MSEs and Large enterprises with majority of the respondents (42.7%) agreed that technology was of great influence in formation of business linkages between MSEs and larger enterprises. The researcher further analyzed the influence technology complexity, quality standards set by the large firms and cost of the technology as some of the technological attributes on formation of business linkages between MSEs and large enterprises and majority of the respondents agreed that those factors significantly influenced the formation of business linkages.

Influence of Labor Mobility on Formation of Business Linkages

The findings revealed that there was a significant statistical association between the variable parameters of labour mobility and business linkages. The parameters under study were; technology diffusion, availability of skilled and knowledgeable workers, worker flows and training. The findings indicated that 65.5% of the respondents had no employees who had worked in large firms, while 34.5% had employees who had worked in large firms which enabled them to gain the relevant skills. The findings also showed that 58.7% of the respondents' employees had attended trainings either offered by their employees or other institutions while 41.3% of the respondents had not attended any.

Conclusion

The study established the factors influencing the establishment of successful business linkages between MSEs and the large. From the study, it was agreed that technology was of great influence in formation of business linkages between MSEs and larger enterprises and especially the complexity, cost and availability of the technology used by the large firms, and the standards set by the large firms

to the MSEs engaging in business linkages with them. The availability of knowledgeable and skilled workers, ability of the MSEs to absorb new technologies, the intensity and patterns of worker flows and trainings offered have also had an impact on the formation of successful business linkages between MSEs and Large firms.

Recommendation

In line with the finding, the study recommends the formulation of policies to strengthen the coordination of institutions supporting MSE developments networks among MSEs, policies aimed at facilitating partnership between MSEs and large firms should be implemented at the entry phase, and policymakers should not disregard the importance of building effective markets and institutions. Business linkages attraction measures should give priority to firms operating in sectors where the technological gap with local MSEs is not too high and expensive to adapt. The attraction policies should prioritize firms which are more likely to generate substantial linkages and promote the internationalization of the host economy.

Areas for Further Study

The study was limited to the factors influencing the formation of successful business linkages between MSEs and larges firms. A study on the nature of linkages between MSEs and large firms and their contributions and benefits to the growth of MSEs and local economy will also bring more light to this field. There is also a need to explore the influence of skills acquired in the foreign investments on formation of business linkages.

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