

**East Africa Collaborative Ph.D. Program  
in Economics and Management**

**The Contribution of Institutional Environment  
and Support to the Growth of Small and  
Medium Enterprises in Rwanda:  
A Survey of SMEs in Kigali**

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**East Africa Research Papers in Business,  
Entrepreneurship and Management**

**EARP-BEM No. 2018:09**

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## **Preface**

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# **The Contribution of Institutional Environment and Support to the Growth of Small and Medium Enterprises in Rwanda: A Survey of SMEs in Kigali**

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## **Abstract**

Although market reforms in developing economies date back to the 1980s and early 1990s no empirical studies have assessed whether the institutional environments in these economies are favorable for small and medium enterprises (SMEs). This followed a recent effort to do so in the context of the developed and emerging economies in Eastern Europe and Latin America, our research developed a valid scale to comprehensively measure institutional environments in developing economies. SMEs are found in every sector of the economy and are crucial for sustained long term growth and employment. Despite the different initiatives to enable SMEs to survive in their operations, most of them have failed. Therefore, the purpose of this study is to ascertain the contribution of an institutional environment and support to the growth of SMEs in Rwanda. Our results show that the factors that make up an institutional environment for SMEs' growth in Rwanda include accessibility to finance, market and training in entrepreneurship skills and knowledge and SMEs' abilities to interpret the environment. The findings indicate that there is a need for improving the factors that affect the institutional environment for SMEs in Rwanda.

Keywords: Institutional environment, institutional support, SME growth.

JEL Classification Codes: G28; L26; O43; O44.

## **1. Introduction**

Institutional theory contends that a firm's external environment is governed by institutions that have a wide range of social structures including rules and norms (Scott, 2004). In addition, institutional theory also focuses on the deeper and more resilient aspects of the social structure. It considers the processes by which structures including rules, norms and routines become established as authoritative guidelines for social behavior (Scott, 2004). Different components of institutional theory explain how these elements are created, diffused, adopted and adapted over space and time and how they fall into decline and disuse. Institutions lay down the rules of the game to which economic players such as business firms must conform to earn legitimacy that boosts their chances of economic survival and relative performance (Chen and Roberts, 2010; North, 1990; Scott, 2004). These rules may take the form of laws, regulations, norms, social conventions and other written or unwritten rules of conduct (Chen and Roberts, 2010).

SMEs' growth is essential for the economic development of nations. This is especially relevant in less developed countries such as Rwanda with serious problems of unemployment and poverty. How to promote the growth of small and medium enterprises has therefore been a central issue with policy planners in developing economies around the world. This topic has evoked considerable interest among scholars of entrepreneurship in recent years. The rate and trajectory of entrepreneurship in developing economies is significantly influenced by their institutional environments (Bruton and Ahlstrom, 2002; Peng and Heath, 1996; Smallbone and Welter, 2001).

Although market reforms in the developing economies date back to the 1980s and early 1990s no empirical studies exist which assess whether the institutional environments in these economies are favorable for small and medium enterprises. In fact, there are no valid scales to comprehensively measure the institutional environments in developing economies underscoring a need to develop good constructs and metrics for this purpose. Following a recent effort to do so in the context of the developed and emerging economies in Eastern Europe and Latin America (Manolova et al., 2008), our study first validates an instrument proposed by Busenitz et al., (2000) in the context of western industrialized countries to two emerging economies in Latin America: Brazil and Mexico. It then applies this instrument to assess the relationship between institutional environment and support to SMEs' growth in Rwanda.

SMEs are found in every sector of the economy and are crucial for sustained long term growth and employment (Macdonald et al., 2007). Specifically, Rwanda has institutions that have helped develop and support SMEs in the country. These include the Ministry of Trade and Industry (MINICOM), which is helping sensitize people to develop an entrepreneurial culture through the 'HANGA UMURIMO' campaign. This is done by encouraging nationals to develop innovative business plans of which the best are awarded resources to start businesses. The Rwanda Development Board (RDB) has several specific initiatives to support SMEs such as training programs, networking and moveable asset registration; it also works at improving the overall business environment in the country.

Despite the different initiatives to enable SMEs' to survive in their operations, most of them have failed. A report by PSFR (2008) citing a study by the Center for the Support of Small and Medium Enterprises in Rwanda CAPMER (2007) shows that a majority of the established SMEs had filed for bankruptcy and a majority of the start-ups failed in their first two years of operations and only less than 25 per cent expanded their businesses. This may be a result of unfavorable rules and regulations, lack of entrepreneurial skills and knowledge, lack of an entrepreneurial culture, lack of access to finance and lack of access to markets (MINICOM, 2010). These factors relate to the institutional environment. Therefore, our study ascertains the contribution of institutional environment and institutional support to SME growth in Rwanda. It also answers the following questions: What is the relationship between institutional environment and SMEs' growth in Rwanda? And how does institutional support affect SMEs' growth?

Our study focuses on the institutional environment in terms of its regulatory, cognitive and normative dimensions. Support focuses on access to finance, access to local and foreign markets and training in entrepreneurship knowledge and skills while SMEs' growth is studied based on enterprises' long-term survival which is explained by an increase in sales and an increase in employment over a period. Our study was confined to SMEs in Kigali city because Kigali is the capital where the researchers were able to find ventures in all categories such as small and medium enterprises and in different sectors of business activity.

## 2. Theoretical framework

### 2.1. Institutional Environment

According to institutional theory, a firm's external environment is governed by institutions which have a wide range of social structures including schemas, rules, norms and routines (Scott, 1995). Scott (1995) adds that these social structures are well established and have attained a high degree of reliance in providing authoritative guidelines for social behavior. Institutions lay down the rules to which economic players such as business firms must conform to earn legitimacy that boosts their chances of economic survival and relative performance. These rules may take the form of laws, regulations, norms, social conventions and other written or unwritten rules of conduct (Chen and Roberts, 2010; North, 1990; Scott, 1995). Legitimacy endows a firm with the right to exist and perform an activity in a certain way (Bruton et al., 2010; Chen and Roberts, 2010). Acs et al., (2008) point out that the relevance of an institutional environment for a business may be the most pronounced in times of economic distress. Support structures for new businesses are often available when the times are good, but at the time of an economic downturn it is hard to find private capital, grant funds, governmental support programs or inexpensive education that would assist start-ups. Hence, it is evident that the tax burden and regulatory requirements imposed on entrepreneurial businesses may feel particularly heavy when a business is already slowing down. Businesses around the world face increasing pressures to reconfigure their strategic orientations and capabilities in response to calls for sustainable development. For instance,

in Philippines the 1996 Marcopper mining disaster was a wakeup call for the country's business leaders to be more environmentally sustainable in their business conduct. This disaster led to the closure of the firm, hundreds of jobs were lost and there was irreversible damage to the natural environment (Bravante and Holden, 2009). Since the accident, regulatory and legislative reforms have been implemented to strengthen the Philippine government's capability to create an institutional environment that effectively mandates the business sector to adopt sustainable environmental practices. However, questions arise about the effectiveness of the various institutional environmental factors such as government policies, regulations and industry practices on the productivity of firms to adopt environmentally sustainability measures.

The concept of a country's institutional profile builds from Scott's (1995) notion that institutional environments consist of three inter-related pillars reflecting normative, cognitive and regulatory dimensions. The regulatory dimension refers to the formally codified, enacted and enforced structure of laws in a community, society or nation which promote certain types of behavior and restrict others (Kostova, 1997; North, 1990; Williamson, 1991). The normative dimension refers to social norms, values, beliefs and assumptions that are socially shared and direct behavior through a web of social obligations and expectations (Beliveau et al., 1994; Kostova, 1997; Scott, 1995).

The cognitive dimension refers to the socially mediated construction of a common framework of meaning or axiomatic beliefs that provide the templates and scripts for action (Scott, 1995). Firms achieve legitimacy from their institutional environment if their behavior and practices conform to specific regulatory, normative and cognitive standards.

## **2.2. Institutional Support**

Support policies for SMEs vary from country to country and from developed countries to less developed countries due to differences in business contexts, cultures and the levels of industrialization. Since East European countries are now members of the European Union (EU), there are various EU programs for SMEs that cover a range of their needs including vocational training and education, infrastructure projects and individual and information technology development (Konopielko and Bell, 1997). In addition, SMEs in these countries also receive direct support from local authorities and governments. Poland and Bulgaria are a case in point where SMEs are provided training and advisory services, management, market information, access to credit, export promotion and the introduction of high-tech production. In the initial stages of transition, these countries suffered some setbacks when SMEs operated in imperfect markets that lacked institutional support. The Central and Eastern Europe (CEE) experience suggests that business support infrastructure, financial support, a legal and institutional framework and cluster and network relationships play a vital role in business development.

SME development is also becoming increasingly important in many Asian industrialized countries such as Korea, Taiwan, Singapore and Australia. The Singaporean government has identified four key problem areas of SMEs: access to technology, manpower, finance and market (Lee and Tan, 2002). In 1998, the Korean government used a number of policies to

foster the growth of SMEs and their involvement in the global economy. This was done by ensuring access to finance, supporting human resource development programs and developing technology and scientific achievements so that businesses could develop extensive relationships with the global market (Gregory et al., 2002). Countries are now focusing increasingly on emphasizing public governance which outlines the broad institutional context within which individual policies are pursued. The need for broad public sector and regulatory reforms is an issue that has moved to the centre stage in both developed and developing countries (Organization for Economic Cooperation and Development (OECD), 1997; the World Bank, 2000).

### **2.2.1. Access to finance**

A number of studies highlight access to finance as one of the driving factors of an enabling economic environment. The World Bank and the International Finance Cooperation (IFC) rank economies according to their ease of doing business. In this framework businesses' ability to get credit is an important criterion (IFC, 2011). The Global Entrepreneurship Monitor (GEM) Entrepreneurship Framework Condition also highlights entrepreneurial finance which is defined as the availability of financial resources for SMEs in the form of debt and equity as one of the key factors for stimulating and supporting entrepreneurial activity (GEM, 2010).

Many entrepreneurs tend to depend on their own or their family's savings to start and operate a business; this means that the avenues of capitalization are limited. Thus, access to capital remains a challenge. For example, Kallon (1990) found that 65.6 per cent of the studied firms depended on personal savings as their sole source of capital, 10.9 per cent had access to family savings, 9.4 per cent used commercial banks and 7.8 per cent drew resources from partners, shareholders and other sources.

Access to finance is necessary for creating an economic environment that enables firms to grow and prosper. However, SMEs in developing countries face significant barriers to finance. Financial constraints are higher in developing countries in general, but SMEs are particularly constrained by gaps in financial systems such as high administrative costs, high collateral requirements and lack of experience within financial intermediaries. Increased access to finance for SMEs can improve economic conditions in developing countries by fostering innovation, macroeconomic resilience and growth in the gross domestic product (GDP) (Dalberg Global Development Advisor, 2010).

### **2.2.2 Training in entrepreneurial skills and knowledge**

Identifying the importance of institutional change for the growth of entrepreneurship, Smallbone (2004) suggests that businesses need to adhere to the following conditions: first, a legal infrastructure that is appropriate to market conditions; second, the creation of a legal framework that facilitates the development of entrepreneurship training and knowledge; and finally, the creation of commodity, capital and labor markets. Institutions that include regulatory and tax authorities, licensing and registration offices and private sector

institutions such as banks, accounting firms, other professional bodies and chambers of commerce must provide business support to SMEs. Such support includes creation of formal and informal support mechanisms and training programs; educational services are particularly important in emerging market economies because entrepreneurs lack basic business skills in terms of business plan preparation, planning, decision making, negotiations, pricing, market penetration, organization and management, management of the workforce and handling of cash flows (Swanson and Webster, 1992). Government sponsored incubators, most especially science, technology and research centers which will facilitate innovation in the long run should be put in place. In particular, entrepreneurs need assistance in conducting market research.

Gatewood et al., (1991) point out that business incubators can play a major role in providing a variety of services to start-up entrepreneurs. Most incubator facilities provide office space, common office facilities, faster and efficient means of communication and counseling and advisory services to their tenants at low costs. Incubators can be very helpful in places where infrastructure is not well developed or where modern physical facilities are costly. Some research evidence also shows that successful entrepreneurs can be developed through educational and short-term training programs and the government should play a big role in fostering entrepreneurship by instructing educational institutions, technical and vocational education (tailor-made) and business education to include entrepreneurship development studies in their curricula to impart knowledge and skills to will-be entrepreneurs. There should also be direct government subsidies for research and development, support for linkages between universities and the private sector and reflect and respond to the needs of specific localities or regions to be effective in encouraging innovations rather than simply importing successful policies from other areas.

### **2.2.3 Access to local and foreign markets**

According to OECD (2004) the rate at which countries grow is substantially determined by their ability to integrate with the global economy through trade and investments; their capacity to maintain sustainable government finances and sound money; and their ability to put in place institutional environments in which contracts can be enforced and property rights can be established.

Globalization and trade liberalization have ushered in new opportunities as well as challenges for SMEs. Presently, only a small part of the SME sector is able to identify and exploit these opportunities and deal with the challenges. A majority of the SMEs in developing and transition countries, however, has been less able or unable to exploit the benefits of globalization and, to add to the situation, SMEs are frequently under pressure in the local or domestic markets from cheaper imports and foreign competition due to lack of an enabling environment (OECD, 2004).

Therefore, governments should facilitate entrepreneurs to participate in local and international trade fairs and exhibition centers as a way of helping them to develop networks which they will use in marketing their products and services in both local and international markets and providing them necessary infrastructure such as roads, energy and modern



transport and communication facilities. In addition, OECD (2004) stresses that with easy access to suppliers and customers, development of industrial parks and trade centers, certain infrastructural elements have a substantial impact on the entrepreneurial environment.

### **2.3 Growth of small and medium enterprises**

The term 'SME' includes a wide range of definitions. Organizations and various countries have established definitive guidelines for categorizing SMEs which are often based on sales, the number of employees or the value of assets. In Rwanda, there is a recently agreed upon definition by all the intervening institutions which is based on criteria such as net investments, turnover and employment.

Insert Table 1 about here

SMEs' growth depends on many factors that vary from country to country. McIntyre (2002) argues that a synergistic relationship between SMEs and the larger enterprise sector is a critical factor. Havie (2002) observes that in China the development of township and village enterprises (TVEs) is an important aspect for the growth of SMEs. Several researchers (e.g. McIntyre, 2002; Julien, 1993; and You, 1995) recommends synergistic relationships and the process of urbanization based on both horizontal and vertical linkages such as industrial districts and clusters.

Various theories explain SMEs' growth from different perspectives. However, for a SME to develop its core competencies, adequate resources (both internal and external) are an important pre-requisite. Rindova and Fombrun (1999) argue that resources, capabilities and core competencies are essential for a firm's competitive advantage. Therefore, adequate resource support and policies to create capability are critical for SMEs' growth as they are small in size and need assistance. The resource based theory provides a framework to explain how a business can identify suitable measures to overcome growth obstacles, have better access to technology, manpower, financial and natural resources, infrastructure and access to the market. Lack of capital or denial of financial resources is a major barrier for SMEs and entrepreneurs, which usually have to mobilize their own capital or their own resources to establish or expand their businesses. Also, SMEs in developing countries have difficulties in accessing bank loans because of the high risks of failing loans, low profitability and lack of collateral required by banks Harvie and Lee (2005) For many SMEs in countries in the region access to finance and capital appear to be difficult. This is a consequence of weak banking institutions, lack of capital markets and inefficient legal frameworks regarding credit and collateral assessment. Financing of SMEs and access to finance play a crucial role in the growth and development of enterprises (the World Bank, 2011).

Porter (1998) proposes that industrial cluster policies can be a growth strategy for a firm; according to the author a cluster is a geographic concentration of interconnected companies and institutions in a particular field. This argument is strongly supported by Enright and Robert (2001), Dijk and Sverrisson (2003) and Nadvi (1995) since SMEs can receive external economic advantages (economies of scale and scope) if clustering and networking offer a potential growth path for them. The networking approach should not be seen in

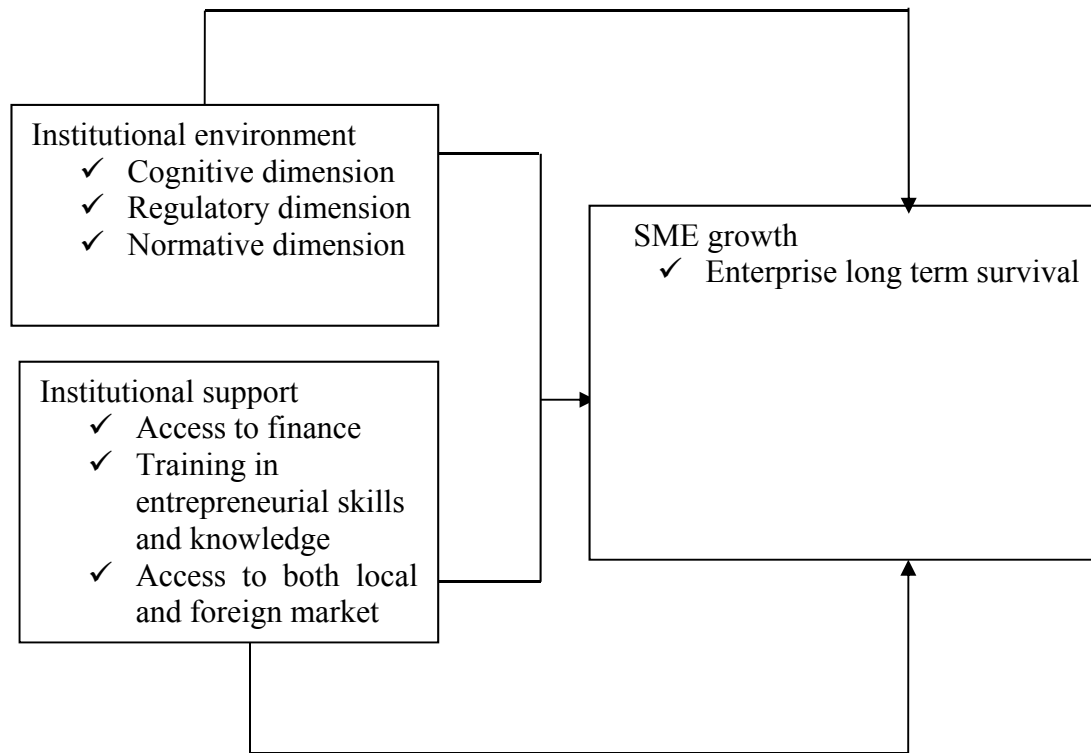
isolation but as being connected in business systems (Ritter et al., 2003). Lechner and Dowling (2000) define networks as the relationships that an individual has with other individuals or relations between organizations that can have various functions. Therefore, network relationships can be considered an important intangible resource for supporting SMEs which do not have sufficient resources. These relationships help SMEs develop links with suppliers, distributors and customers, or use social contacts including acquaintances, friends, family and kin.

North (1990) emphasizes that market economies convert resources - land, labor, energy and capital -- to the manufacture of services and goods. To make this conversion a success, institutions must also help and guide these transformations in predictable ways. Observing the economic histories of both newer and mature markets in Asia, North America and Western Europe Kartz (1995) maintains that private enterprises cannot emerge and prosper in an imperfect market without a conducive policy environment and institutional support system.

### **3. Conceptual frame work**

This research was guided by the conceptualization that SME growth if is to be improved; there is need for an effective enabling institutional environment and effective institutional support. Given that SMEs do not operate in a vacuum, investigating these relationships would be beneficial. Growth is conceptualized in terms of SME long term survival. SME survival is major concern in Rwanda as indicated by their high rates of failure. Institutional environment is conceptualized to comprise of cognitive, regulatory and normative factors. Previous studies have established that an enabling institutional environment boosts SME growth (Busenitz et al., (2000). Therefore, it was expected that if the institutional environment favoured SME operations, this would improve SME growth. Support is conceptualized to comprise the kinds of support that can be accessed from various institutional bodies in Rwanda. The support considered under this study is access to finance, entrepreneurial training and access to markets. Previous studies indicate that with such support, there is little doubt that SMEs will fail to live longer (Segnestam et al., 2002). It is therefore expected that when SMEs can readily access such support, they can improve their growth. See also Figure 1.

Figure 1: Conceptual framework



### 3. Research Methodology

Our study used cross-sectional designs together with the quantitative research design to establish the factors of an institutional environment that affect SMEs' growth. The population consisted of 3,352 registered SMEs' in Kigali (National Bureau of Statistics for Rwanda, 2011). A sample of 341 SMEs was chosen according to Research Advisors (2006). We used the convenience sampling method (Cosby, 2004) where we selected respondents with ease.

Primary data was collected from the respondents using self-administered questionnaires. The variables for primary data included the institutional environment and the variables were measured by a combination of different items measured on the Likert scale. Institutional environment was measured by the normative, cognitive and regulatory dimensions (Kostova, 1997; North, 1990; Williamson, 1991). Institutional support was measured by access to finance, training in entrepreneurial skills and knowledge and access to both local and foreign markets. This was according to Segnestam et al., (2002). Growth of SMEs was measured by enterprises' long term survival. This was according to North (1990); and Scott, (1995). The data collected was edited for completeness and consistency to ensure correctness of the information given by the respondents. Statistical package for social scientists (SPSS 17) was used for data entry and an analysis of the study variables. A descriptive analysis was

conducted to establish the institutional environment factors that affect the growth of the SMEs in Kigali.

#### **4. An Analysis of the Results**

Findings from our study indicate the following on the factors affecting the institutional environment of SMEs in Kigali: Sixteen of the 23 items that were found to be significant with high inter-correlation coefficients were retained. A KMO statistic of .85 which is above the acceptable .70 threshold was obtained after deleting seven items that had weak inter-item correlations (coefficients less than .3). Three factors constituting the institutional environment with Eigen values greater than 1 were extracted from the retained items. These factors in total explain 50.07 per cent of the total variance in the institutional environment. The factors were labeled regulatory, cognitive and normative dimensions. The regulatory dimension explained more of the institutional environment (29.21 per cent) followed by the cognitive dimension (12.16 per cent) and the normative dimension (8.7 per cent). This implies that the regulatory dimension explained institutional environment more than cognitive and normative dimensions in the institutional environment. The regulatory factors related to the government's efforts at enhancing SMEs' growth. The results indicate that the regulatory dimension is very critical.

Insert Table 2 about here

#### **4.1 Correlation Analysis**

Table 2 shows the correlation analysis of the respondents' understanding of the relationship between the institutional environment, institutional support and SMEs' growth. The correlation analysis was done to establish the relationships between the independent variables and the dependent variable.

Insert Table 3 about here

#### **4.2 The relationship between the institutional environment and growth of SMEs**

The first question was on the relationship between the institutional environment and SMEs' growth in Rwanda. Our results show that the institutional environment had a significant and positive relationship with SME growth ( $r = .159$ ,  $p < 0.05$ ). This implies that any positive change in the institutional environment was associated with positive changes in SMEs' sustainability.

#### **4.3 The relationship between institutional support and growth of SMEs in Rwanda**

The second question was whether institutional support had a significant relationship with SMEs' growth in Rwanda. Our results show that institutional support was significant and inversely related to SME growth ( $r = -0.205$ ,  $p < 0.05$ ). This result is surprising and contrary

to what was expected. However, a further analysis of the descriptive statistics of institutional support indicated that most of the respondents were unaware of the support provided to SMEs. The results in Table 4 indicate that individual items and the composite item had a mean of 3 on a five-point Likert scale. This explains the inverse relationship between institutional support and SMEs' growth.

Insert Table 4 about here

#### **4.4 The relationship between institutional environment, institutional support and SMEs' growth: Regression Analysis**

This analysis was done to explain the predictive powers of the institutional environment and institutional support on the dependent variable of SME growth. According to Table 4, the results from the findings indicate that the institutional environment and institutional support accounted for a 5.8 per cent (R-squared .058) variance in SME growth in Kigali. The unstandardized coefficients B shows that the values of the numbers for institutional environment were in the linear regression equation while the value for institutional support showed an inverse equation. The relationship between the institutional environment, institutional support and SME growth was 0.196 and -0.231 respectively. This means that for every change increase in the institutional environment, SME growth improved by 0.196 and for every increase in institutional support, SME growth improved by -0.231. The SMEs' growth t-value of 16.648 indicates that the model was significant at the 1 per cent level. The p-value of  $P \leq .000$  indicates that the variables of institutional environment and institutional support were significant in SMEs' growth in Kigali.

Insert Table 5 about here

### **5. Discussions of the findings**

#### **5.1 The relationship between institutional environment and growth of SMEs**

Our findings show that institutional environment was positively associated with SME growth. This concurs with numerous studies that highlight, for instance, access to finance as one of the driving factors of an enabling economic environment. The World Bank and the International Finance Cooperation (IFC) rank economies according to their ease-of-doing business. In this framework, a business' ability to get credit is an important criterion.

In line with these findings, authors such as and Lundvall (1992), Nelson (1993) and Sorge (1991) discuss that a country's institutional environment comprises of relatively stable rules, social norms and cognitive structures that guide and constrain domestic economic activity. It is well understood that a country's institutional environment guides firms' strategies and helps determine the nature and amount of business activity that takes place within the country's borders (Lundvall, 1992; Nelson, 1993; Sorge, 1991). The institutional environment sets the framework for market transactions by defining the alternative courses of action open to firms (North, 1990) dictating potential risks and payoffs for different

activities and specifying the conditions under which firms hold legitimacy (Meyer and Rowan, 1977).

## **5.2 The relationship between institutional support and growth of SMEs in Rwanda**

Our findings show that institutional support had an inverse relationship with SME growth with ( $r = -.205$ ). This is explained by the fact that the respondents were unaware of the existing institutional support for SME growth in Kigali. This means that there is a need for generating awareness about different avenues of support provided by both central and local governments to SMEs. In disagreement with these findings, authors such as Nguyen et al., (2009) state that support policies for SMEs vary from country to country and from developed countries to less developed countries due to differences in business contexts, cultures and the levels of industrialization. In addition, according to Batra and Mahmood (2003), SMEs in developing countries in East Asia, for instance, receive support from local governments in the form of microfinance, interventions to increase private sector training, technology development and market information. China, Malaysia, Indonesia and Thailand have benefited from these policy reforms, network relationships, cluster linkages to markets and the new support infrastructure (Harvie, (2002); Tambunan, 2005).

Based on the experiences of CEE countries, Dallago and McIntyre (2003) state that SMEs are not themselves sufficient for growth without the proper development of institutions and support structures. Further, North (1990) found that institutions were critical determinants of economic behavior and they can impose direct and indirect effects on the prevalence and types of entrepreneurship in a society. Therefore, promoting sustainable enterprises calls for the strengthening of institutions and governance systems which nurture enterprises by building formal structures, coordination amongst them, availing necessary resources and equipping people working in these institutions with skills and knowledge which will enable them to offer good services to SMEs when called upon. Promoting sustainable enterprises is also about ensuring that human, financial and natural resources are combined equitably and efficiently to achieve innovation, enhanced productivity and resource conservation (CAPMER, 2004).

## **5.3 The relationship between institutional environment, support and SMEs' growth**

Our findings indicate that the institutional environment and institutional support accounted for 5.8 per cent (R-squared .058) variance in SME growth in Kigali. The p-value of  $P \leq .000$  indicates that the variables of institutional environment and institutional support were significant for SME growth in Kigali. In support of our findings, previous studies indicate that there are reasons to believe that an institutional environment which favors new business activities and entrepreneurship can have a direct and positive impact on the performance of new firms. However, we also believe that these effects of the institutional environment are channeled to a firm through key individuals' interpretations of the state of these institutions (Busenitz, et al., 2000). Also, since institutional profiles are domain specific (Kostova, 1997), we expect that younger firms experience the effects of institutional environment for

entrepreneurship more strongly than the more established firms. Bowen and DeClercq (2008) stressed that under institutional arrangements entrepreneurial individuals are more likely to engage in the creation of new wealth through productive entrepreneurships.

## **6. Summary and Conclusions**

Our study looked at the contribution of institutional environment and support to SMEs' growth in Rwanda. The factors that constitute the institutional environment can be summarized as: The regulatory dimension can be interpreted as accessibility to finance, access to market and training in entrepreneurship skills and knowledge as well as an interpretation of the environment. Our findings also show that there is a need to improve the institutional environment for SMEs in Rwanda especially in access to finance and fiscal regulations because our study found that the institution environment was positively associated with SMEs' growth in Rwanda. This is in line with Bartholomew (1997); Lundvall (1992); Nelson (1993); and Sorge (1991). Our study also concludes that a country's institutional environment guides firms' strategies and helps determine the nature and amount of business activity that takes place within the country's borders. This also concurs with North (1990) who stresses that the institutional environment sets the framework for market transactions by defining the alternative courses of action open to firms. These findings lead us to the conclusion that institutional support has an inverse relationship with SME growth. This is explained by the fact that the respondents were unaware of the existing institutional support for their growth. More specifically, a majority of the respondents were not sure about the kind of support being provided to them like financial and marketing institutional support being provided to facilitate their operations and protection from outside competition.

Contrary to this finding, using the experiences of CEE countries Dallago and McIntyre (2003) state that SMEs were not themselves sufficient for growth without a proper development of institutions and support structures. Kartz (1995) observes from economic histories of both newer and mature markets in Asia, North America and Western Europe that private enterprises cannot emerge and prosper in an imperfect market without a conducive policy environment and institutional support systems. Institutions must be designed so that they are able to work in the environment in which they function. In addition, our results also indicate that institutional environment and support accounted for a 5.8 per cent (R-squared .058) variance in SMEs' growth in Kigali. However, the institutional environment had a linear relationship with SMEs' growth while institutional support showed an inverse relationship. Therefore, the relationship between institutional environment, institutional support and SME growth was 0.196 and -.231 respectively which means that for every increase in the institutional environment, SME growth improved by 0.196 and for every increase in institutional support, SME growth improved by -.231. The p-value of  $P \leq .000$  indicates that the variables of institutional environment and institutional support are significant for SMEs' growth in Kigali.

## 7. Recommendations

Based on our findings we make the following recommendations for SMEs in Kigali to improve their growth:

- There is need to establish whether the following aspects of institutional support are provided to SMEs in Kigali easily: Access to loans at low interest rates, mentorship to entrepreneurs, access to markets for their products within and outside the country, prevention of outside competition for SMEs' products and ensuring that SMEs' products easily reach the final consumer at less costs.
- SMEs in Kigali should concentrate more on improving the institutional environment than institutional support because it positively improves their growth.
- There is also need for SMEs in Kigali to understand why institutional support inversely influences SMEs' growth as this will help them structure appropriate strategies to support and to improve SMEs' growth positively.

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Table 1. Definitions of MSMEs used in Rwanda

Size of the Enterprises	Net capital investments in Million FRW	Annual Turnover in Million FRW	Employment Number
Micro-Enterprises	Less than 0.5	Less than 0.3	Less than 3
Small Enterprises	0.5 to 15	0.3 to 12	3 to 30
Medium Enterprises	15 to 75	12 to 50	30 to 100
Large Enterprises	More than 75	More than 50	More than 100

Source: MINICOM (2010).

Table 2: Factor analysis of the institutional environment in Rwanda

Items	1	2	3
<b>Regulatory</b>			
The government has made it easy for SMEs to access financial services for their business operations	0.751		
Local and central governments have special support available for individuals who want to start a new business	0.715		
The government provides free entrepreneurial training and sensitization to SME owners or managers	0.692		
SMEs are not over taxed in the initial stages of their operations	0.677		
The government has made it possible for SMEs to trade across borders	0.665		
The government controls prices of products/ services	0.557		
<b>Cognitive:</b>			
I /we understand the rules and regulations imposed on us and how they affect our business		0.766	
I / we understand the procedures for securing a loan		0.744	
I / we know where to find the information about the market for our products or services		0.656	
I / we know different taxes and payment procedures		0.641	
I / we know and understand different financial products such as short-term loan, medium-term loan, long-term loan, over draft and salary advances offered to us by financial institutions		0.633	
I / we know and understand SMEs' development policy and other government policies		0.515	
I / we know how to legally protect a new business		0.495	
<b>Normative:</b>			
Financial institutions in Rwanda provide loans to SMEs easily			0.735
There is protection of new businesses by the government from outside competition			0.638
The institutions of higher learning in the country produce the best workforce which is able to start a new business or work for other organizations			0.633
Eigen values	4.67	1.94	1.39
Percentage of variance	29.21		8.70
		12.16	
Cumulative percentage of variance	29.21	41.37	50.07

Table 3: Correlation analysis

Variables	1	2	3
Institutional Environment (1)	1	0.268**	0.159**
Institutional Support (2)	0.268**	1	-0.205**
SMEs' Growth (3)	0.159**	-0.205**	1

Note: \*\* Correlation is significant at the 0.01 level (2-tailed)

Table 4: Descriptive statistics of institutional support

Items	Minimum	Maximum	Mean	Std. Dev
It is easy to access loans from financial institutions	1.00	5.00	3.0382	1.48640
The interest rates on loans in the country are favorable for SMEs	1.00	5.00	3.3248	1.29987
The procedures to access loans from banks are simple for SMEs	1.00	5.00	3.1911	1.43277
There are entrepreneurship training centers in the country to help train SME owners already in business and also those who wish to start a new business	1.00	5.00	2.8185	1.01844
The government has put up incubation centers for SMEs' upcoming ideas to be tested	1.00	5.00	2.8949	1.10116
It is easy for SMEs to access markets for their products outside the country	1.00	5.00	3.4586	1.27893
There is less outside competition for SME products	1.00	5.00	3.1592	1.32081
SMEs' products easily reach the final consumer at less costs	1.00	5.00	3.0605	1.18813
Composite Variable Mean			3.11	

Table 5: Regression analysis of Institutional environment, institutional support and SMEs' growth

Coefficients <sup>a</sup>							R sq	adjusted R sq	F	sig
		Unstandardized Coefficients		Standardized Coefficients	t	Sig.				
		B	Std. Error	Beta						
	(Constant)	2.316	0.139		16.648	.000	0.058	0.048	2.834	0.60
	Inst. Environment	0.196	0.085	0.194	2.309	0.022				
	Inst. support	-0.231	0.055	-0.351	-4.179	0.000				
a. Dependent Variable: SME growth										