

DIVESTING AND INVESTING AS STRATEGIC DECISIONS
IN SMALL BUSINESS ENTREPRENEURSHIP

by

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B. Com. (Hons) (Natal)

Submitted as the dissertation component in partial fulfilment of the requirements for the
degree of

MASTER OF BUSINESS ADMINISTRATION

in the

School of Business,
University of Natal
Pietermaritzburg.

2003

ABSTRACT

With many studies on small business entrepreneurship indicating high failure rates, South Africa is no exception. However, the small business is a critical sector of the South African economy, as it contributes significantly to the country's job creation, innovation, empowerment, economic growth and development. The government has also identified the SME sector as the pinnacle for its important national development strategies. As failure seems to be higher at the entry level, it becomes important that all business opportunities are properly investigated.

This study first looks into the divestiture of a poor performing business, K.H. Foods Services CC trading as Steers. The aim is to assess entrepreneurally whether the business indeed needs to be divested. As the funds from the divestiture were to be re-invested, an investigation of a new business opportunity is undertaken. A Chicken Licken franchise is chosen as a better mode of entry into the Richmond market. A cost-benefit analysis was done for both cases. The results of the analysis reinforced the decision to divest and invest. The analysis also gave an indication that the new business was a better investment option when compared to other investment alternatives such as a financial institution investment and an insurance lump-sum investment. The new business venture showed better returns on capital invested, and its payback period was shorter than other investment options. These analyses were supported by a consumer survey. The purpose of the survey was to test whether a need existed in Richmond for a Chicken Licken franchise, and most importantly, to establish whether this franchise will enjoy the support of Richmond consumers.

To achieve this aim, a questionnaire was used to collect a relevant data from a representative sample of all adult resident population of Richmond who visit public places. The quantitative data was captured and analysed using the 'Statistical Package for Social Science (SPSS). Additionally, a multiple regression model was formulated and tested to examine the demand for Chicken Licken in the Richmond region.

The results suggested an overwhelming support for a Chicken Licken franchise business in Richmond. Based on this survey and other strategic analyses, the decision was taken to open a Chicken Licken outlet in Richmond.

DECLARATION

This dissertation represents original work by the author and has not otherwise been submitted in any form for any degree or diploma to any university. Where use has been made of the work of others, it is duly acknowledged in the text.

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K.H. Ngcobo

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ACKNOWLEDGEMENTS

For this work I am greatly indebted to my supervisor, Dr D. Mahadea for his assistance and wise guidance.

I would also like to express my gratitude to the following people:

My family, for their constant support, especially to my daughter,
Nonduduzo, who is my inspiration

Aira Kotcha, for his assistance with the statistical analysis of the data,

Richard Bell, for editing this work,

And

My parents for their constant love and support, especially to my mother who held me by hand and led me to school on that first day. This dissertation is dedicated to them.

CHAPTER 1

INTRODUCTION

South Africa is faced with a number of social and economic challenges. The small business entrepreneurship is still an extremely important weapon to be unleashed. This sector is known to be a strong pillar for most world economies when it comes to job creation and economic growth. Consequently, entrepreneurship can be considered as key to job creation and economic growth. The small business sector may well be the foundation for South Africa's breeding ground for entrepreneurship and an important vehicle for black empowerment. Although the development of small businesses is showing encouraging results, numerous outstanding issues are indicative of the challenges that still lie ahead. These issues also underpin the objectives of the 1995 White Paper on SMMEs development.

In many countries small businesses are known to have a high failure rate; South Africa is no different. As a result of the legacy of our past, some of our problems may indeed be unique. Whilst faced with these problems, viz. unemployment, inequalities and low economic growth, South Africa lacks entrepreneurs. According to the Chambers Digest (Morris, Chamber Digest, 21 November, 1998:6) the entrepreneurial sector of society accounts for about 80 to 95% of all new jobs created in industrial nations. It has also been shown that there is a direct positive relationship between the level of entrepreneurial activity in a society and the growth of the GDP, yet South Africa has the lowest rate of entrepreneurship in terms of necessity, start-up and new firms (GEM, 2002:59). This is not different than fighting a war without weapons!

The literature review, in *Chapter 1* and *Chapter 2*, looks into some of these issues, but the main purpose of this study is to investigate the implications of the two strategic decisions, investment and divestment. With regard to the investment, the opportunity cost of resources needs to be considered. In other words, a better investment option needs to be chosen amongst other possible options of the same risk. In the case of a divestiture, the challenge is what to do and when, in order not to lose the funds invested in a failed investment. Both these strategic issues have a direct link to the failure or success of the small business.

This study looks into these two strategic issues in a real business environment. A Steers franchise business, K.H. Foods Services CC, established by the present author in 1999, is divested because of poor performance. The funds are to be re-invested in a new business opportunity. The cost-benefit analysis was undertaken for both cases. As part of the viability study for the new investment, which is a Chicken Licken franchise business in Richmond, a consumer survey was undertaken and strengthened by multivariate analyses. The aim of the survey was to test the attitudinal response of the Richmond consumers towards a Chicken Licken franchise. In order to achieve this aim, the following aspects have been investigated from the Richmond market:

- Richmond consumers' awareness of the Chicken Licken brand.
- Establishing whether people in Richmond like to eat chicken.
- Establishing whether people in Richmond like Chicken Licken products.
- Determining whether a need exists in Richmond for a Chicken Licken franchise.
- Establishing whether a Chicken Licken franchise will be supported in Richmond.
- Determining the income levels of Richmond consumers.

The consumer survey is considered key because an opportunity is not yet a business until support from consumers is ensured. A Chicken Licken franchise was not selected because the writer already owned one in Nongoma, in northern KwaZulu-Natal, but because of a market gap.

Franchising is one option of entering entrepreneurship. Based on mutual relationship between franchisor and franchisee, the franchise offers attractive benefits for both parties. While it offers a tried and tested formula for the franchisee, the challenge is to choose the franchise that the entrepreneur can afford and that consumers enjoy; and, most importantly, one that promises a better return on the capital invested, hence the need for proper entrepreneurial assessment.

CHAPTER 2

THE SIGNIFICANCE OF SMALL BUSINESS ENTREPRENEURSHIP

2.0. INTRODUCTION

Considerable attention has been devoted to the development of small business in South Africa. Studies have shown that this is an important sector for economic development and sustained economic growth. Seen also as an important breeding ground for entrepreneurship, in South Africa it is earmarked for carrying out national strategies for job creation and participation by the previously marginalized communities.

Chapter 2 looks at the role the small business sector is playing in world economies and the challenges that are still facing South Africa.

2.1. DEFINITION OF A SMALL BUSINESS

In the South African context, the term “small business” describes a diverse range of activities, differing in aspects such as size, sector, ownership structure and formality. The definition and classification of a small business in South Africa is provided in the National Small Business Act No. 102 of 1996. The Act describes a small business as a separate and distinct entity, which is not part of a group of companies. If the business has subsidiaries and branches, these need to be included when measuring its size. A small business should be managed by its owner or owners and can therefore be a natural person, a sole proprietor or partnership, or a legal person, such as a close corporation, co-operative or a company (Ntsika, 1999:7). The Act classifies small businesses into four categories: micro, which includes survivalist enterprises, very small, small and medium. In its classification, the Act has adopted the international practice of using quantitative criteria relating to employment, turnover and assets and the enterprise must comply with all three (Ntsika, 1997:8).

It is important that a small business is properly defined. This is firstly, in order that policy-makers and service-providers know exactly which target groups they need to assist so that they can develop better policies and services for the right sector (Ntsika, 1997:8).

Secondly, it is also important for small business owners to know in which target group they fall, so that they can determine for which support-measures they qualify (Ntsika, 1997:8).

Lastly, defining small business is necessary for research purposes. Researchers need a common understanding of what a small business is so that they can measure and compare its performance in different regions and sectors and with other countries (Ntsika, 1997:8).

Small business entrepreneurship contributes significantly to economic growth, social development and employment provision in South Africa and most other countries. It is often described as the natural home of entrepreneurship and its value is recognised in a great variety of economies, irrespective of their level of development (Vosloo, 1994: 159). Small business plays a crucial role in experimentation and innovation that leads to technological change and employment growth. They are the essential mechanism by which many can enter the economic and social mainstream (Acs, 1999: 11-17). This is indeed an important factor in South Africa because, in the apartheid period, most blacks were excluded from engaging in formal business ventures, except in designated areas. Contrary to the static view that small firms have an inefficient scale of operations, which results in lower levels of productivity and lower wages for workers, Acs (1999) agrees that small firms contribute positively to the economy. According to him, small businesses play two very important and unique roles, namely efficiency and dynamics. With regard to efficiency, they can provide certain goods and services better and more efficiently than large firms. His argument is that, even in the presence of pervasive scale economies, the small firms are still able to survive and thrive. As far as dynamics are concerned, he argues that small firms are needed to provide the entrepreneurship and variety required for macroeconomic growth and stability. They serve as agents of change and provide an essential source of new products and experimentation that otherwise would remain untapped in the economy. In this way they offset any static efficiency losses (Acs, 1999: 100).

Vosloo (1994) is very much in agreement with the view that small firms create a share of net new jobs that exceeds their static share of employment and the capital invested per job created is also significantly smaller than in the case of larger firms. This holds whether one defines small firms as firms with fewer than 100 or fewer than 500 employees (Vosloo, 1994: 167). Maree also concurs with these views. According to him small businesses are better able to adapt to changes and utilise new opportunities, even during an economic recession, thus contributing to economic stability (Maree, 1996:5).

The small firm sector provides an important field of opportunity and advancement for individuals, who, because of absence of qualifications and other characteristics, would have little chance of comparable opportunities in sectors more dependent on formal qualification. The small business is often able to serve those areas and communities where markets are too small to support production on the scale undertaken by large enterprises, e.g. the rural areas. These make them even more important in the South African situation, that is characterised by large rural areas and the very large unskilled labour force that result from mainly the legacy of our past. African countries therefore could ignore this sector at their own peril and even the success of Nepad depends on how much Africa invests in this sector, argues the City Press reporter (City Press Business, 18 May, 2003:1).

2.2. DRAWBACKS OF SMALL FIRM ENTREPRENEURSHIP

Although owning a small business provides entrepreneurs with a number of powerful incentives and rewards, these perhaps far supersede the drawbacks. Nevertheless, it is still important that drawbacks are mentioned, so that anyone planning to enter the world of entrepreneurship should be aware that there might be many demands and mishaps along the way and that these are not to dissuade them from engaging in small business firms. A few drawbacks associated with small business entrepreneurship are listed below:

- **Uncertainty of income.** Opening and running a small business provides no guarantees that an entrepreneur will earn enough money to survive. The owner often has trouble meeting financial obligations, especially in the early days of the business

(Scarborough and Zimmerer, 1996:10). This may even have an impact on the whole family's welfare.

- **Risk of losing the entire family savings.** Not all start-ups have the same chance to succeed. Some studies have shown that 51% of new businesses shut down within four years. Running a business therefore is much more risky than working for someone else. If the business fails, you stand to lose far more than just your job. If the business is a sole trader, not only will your hard work have been no avail, but you might also suffer even more severe financial losses if the business owes money, as you are personally liable to your creditors. These factors need to be pointed out, so that actual and potential entrepreneurs are aware of them and prepare themselves for the consequences thereof (Scarborough and Zimmerer, 1996:10).
- **Accepting lower quality of life until the business gets established.** The long hours and hard work needed to launch a company can take their toll. Entrepreneurs often find that their roles as husbands and wives or fathers and mothers take a back seat to their roles as company founders and it is more so in the early days of the life of the business (Scarborough and Zimmerer, 1996:12).
- **High levels of stress.** The risks taken are coupled with uncertainty. The business keeps on demanding more hard work and more funds whilst it is still generating little or no profits (Scarborough and Zimmerer, 1996:13). These may be very stressful to the entrepreneur, when one considers that small businesses are typically short of cash. They cannot raise capital in the same way that large companies can and this can impede their strategic options (Burns, 2001: 9).
- **Increased responsibility.** Although it is exciting to be one's own boss, the realization that the decisions that one makes may cause a success or a failure may have a devastating effect on some people, especially when there is no one else to consult (Scarborough and Zimmerer, 1996:13).

In spite of these drawbacks, surveys have shown that owners of small businesses believe they work harder, earn more money and are happier than if they worked for large companies. Apart from economic benefits, therefore, owning a small business has some personal benefits to the owner. Some of these are:

- **Control over your own destiny.** Being an owner of a business provides entrepreneurs the independence and the opportunity to achieve what is important to them. Entrepreneurs like to “call the shots” in their lives and they use their businesses to bring this desire to life (Scarborough and Zimmerer, 1996:8). This is typical of their character, namely, *locus of control*. These people believe that the outcome of an event is determined by their own actions, therefore luck, chance, fate or the control of other people are less important than one’s own. Internal locus of control is thus that force that compels many people to start their own businesses to gain independence, autonomy and freedom (Hatten, 1997: 43).
- **Getting an opportunity to make a difference.** Entrepreneurs are starting businesses because they see an opportunity to make a difference in a cause that is important to them (Scarborough and Zimmerer, 1996:8). This is typical of their trait, namely that they are *attuned to opportunity*. Good entrepreneurs are constantly searching for new opportunities. This means that they are never satisfied with the way things are at any moment in time and they use this sense of dissatisfaction to make sure that they never become complacent (Wickham, 1998: 40).
- **An opportunity to reach your full potential.** There are people who find their work boring, unchallenging and unexciting. To most entrepreneurs, there is little difference between work and play. Their businesses therefore become the instruments for self-expression and self-actualisation, as owning your own business will challenge all your skills, abilities and determination (Scarborough and Zimmerer, 1996:9).
- **Opportunity to reap unlimited profits.** The profit that the business earns is one of the motivating factors in the entrepreneur’s decision to launch a business. Thus, owning a business is one of the best ways to accumulate wealth (Scarborough and Zimmerer, 1996: 9). This can also be passed on to children or other family members, who can continue earning profits. In South Africa, this is a common practice among the Indian community. According to Burns, entrepreneurs exploit change for profit and they often see opportunities where others see problems (Burns, 2001: 30).
- **Opportunity to contribute to society and to be recognised for your efforts.** Small business owners are often amongst the most respected and most trusted members of

their communities. Business deals are mostly based on trust and mutual respect and these are the hallmarks of many established small companies. These business owners thus enjoy the trust and the recognition they receive from their customers, whom they have served so faithfully over the years (Scarborough and Zimmerer, 1996: 9). The other contributions are creation of economic opportunities for one's community in the way of jobs. Some small businesses, especially in the rural areas, serve as community centres, e.g. pension pay-points, health services such as mobile clinics and the community uses the shop for their postal services, like using the shop's post box or private bag and collecting their mail from the shop. In the far, remote, rural areas, small businesses bring goods to the convenience of their communities and in this way save them transport costs.

It is true that, today, small business is regarded as the embodiment of economic freedom and individual liberty. The small business can be seen as a practical way of solving problems of unemployment and of enhancing economic growth (Vosloo, 1994: 168).

2.3. GROWTH OF SMALL BUSINESSES

The afore-mentioned factors, coupled with the trends and incidents that are discussed in the paragraph below, have forced business leaders, policy-makers and academics in most countries, and indeed in South Africa, to change their mind-set and focus on the creative energies of entrepreneurs and the benefits of small business as a vehicle for entrepreneurship. Some of these trends are discussed below:

The shift in most economies away from manufacturing towards the service sector, where small firms often flourish because of their ability to deliver personalised, flexible and tailor-made service at local level (Burns, 2001: 17).

Availability of international opportunities as the process of globalisation is taking place and most international trading barriers are falling away, opening vast opportunities in world markets. Often small companies form joint ventures with foreign partners, in this way overcoming other international barriers, such as customs, language and perhaps local content requirements (Scarborough and Zimmerer, 1996: 15).

Strategic downsizing and re-engineering of large corporations have had their influence in small business growth. Whilst in the past competitive conditions favoured large companies with their hierarchies and layers of management; today with the pace of change constantly accelerating, nimble and agile small companies have the strategic advantage. Nimble competitors can dart into and out of market niches and can exploit opportunities quickly. The balance has therefore tipped in favour of small, entrepreneurial companies. This has ushered in the age where “small is beautiful” (Scarborough and Zimmerer, 1996: 3).

Another trend influencing this swing is a rapid move away from an industrial economy to a knowledge-based one. What matters now is not so much the factors of production but knowledge and information. A knowledge-based economy favours small business because the cost of managing and transmitting knowledge and information is very low and computers and information technology are driving these costs even lower still (Scarborough & Zimmerer, 1996: 3).

The failure of the centrally and socially planned economies, and the impressive prosperity of the market oriented Western countries, have clearly shown that the creative energies of entrepreneurship bring about business formations and expansions. These, in turn, contribute to job creation and material prosperity in a competitive environment. The lesson for South Africa, in its quest to address its high unemployment problem is the stimulation of entrepreneurship at the SMME level (Vosloo, 1994: 159).

2.3.1. Other Factors Contributing to the Growth of New Firms

- The new firm resurgence is primarily an impact of deepening economic recession. Increasing levels of unemployment push individuals into business formation and withdrawals of large business organisations from less profitable activities leave market niches in which more flexible small firms may still operate profitably. Firm formations also become more attractive in a period of recession, because increased business closures lead to the availability of cheap, second-hand equipment (Hannu and Hannu, 1994: 38). People who lose their jobs due to depressed market conditions will anticipate their returns to be highest as entrepreneurs, compared to two options

open to them, remaining unemployed or seeking another job with another employer (Hannu and Hannu, 1994: 39). Mahadea to suggests that being unemployed for a long time aggravates the situation so much so that the “unemployed” become “unemployable” (Mahadea, 1997: 97). Under such circumstances, therefore, the only remaining alternative for the unemployed is to venture into self-employment.

Apart from depressed market conditions, carrier dissatisfaction could have the “push” effect to entrepreneurship (Lawrence and Hamilton, 1996: 79). In their studies, these writers found that, in New Zealand, unemployment, or the prospect of it, was the primary motivating factor for about 50% of all new firm founders surveyed (Lawrence & Hamilton, 1996: 80). According to Mitchell (2003:10) in South Africa, 37.8% of African entrepreneurs, 30.4% of Indian entrepreneurs and 30.8% of European entrepreneurs started their businesses because of the difficulty to find a job. This has a “push” effect.

- The income growth theory, on the other hand, views the growth of new, small firms as an impact of substantial income growth and growth of demand for more sophisticated goods. These developments, in turn, create niche markets for new small businesses. The consequence of this dynamism therefore has a “pull” effect, contrary to the former view (Hannu and Hannu, 1994:38).

The following statistics further highlight the important role and contribution made by small firms. In most European countries small businesses constitute about 95% of all business enterprises and provide about 60% of all job, and, in most Asian countries, small enterprises form 98% of all companies and contribute about 55% of the GDP and account for about 80% of all job. (Utch *et al.*, 1999:1). In the United States of America 98% of all businesses are small firms (Steinhoff and Burgess, 1993:4). In the year 2000, for instance in the USA, small businesses have created three-quarters of the country’s new jobs and have made up 97% of all identified exporters (Laing, Mail & Guardian, 13 June, 2003: 22).

In view of the above, one is inclined to agree with Mare that small businesses are the “absorbers of economic setbacks and recessions, refuges for entrants to the labour market and important contributors to the generation of wealth” (Mare, 1996: 5).

2.4. SMALL BUSINESS IN SOUTH AFRICA

Although South Africa's small business development is relatively new, when compared with other emerging economies, its importance has been established. According to the Department of Trade and Industry's (1995) White Paper on SMMEs, this sector is geared to drive the very important national economic and social strategies, e.g. GEAR and the RDP.

The development and promotion of small business in South Africa has therefore been one of the government's major policy objectives since 1994. It has been identified as the important vehicle for job creation, equitable economic growth and redressing the imbalances in terms of participation of the previously disadvantaged. This, then, led to the introduction of the 1995 Government White Paper, for which the primary objective was to develop the small business sector, mainly through creating the enabling environment in which small businesses could grow and flourish. In addition to this basic objective, several more-detailed policy objectives are identified in this document and these are discussed below.

Firstly, the policy aims to facilitate the greater equalisation of income, wealth and economic opportunities, which is inseparable from a strengthening of a labour absorptive process in the micro enterprise and survivalist segments, the redressing of discrimination with respect to blacks and small enterprises in the rural areas (White Paper, 1995: 15).

The second objective is to create long-term jobs, which demands policy interventions designed to upgrade human resource skills and to strengthen the use of appropriate modern technologies (White paper, 1995: 15).

The third goal is to stimulate economic growth through addressing the obstacles and constraints that prevent small businesses from contributing to overall growth (White Paper, 1995:16).

The fourth objective outlined in the Government White Paper is that of strengthening the cohesion between SMMEs to overcome their isolation or loneliness by promoting the networking of SMMEs to build collective efficiency, to address development obstacles, and to take up opportunities (White Paper, 1995: 16).

The fifth and last national strategy is to level the playing field between bigger and small business with regard to market opportunities, regulation and competitive structures which in the past had favoured larger enterprises and enterprises in urban areas. It therefore aims at addressing these imbalances and enhancing co-operation and interaction between these segments of the economy (White Paper, 1995:16).

One outcome of this White Paper was the establishment of the small business support agencies of the Government, Ntsika Enterprise Promotion Agency and Khula, with their network of service providers. They are both key institutions of the National Small Business Strategy. Ntsika facilitates non-financial support and business development services to SMMEs through a broad range of intermediaries known as Local Business Service Centres (LBSCs) and Tender Advice Centres (TACs). Their services also include SMME training, counselling and advice, market development and business linkages and programme design research and information. Khula also provides loans through the Retail Financial Intermediaries (RFIs). It provides loans covered by its credit guarantees to RFIs for on-lending to SMMEs and then helps the RFIs to build in-house capacity in the area of small business credit administration (Ntsika, 1998: 26).

Since their establishment, these institutions have had a number of successes in terms of the sector growth and economic contribution, although there are still many challenges ahead.

According to Ntsika, small business in South Africa has been targeted because they are able to:

- ❑ Create jobs at low capital cost.
- ❑ Contribute significantly to the economy in terms of output of goods and services.
- ❑ Improve forward and backward linkages between economically, socially and geographically diverse sectors.
- ❑ Create opportunities for developing and adapting appropriate technology.

- ❑ Provide an excellent breeding ground for entrepreneurial and managerial talent.
- ❑ Develop a pool of skilled and semi-skilled workers.
- ❑ Act as ancillaries to large-scale enterprises.
- ❑ Adapt to market fluctuations.
- ❑ Fill market niches that are not profitable for large enterprises.
- ❑ Lend themselves to development policies favouring decentralisation and rural development.
- ❑ Help alleviate the negative consequences of restructuring the economy.
- ❑ Use local, often recycled, resources.
- ❑ Provide solutions for the newly urbanised, unemployed, retrenched and rural and urban entrepreneur.
- ❑ Have a high propensity to save and re-invest, even at very low-income levels.

In South Africa, therefore, the small business sector has been firmly established. It is targeted firstly as a means of stimulating growth generally, secondly as a vehicle for distribution of wealth and attaining more equitable growth and thirdly as a means to address rising unemployment, as large corporations' demand for labour seem not to be increasing in proportion to their growth, as the result of a number of reasons, including mechanisation due to global competition.

In addition to the Government's efforts to develop small businesses, donors, both national and international, and the private sector, have made significant contributions to accelerate the growth of small firms (Ntsika, 2001: 19).

2.5. GDP CONTRIBUTION OF THE SME SECTOR AND THE CHALLENGES FACING SOUTH AFRICA

Since the government has embarked on this long process of highlighting the importance of small business and creating the right environment in which small business could grow and flourish, much has been achieved. Although challenges facing small businesses still exist, their contribution to the economy has been enhanced.

Statistics in South Africa indicate that the small business sector is already playing an important role in the economy. The number of new registrations is showing encouraging trends of enterprise growth over the period 1990-1998. Proprietary Limited companies registrations increased from 6 369 in 1990 to 23 6551 in 1998 while close corporations increased from 28 008 in 1990 to 73 114 in 1998 (Ntsika 1998: 61), indicating substantial growth.

According to Ntsika (2000:35), small business in South Africa represents 97,5% of the total number of business firms. These firms contributed 34,8 of the GDP, employed 55% of the country's labour force and contributed approximately 42%, in 2000. Although some of these figures do not yet match international levels, some improvements, however, are already showing, especially the contribution to GDP that has improved from a figure of 32.7% in 1995 and employment creation that has improved from a figure of 44% in 1995. (Ntsika, 2001: 40). Although there are significant strides taken regarding the development of small business entrepreneurship in South Africa, as these statistics indicate, many challenges lie ahead. The following are some of these challenges:

2.5.1. Unemployment

There appears to be no end to high unemployment levels in South Africa. The fact that the unemployment rate has remained stubbornly in double digits for the last few years is indicative of this. In both the public and private sectors, employment seems to continue shrinking. Unemployment in South Africa has increased from 6,7% in 1960 to 29,3 in 1995 (Loots, 1998: 319). It is currently sitting at 41% (SA Survey 2002-2003: 215). Small businesses are typically labour-intensive and they source much of their input locally and are thus an important vehicle for addressing this problem (Ntsika, 1998:16).

Various reasons have been put forward for the persistent unemployment problem in South Africa and, according to Mahadea, "some unemployment is bound to exist in a transforming economy", in which category this country falls (Mahadea, 1997: 101). Loots cites the inability of the South African economy to create sufficient employment opportunities for its growing labour force (Loots, 1998: 319). Although the Government has put together the GEAR Macro Economic Strategy, its targets of

economic growth and job creation are yet to be realised. The absorption capacity of the labour force has surely declined. It has dropped from 79.6% in the nineteen-seventies to almost zero during the period 1990-1995 (Loots, 1998: 325). It becomes evident, therefore, that the creation of jobs in South Africa should not only be anchored on economic growth, but some other creative alternatives need to be found (Loots, 1998: 335).

Other contributory factors to job losses or unemployment in South Africa include the following:

- ❑ Corporate downsizing, reduction in workforce, forced early retirement and government privatisation are some of the common terms in South Africa that describe job losses. Downsizing seems to be an international trend, Companies are “breaking themselves down into smaller units”, as the new belief is that “in the management of creativity, size is your enemy” (Burns, 2001: 60).
- ❑ The average annual increase of 2.9% in labour productivity, that indicates that employers encourage existing workers to work harder (Loots, 1998: 334).
- ❑ The presence of foreign job seekers and illegal immigrants (Loots, 1998: 334).
- ❑ The generally low skill levels in the labour force, whilst current trends indicate that employment has expanded only in sectors requiring skilled labour (Loots, 1998: 335).
- ❑ The substantial increases in real wages of unskilled and low-skilled workers (Loots, 1998: 335).
- ❑ The impact of external factors such as globalisation of markets, reduction of trade restrictions, availability of cheaper imported goods and the rapid change of technology (Loots, 1998: 335).
- ❑ Productivity of the labour force in South Africa has risen to 52% since 1992, the reason, however, is not that south African workers have adopted a dynamic work

ethic, but because of “the jobless prosperity boom being enjoyed by the country’s manufacturing industry”, as a result of mechanisation. In order to match global prices, volume and quality, this industry has resorted to mechanisation as their strategic option. One example is that Toyota is investing R3.5bn to increase its production capacity, as part of their global strategy. This investment, according to their chairman, is “not likely to add significantly to job opportunities” (Thomas, Financial Mail, Nov. 8, 2002: 35).

- Globalisation, burdensome labour legislation in South Africa, low saving and investment, high levels of crime, HIV/Aids and corruption mitigate against labour intensive investment (Mahadea, 2003:).

In view of the above, it becomes evident that economic growth does not, at present, contribute to the required job opportunities, nor can it be expected to do so in the near future. As unemployment is still a thorn in South Africa’s flesh, it becomes clear that small businesses are not yet fully compensating for job losses from large corporations, nor absorbing enough new job seekers to help combat unemployment. The challenge facing this country, therefore, is to speed up the process of developing and nurturing small business, so that it fully fulfils its objectives as set out in the White paper and that South Africa reaches the levels of other developing communities.

2.5.2. Participation in the sector by Africans

One of the advantages of small businesses is that they are an effective mechanism by which many can enter the mainstream economy. Indeed, one of the key underlying principles of the national small business strategy was the enhancement of participation of blacks and the previously marginalized, in order to attain equalisation of income, wealth and economic opportunities. According to Ntsika (2001: 53), the current emerging trends, are that there are still disparities in the nature of business engagements among different population groups, as depicted in (*Appendix 2* on page 109). Participation by blacks appears to be concentrated in the lower end of the SMME spectrum, with their presence decreasing as the size of the enterprise increases. Ntsika (1998:55) points out

that there are disparities in self-employment. Among the white population group 18% are self-employed, compared with 6.3% for Africans.

According to the study conducted by UNISA's Bureau of Marketing Research, the black labour force is responsible for approximately 4% in terms of manpower quantities in the formal sector, whilst needing 90% of all job opportunities over the period 1991-2011 (BMR, 1994: 20). The white group is responsible for 85% of the supply of entrepreneurship and will have a share of only 3% in the total labour force increment. This study reveals that if the skill distribution of the whites' labour force does not improve (even though it is already known that it has reached the world's best levels), it will only be able to provide four entrepreneurs for each 1000 increase in black labour force members (BMR, 1994:20). The unemployment for blacks is the highest amongst other population groups, at 43% against a rate of 4.6% for whites (Ntsika, 1998: 34). This indicates that, in order for the black population group to compensate for the economic imbalances arising from the proliferation of their labour force members, they will have to expand their entrepreneurial cadre in the formal sector eleven times, over a period of twenty years, disregarding the backlog of workers not in employment (BMR, 1994: 20).

It therefore becomes clear that the development of small business needs to be expedited. This sector has a potential of redressing racial and geographic inequalities, as well as promoting entrepreneurial activity and in this way harnessing South Africa's inputs to enhanced national production and employment creation.

2.5.3. Entrepreneurship

Entrepreneurship is now widely regarded as an integral part of a successful formula for achieving economic growth. It plays a key role in combining the factors of production, as these are not self-mobilising. It is entrepreneurs who must mobilise them and actually get the economic production machine running. Entrepreneurship is therefore part of the ignition mechanism of business enterprise (Vosloo, 1994: 153-154).

The most efficient economic system, according to economic theory, is one in which unimpeded markets determine the price at which goods are bought and sold. Under such

an environment, efficiency would imply that resources are distributed in an optimal way, meaning that the satisfaction that people can gain from them is maximised (Wickham, 1998: 10). This means that the overall health of the economy hinges largely on the dynamism of entrepreneurial activity.

Sharing
 Entrepreneurs are among the few people who are willing to share their hard-earned family savings with other families when they open their businesses. Even when they have made profits in their businesses, these are further reinvested in the business, increasing the size of the cake, so that more families can share. Wickham seems to be agreeing to this thought. According to him, entrepreneurs are not selfish people and they cannot afford to be. They recognise the value that other people bring to their ventures and the importance of motivating those people in order that they make the best effort they can on its behalf (Wickham, 1998: 40). It is true that entrepreneurship is not a 'zero sum game,' but it often creates win-win scenarios (Wickham, 1998: 26).

win-win scenarios
 No matter how well we plan the future, there is always the possibility that some chance event will result in outcomes we neither expected nor wanted. It is why, perhaps, Wickam further suggests that the primary function of entrepreneurs is to accept risk on behalf of other people, and that there is a *market* for risk. Entrepreneurs are therefore providing a service by taking the risk off people's hands, as risk is something that people generally want to avoid (Wickam, 1998: 12). An entrepreneur is a wonderful person if he or she achieves success; if he or she fails then he or she is not! This brings us to the point which is very important and that is that the risk taken should be calculated and minimised to most optimal levels so, that the perception that entrepreneurs gamble with risk can be changed around and they are rather perceived as people who enjoy evaluating and exploiting the unexplored and unknown. There are people who find delight in challenges that are the true characteristics of real successful entrepreneurs. Entrepreneurs are also associated with a characteristic known as a high need for achievement, n-Ach. Individuals with a low need for achievement seem to be content with their present status, while, individuals with a high need for achievement like to compete with some standard of excellence and prefer to be personally responsible for their assigned tasks (Longenecker, Moore and Petty, 1997: 9). "A need to achieve is associated with successful entrepreneurs and research suggests that nations with high

levels of n-Achievement are associated with above average growth” (Mahadea, 1994: 43).

There are the kind of people that we need more and more of in South Africa, with its social and economic challenges that it is face it in terms of economic growth, poverty alleviation and job creation. This view is also expressed by Mahadea, “economic growth rates among and within countries at different time periods can be explained by the contributions of labour, capital and a residual factor.” “ Entrepreneurship is a vital part of this residual factor” (Mahadea, 1994: 42).

There is a huge shortage of these entrepreneurial people in South Africa. Van Aardt, Van Aardt and Bezuidenhout, (2000: 1) also express this view, that South Africa has few people with entrepreneurial qualities. This leads to a situation in which even the economy performs poorly, because it is a very small number of people that succeeds as entrepreneurs. This was the view of the Deputy Minister of Trade and Industries, Phumzile Mlambo-Ngcuka: “Only 2% of South Africans are entrepreneurs, the world average is 10%.” The thrust of the government’s strategy on small business promotion is to unearth the missing 8%” (Enterprise, August, 1997: 2). Studies conducted by the Global Entrepreneurship Monitor confirm this shortage. These studies, conducted in 2002, rated South Africa below the average rate of entrepreneurial activity amongst developing nations. According to the GEM study, it is of great concern that South Africa has the lowest Total Entrepreneurial Activity (TEA) rate of all developing countries. The developing countries have a combined mean of 14.15, against the 6.54 TEA index for South Africa (Global Entrepreneurship Monitor, 2002: 13-14). This study reveals that South Africa has an entrepreneurial pool made up of 58% opportunity and 42% necessity entrepreneurs. Opportunity entrepreneurs are those that are in business because they are pursuing a business opportunity, while the necessity entrepreneurs are those that are involved in entrepreneurial effort because they have no choice of other work. Other countries rankings are 74% for opportunity entrepreneurs and 26% for necessity entrepreneurs, that indeed the development of entrepreneurs in South Africa remains one of our challenging issues.

2.5.4. Progressing beyond the start-up phase

There can be no doubt that small businesses face a wide range of constraints and problems that can result in their failure and may end in total closure. The view by many writers is that pinpointing them exactly would be a mammoth task as they are complex. Inadequate turnover, for example, may be offered as the explanation for the failure of a business, whilst the underlying reasons for this might have resulted from economic conditions that were beyond the control of the manager, or from poor pricing or promotion strategies that resulted from weak management (Longenecker, Moore and Petty, 1997: 36). They are complex indeed! While the present study does not attempt to delve too much into small business failure factors, some of them are mentioned in the following section.

The creation of employment by small firms is one of the important contributions they make to the economy. Employment in small businesses expands as a result of new enterprises starting up and through expansion of existing enterprises. The birth of new firms is also vital to offset closure of other enterprises (Mead and Liedholm, 1998: 61). According to Storey, though, young small businesses have a higher propensity to failure than the old ones and the most powerful influence on their survival is whether or not they grow within a short period after starting up (Storey, 2000: 109). “Time is of the essence, a prolonged infancy is a sign of pathology” (Adizes, 1988: 33). In studies conducted in four African countries, (Swaziland, Botswana, Zimbabwe and Kenya), 50% of the closures took place within three years of start-up (Mead and Liedholm, 1998:65). According to Scarborough and Zimmerer (1996:10), in America 51% shut down within four years. These facts are worth noting, especially for supportive agencies, so as to enable effective intervention; for instance, focusing on particular stages in the enterprise’s life-cycle, where the intervention can do the most good (Mead and Liedholm, 1998: 71).

The start-up survival situation in South Africa is not yet in line with other countries, according to the GEM report. While South Africa has a high number of start-ups, it is but a few that reach the stage where they are able to pay salaries and wages for longer than three months. South Africa ranked 15th out of 37 countries in the level of start-up activity, indicating that our start-ups have a low success rate. The challenge, therefore, is

a need for more encouragement towards the start-up phase, to ensure that businesses develop to the point where they can start and continue to pay salaries and wages (GEM, 2002:15).

According to Adizes (1988), organizations have life-cycles that they have to go through. Organisations are faced with struggles and difficulties accompanying each stage and the challenges are to win these transitional problems, in order to move to the next phase of development. While all stages have their unique problems it seems that the start-up phase, or the “infant organisation” phase, is a make or break stage (Adizes, 1988: 32). The organization is young, there are no previous track records or organisational memory to rely on, and yet the founder is constantly being tested with problems for which he is not prepared. With few or no policies, performance is inconsistent and management is by crisis. This makes the organization vulnerable and its problems can easily become a fatal crisis (Adizes, 1988: 33). Young organisations therefore need a total founder’s commitment, as they require much hard work and many sleepless nights, in spite of the fact that there are no tangible results.

Secondly, if the organisation is to grow, management must also grow and if this does not happen a change in leadership is called for. Most small businesses are run by their founders and they need to have a variety of skills suitable for varying stages in the growth phases in order to succeed. Infant mortality will occur if the owner/manager loses control (Adizes, 1988: 32). The challenge is to move through the start-up stage quickly, otherwise pride of ownership evaporates and commitment dies (Hatcher, 2002, MBA lecture notes). The other important aspect is that of a strategic challenge for management at different life cycle stages of the young organisation, because various strategies are suitable for specific stages of the product or industry evolution. Johnson and Scholes (1997: 322) suggest that the “life cycle analysis” gives an indication if a strategy is likely to be appropriate, given the stage of the product life-cycle and/the industry life-cycle. The analyses also take into account the competitive position of the business in that particular industry. These analyses will be explored further when the Chicken Licken project is examined in Chapter 6.

Another critical issue at the infancy stage is under-capitalization. There is a tendency to underestimate the need for cash and working capital. The more the company sells, the

higher the probability of developing under-capitalization. “A company with 35% or more average sales growth per year will generally experience difficulties in financing this growth from its own internal sources” (Adizes, 1988: 24). The challenge is that record-keeping should not only focus on accrual accounting, but also on cash flow, with specific attention to monitoring the turnover of accounts receivables and inventory, so as to avoid unnecessary increases in working capital that can drain the young organisation’s liquidity. The rule is to avoid the tendency of taking short term loans for investments that yield results only in the long run, avoid giving exorbitant discounts too soon and avoid selling stock to venture capitalists who are not sympathetic to the business (Adizes, 1988: 24). Sometimes these financial problems are not of the entrepreneurs making. Small businesses are normally at a disadvantage in competition for capital required for growth and expansion. It is the demands of large organisations that are favoured by most financial institutions. The rationale is that small-scale lending is less profitable and highly risky to these institutions, as the costs of appraisal, supervision and recovery do not vary according to the amount lent (Cook, 2001: 17). A study by Dun and Bradstreet revealed that 47.3% of failure among small businesses is as a result of finance (Longenecker, Moore, and Petty, 1997:36). Finance has also been cited by Ntsika as one of the factors that inhibit growth in this sector, especially amongst blacks (Ntsika, 2000: 64). Khula was established in South Africa precisely to address this issue.

Small or young organisations are characterised by simple structures. All powers are centred on the owner or CEO. The weakness of this structure is that the chief executive or owner can get so enmeshed in operations problems that he loses sight of strategic issues, or he can become so enthusiastic about strategic opportunities that the more routine operations wither for lack of attention and eventually pull down the whole organisation. Whilst this structure has some merits, this is one of its critical disadvantages: everything hinges on the “health and whims of one individual” (Mintzberg, 1979: 313).

The next weakness of the simple structure, which is as critical as the first one, is that, when structural changes must come, the only person with the power to make them is the owner/chief executive himself or herself and he or she often overlooks or resists change, which is critical as the business moves to different stages of its growth (Mintzberg, 1979: 312). Scarborough and Zimmerer (2000: 29) call this an “inability to make the

entrepreneurial transition.” “Success or failure is what happens to a business at a particular time and how the owner reacts to it which makes for success or failure” (Torrence, 1986:58).

It needs to be mentioned that, although small business failure has negative consequences, which include loss of entrepreneurs' and creditors' capital, social and economic effects, it has some positive effects as well. They provide a mechanism that can lead to allocative improvement within the economy, with resources being shifted from low to higher returns. Failure information provides guidance to those contemplating starting a business, it gives signals that entry into industry *a* is risky or at least more risky than entry into industry *b*, and it also provides experience for those involved (Storey, 2000: 78).

2.5.4.1. Small Business Success

According to Wickham (1998: 91) success of the venture can best be understood in terms of four interacting factors, namely:

- ❑ **The performance of the venture.** This is indicated by a variety of quantitative measures. These relate to its financial performance and the presence it creates for itself in the market place.
- ❑ **The people who have expectations from the venture.** An organisation is made up of individual people and success, if it is to be meaningful, must be experienced by those individuals as well. Organisational success is a means to an end of personal success. The organisation creates the resources that interested individuals can use to improve their lives. The success of the venture therefore must be considered in terms of the expectations of these individuals who are called its stakeholders (inside stakeholders and outside stakeholders).
- ❑ **The nature of those expectations.** According to Pearce and Robinson (200:48), each of these groups has justifiable reasons for expecting that the business satisfy their claims in a responsible manner. If it is to be meaningful, the success must not only be experienced by the organisation, but also by those individuals/institutions that

make up its stakeholder groups, the entrepreneur(s), employees, suppliers, customers and perhaps the government. Success provides the means by which to fulfil the different goals of these groups.

- ❑ **Actual outcomes relative to expectations.** Success, therefore, is achieved if the organisation uses its performance to meet, or to exceed, the financial, social and personal growth expectations of those people who have an interest in it. It must survive and prosper in the marketplace, it must reward its stakeholders for their contributions and it must be financially secure (Wickham, 1998: 92-93).

In view of the above, it is therefore that a great need exists in South Africa to help nurture small businesses, to improve the start-up and survival rates. Currently, the survival rate is 12%, according to City Press Business. Other developing countries such as Singapore have a survival rate of 97% in a three-year cycle, indicating that our situation needs to be improved significantly (City Press Business, 18 May, 2003:1).

2.5.4.2.Constraints in small business growth

According to the survey on township entrepreneurs, finance is identified as still the most widespread inhibitor of success, with 65% of township informal entrepreneurs and 39% informal entrepreneurs citing this as their main problem (GEM, 2000:32). Ntsika has established that it is still difficult for black entrepreneurs to obtain venture capital funding. The three problems listed below are the most common facing black entrepreneurs.

- ❑ **Perceived quality of the management team.** The quality and experience of management ranks first in the assessments for venture funding applications. In most cases, entrepreneurs from historically disadvantaged backgrounds are negatively perceived, especially if it is a new venture that has not yet proved itself on the market (Ntsika Annual Review, 2000: 64).
- ❑ **The bias towards large investment and well-established enterprises.** New ventures that have not yet established themselves on the market are perceived to have a

relatively high risk and there is also the transaction cost constraint for small businesses (Ntsika Annual Review, 2000: 64).

- ❑ Own capital requirement is the third obstacle for the previously disadvantaged. The capital base is still thin amongst these emerging entrepreneurs and yet financial institutions are unwilling to support an idea if the entrepreneur has not backed it up with own capital (Ntsika, 2000: 64).

The causes of business failure are numerous. This study aims to highlight those factors that the writer feels are related to the small firm start-up phase, which seems to be one of the main problems facing the growth of the small firm in South Africa. Starting a new business is the main focus of this study. The following causes of failure are therefore worth mentioning, as they apply pertain to the start-up stage:

- ❑ **Wrong site identification.** Location needs to be selected after proper study, investigation and planning. Factors such as the impact of rentals on profits, potential sales, current and possible future competition need to be covered. Barrow points out that overlooking this could be catastrophic and that this has been the demise of many entrepreneurs (Barrow and Brown, 1997: 45).
- ❑ **Lack of marketing research.** It is important to establish whether or not there is a gap for the product or service to be offered on the market. It needs to be established what the attitude and perception of that particular market is about the product or service. One does not have to open a business to prove that there are no customers for the goods or services offered, because this would have catastrophic financial implications (Barrow and Brown, 1997: 45).
- ❑ **Lack of strategic management.** As businesses are now dealing mainly with mature product or service markets, the importance of entry strategies becomes vitally important. Entry strategies require either innovation or entering the market at a competitive strategic advantage, which, according to Porter (1985), evolves around generic strategies and positioning either for cost leadership, differentiation or focussing. Too many small business entrepreneurs neglect the process of strategic management, because they think it is something that benefits only large companies.

Building a strategic plan forces an entrepreneur to assess realistically the proposed business's potential and it further enables the entrepreneur to make the "entrepreneurial transition", as the cycle of the market evolves (Scarborough and Zimmerer, 1996: 27). While this is important at all stages of the industry development, one feels it is even more important at the start-up phase, as most studies have shown that most fatalities in small businesses occur at this initial stage and its at this stage that management is continually challenged to make effective strategic adjustments, in order to move up to the next phase.

Conclusion

In concluding this chapter, it must be reiterated that the importance of small business, especially with regard to job creation, economic growth and empowerment, has been established in South Africa. Some progress is evident in policy measures and strategies to nurture and support the development of small business entrepreneurship in South Africa. However, more needs to be done in order to enable this sector to play its full role in helping alleviate the ills of South Africa society. The challenge goes out to the entrepreneurs themselves to carefully consider all the relevant factors when they enter the world of entrepreneurship, to ensure the survival and prosperity of their businesses. The following chapter covers these issues, including entry routes and entry strategies in order to ensure firms' competitive advantage.

CHAPTER 3

ALTERNATIVE ENTRY ROUTES AND STRATEGIES

3. 0. INTRODUITION

Every entrepreneurial venture is different and has its own history. Its successes are the result of its having faced and addressed specific issues along the way. Perhaps the first crucial challenge for the entrepreneur is to make certain that the idea truly represents the existence of a real business opportunity. The venture must be able to produce and sell a product, or a service needed and desired by consumers. This means that the venture must be able to draw enough customers, who are willing to buy at a price high enough and at a volume high enough to make a profit (Siropolis, 1986: 107). Starting a business is thus filled with enthusiasm, frustration, anxiety and hard work. There is a high failure rate, especially at the start-up phase and we have seen in the previous chapter that some of the common causes are lack of capital and failure of management to meet various strategic challenges at different stages in the growth of the business.

When starting a new business, therefore, some of the important issues that need to be addressed involve deciding what type of business is to be chosen, what entry route is to be used, which strategies are likely to give the fledgling business a sustainable competitive advantage and what legal form the new venture should take. "Whatever type of business opportunity is involved, it must be genuine. This means that the new business must have some type of advantage that will provide a competitive edge. The prospective entrepreneur must visualize some new product or service or location or angle that will not only "get the foot at the door but keep it there!" (Bekker and Staude, 1996: 25). It therefore becomes critically important that these issues are carefully considered, as they entail the survival, growth and prosperity of the prospective undertaking, since failure, as shown in the previous chapter, has severe consequences. Chapter 3 will be dealing with some of these issues.

3.1.0. DECIDING ON THE TYPE OF BUSINESS

Choosing a type of business involves making a commitment for the eventual establishment or acquisition of that type of business (Bekker and Staude, 1996: 27). It is therefore of the utmost importance that the decision made on the type of business is meticulously thought through by the prospective entrepreneur, as the success of the venture will require his or her dedicated commitment, and much more. It will also need the commitment of his or her financial resources and sometimes even other investors' or lenders' funds. As each sector will have its particular characteristics, and thus its particular demands for these resources, the decision needs to be carefully considered. Care needs to be taken that no important factor is overlooked, as the main aim is to minimise risks and position the new venture such that it effectively exploits the opportunity identified and to give it a firm foundation for developing a sustainable competitive advantage.

3.1.1. Choice of sector

The sector could be agriculture, mining, manufacturing, construction, a trading business or a service business. Each sector has its unique characteristics that need to be considered when anticipating entry. According to Storey, failure rates of small businesses do vary from one sector to another, although the differences are relatively modest (Storey, 1994: 94). However, for survival, any information is crucial, no matter how minute. It is important, therefore, that the prospective entrepreneur gathers all the facts regarding the sector of choice and carefully analyses these. Some of the important issues that need to be investigated relative to the sector of choice include the factors that are discussed below.

3.1.1.1. Personal qualities

It is important to ensure that the sector or the kind of business chosen matches the technical knowledge and the experience of the prospective entrepreneur. The nature of the opportunity identified may dictate that one or more of the qualities the entrepreneur

possesses will play a vital role in the eventual success of that venture (Van Aardt and Van Aardt, 2000: 52). In order for the opportunity to be translated into reality, with a chance of success, the entrepreneur must possess appropriate skills and competences, as he or she is the most important factor for the ultimate success of that venture. The vital step for the prospective entrepreneur is to define his or her businesses with precision, in order to ensure that own skills and industry challenges really match (Siropolis, 1986: 94 - 95).

3.1.1.2. Attractiveness

The sector chosen must be attractive enough to yield consistently good returns on investment. Whether an industry is attractive depends on the presence of favourable competitive conditions and a market environment conducive to long-term profitability (Thompson and Strickland, 1998: 217). What is important for the entrepreneur, amongst other things, is an understanding of the dynamics of market growth, market maturity, competition in the industry and the general environment. The timing of entry is critical, according to Barrel, as it can be catastrophic for the new venture to enter the market at an entirely wrong time of the life cycle of the market or product (Barrel, 1990: 25).

3.1.1.3. The Cost of Entry

The cost of entry to that particular industry or target market needs to be given serious attention. The entry cost must not be so high that it erodes the potential for good profitability. The paradox, however, is that the more attractive the industry, the more expensive it can be to get into. Thus buying a company already in the business would often entail high acquisition costs, because of the industry's strong appeal (Thompson and Strickland, 1998: 217). It would therefore be important for the entrepreneur to carefully weigh his or her options and select the most cost-effective alternative. Different businesses would have an impact on the size of the venture capital required. Some processes in mining and manufacturing, for instance, might call for sophisticated and costly plant and equipment. These are all-important factors that the entrepreneur might ignore, at his or her own peril.

3.1.1.4.Location

Sector selection is important because particular locations will be suitable for particular industries. The question is which location factors to consider relative to the sector, as the underlying aim is to choose an appropriate location that serves the needs of the business's target market most efficiently. In manufacturing, for instance, locating close to markets that the manufacturing firm plans to serve is extremely critical, when cost of transportation of finished goods is high relative to their value. A firm that requires raw materials that are difficult or expensive to transport may need a location near the source of those raw materials (Scarborough and Zimmerer, 1996: 495-496). One of the location criteria for retail is to choose a location where there is a cluster of businesses as, these are known to pull more volumes of customers than would a stand-alone business. Location is therefore important for operating costs and for strategic reasons.

3.2.0. ENTRY ROUTES

The skill of the entrepreneur lies in recognizing the gap in the market and when and how it should be exploited. The next critical decision to be taken by the entrepreneur is choosing the right entry mode. There are four different types of entry routes the small business entrepreneur may choose from and each has its own advantages and disadvantages. The entrepreneur needs to weigh up which route will best suit the opportunity identified. These entry routes are *start-up*, *buyout*, *taking over a family business* or *buying a franchise*.

3.2.1. Start-up

Starting a new business from the ground is the most difficult option, because nothing is in place. It is difficult as even the history of the business is yet to be made. The information available to the entrepreneur at this stage might only be the outcomes of the viability studies and estimated figures. There are therefore more risks and uncertainties involved. In a takeover, for instance, there are past records that may tell the entrepreneur what the turnover was during a particular year and whether the trend of revenues was

going up, standing still or going down (Siropolis, 1986: 108). With the new venture, however, nothing happens until it is made to happen. To many people the process of taking an idea through all the steps and challenges, until it becomes a viable business, is the essence of entrepreneurship (Hatten, 1997: 178). This is the road travelled by many successful entrepreneurs, for whom founding and moulding a business poses a much greater challenge than taking over an existing business. Some of them have become big names in the world, e.g. Bill Gates. Pure entrepreneurs seek a business that is truly their own creation. They crave the creative satisfaction that comes from planting an idea and then making it grow into a strong and sturdy business (Siropolis, 1986: 106). Although starting a new business from scratch might seem difficult to some, to others it is still a challenge worth taking.

3.2.1.1. Reasons for start-ups

Although entrepreneurs must put a lot of effort into obtaining information about their markets, according to Siropolis there are practical reasons why they may prefer to begin from scratch. Some of these reasons are listed below (Siropolis, 1986: 107).

- ❑ Start-up may be chosen in order to avoid the ill effects of the previous owner's mistakes.
- ❑ Entrepreneurs may decide to take this route in order to be able to choose their own banker, equipment, inventories, location, suppliers and workers, without being bound by commitments and policies made by the previous owner of the business.
- ❑ This route may be chosen in order to be able to create the entrepreneur's loyal customers.

3.2.1.2. Kinds of start-up ideas

There are a few options in deciding on the start-up idea and these are discussed below.

□ Exploiting Partial Momentum from an Existing Product or Service

There are three approaches to this idea, namely meeting a supply shortage, transferring a product or service to new locations or capitalizing on unused resources.

The first approach is to provide customers with an existing product or service that is not available in that particular market. The chances of success are greatly improved when starting up in this way, as the founder knows and understands the markets and products or services involved (Barrow, 1993:90). This is the approach that is referred to by Hodgetts and Kuratko as a *new-old approach*. This is when an entrepreneur piggybacks on someone else's idea, by either improving a product or service or offering it in an area where it is currently not available (Hodgetts and Kuratko, 1995: 92). As the entrepreneur will have to recruit capital and talent to introduce the new firm in a new setting, there is a risk that the entrepreneur may not have sufficient resources to get the new firm started or to sustain it, once competition develops (Bygrave, 1994: 60).

An opportunity for an existing product could exist when there is a sudden supply shortage in the economy that is unrecognised by established sources of supply. This may give entrepreneurs an opportunity to fill the gap. The risk here is that when the shortage goes away, and the established suppliers get better equipped to fulfil the demand, competition may resume and the small business owner may not be in a strong position to face it (Bygrave 1994: 61). Barrel warns that it should not just be assumed that, because a product has succeeded in one market sector or geographical area, it will automatically enjoy the same level of acceptance elsewhere (Barrel, 1990: 52). Exploiting a new market with an old product or service would require as much thought and planning as an entirely innovative exercise and the entrepreneurs need to guard against complacency or drawing the wrong conclusions from previous experience based on data compiled from different markets. This underlines the importance of doing own fresh research and assessment, even if it is an old product that has proved itself elsewhere. Lastly, the availability of unused resources, for example from harvesting industries, could be utilised by the young

entrepreneur to manufacture the same product or products and introduce them in niche markets that were unexploited by incumbents (Bygrave, 1994: 62).

❑ **Developing new products or service**

There are start-up ideas that are concerned with providing customers with a new product or service. Hodgetts and Kuratko (1995: 92) refer to this as a *new-new approach*, which is an approach indicating that the development of entrepreneurs in South Africa still remains a challenging issue that entails new products or services entering the market. This is a much more risky approach than dealing with what has already been proved successful on the market, as is the case with other options. This approach requires a great deal of information-gathering in terms of market research and new product planning. “What it takes to start a company around a new product or service includes, most importantly, the discovery of an intersection between the market for that product or service and a way to create one” (Bygrave, 1994: 56). This is an approach that will need a lot of much research and market surveys and that may also put a great demand on resources. There are some risks involved in developing a new product or service (Bygrave, 1994: 57). These are listed below.

- The design task may be practically impossible for the entrepreneur to accomplish on time.
- The new venture may err in the design.
- A stronger company with stronger resources may follow and wipe out the young start-up.

❑ **Enhancing the old product**

This is a start-up idea that centres around providing customers with an old product or service that is upgraded and enhanced. The improvement could be in the way of lower costs or superior service (Longenecker, Moore and Petty, 2003: 122). According to Barrel (1990:55), this is achieved by either enhancing quality or making a product or service more valuable or of greater utility to the customer. The other approach that falls under this category is what Bygrave (1994:59) calls the “parallel competition”. This is the introduction of new products that are not really new, but are sufficiently different in

design to allow the new entrepreneur competitive entry. This often results in fierce competition and the entrepreneur might be tested on his or her financial capabilities. The start-up, therefore, may not have sufficient funds to carry it to profitability and to face possible competition from established competitors.

3.3.1.3. Advantages and disadvantages of start-ups

Starting a business from scratch has various advantages and disadvantages. When selecting an entry option, prospective entrepreneurs need to acquaint themselves with these, in order to make informed decisions (Brenner, Ewan and Custer, 1990: 7).

□ Advantages

- This means having a choice in deciding where your product or service will be marketed, where your business will be located and which individuals you will hire.
- New credit connections and relationships are developed.
- No pre-existing equipment or inventory, the entrepreneur chooses only the equipment and inventory; that are needed according to particular requirements of the new business.
- Customer contacts and relationships are new, which permit the entrepreneur to establish his or her own reputation and unique image.
- Suppliers can be evaluated and chosen according to the business needs, as they are not predetermined.
- The business created can reflect the founder's personality.
- No previous bad records are taken over.
- It gives an entrepreneur the opportunity to provide his or her unique product or service to the market.

❑ Disadvantages

- Obtaining credit and finance for the new business may prove to be difficult because of the lack of previous track records.
- Planning for and organizing a new business may take more time and energy than acquiring an existing business.
- The entrepreneur may have to supplement his or her income whilst the new business is still not showing sufficient profits.
- It may take time to establish a solid customer base that has confidence in the product or service.

It is important, therefore, that this option is considered after careful weighing-up of these advantages and disadvantages.

3.2.2. Acquiring a going concern

The option of buying a business that is already in operation appears attractive, for a number of reasons. It offers a way of avoiding the beginner's hazards as the existing business is already functioning and may even be a proven success. Many of the serious start up problems should already either have been avoided or corrected (Hatten, 1997: 153). There are two important needs that can be circumvented by the entrepreneur entering business by the way of acquisition. These are the need for expertise and the need for capital. Expertise is readily available because present employees of the acquired business should already have been experts in their jobs. Having the seller helping to finance through leveraging the buyout can circumvent the need for capital. The buyer can also arrange to pay off over time from earnings of the business and may be able to borrow against assets of the business from financial institutions (Bygrave, 1994: 65). Nevertheless, it is still important that the entrepreneur scrutinises all entry route options, as buying an existing business may have its problems. Whilst buyers have a tendency to become emotionally attached to a certain business opportunity, sellers have a tendency to emphasize only the positive aspects of their businesses, because they do not want to jeopardise the sale (Brenner, 1990: 13). Sellers also tend to hide their true motives for selling their businesses, often giving *good* rather than *true* reasons (Siropolis, 1986: 98).

The prospective entrepreneur therefore needs to thoroughly investigate the acquisition, using expert assistance.

3.2.2.1. Advantages and disadvantages

This option has its advantages and disadvantages that the entrepreneur needs to carefully take into account when anticipating this as an entry route.

□ Advantages

- Customers are already familiar with the location of the existing business (Hatten, 1997: 153).
- Planning can be based on actual historical figures, rather than on projections, as with a start-up (Hatten, 1997: 153).
- There is already an established customer base (Hatten, 1997: 153).
- Supplier relationships are in place (Hatten, 1997: 153).
- The amount of inventory and equipment are already in place (Hatten, 1997: 153).
- Experienced employees are already in place (Brenner, 1990: 14).
- Possible owner financing (Brenner, 1990: 14).
- If the seller is more eager to sell than the buyer, the business may be available at a bargain price (Longenecker, Moore, and Petty, 2003: 128).
- The seller may provide valuable assistance in running the business, which can help prevent the entrepreneur from making costly mistakes through ignorance (Brenner, 1990: 14).
- The transaction becomes a single purchase issue (Brenner, 1990: 14).
- One competitor is eliminated (Brenner, 1990: 14).

□ Disadvantages

- It may be difficult to change the old image of the business in the initial stages, especially if it had a bad one (Hatten, 1997: 153).

- Current employees may be incompetent or may not be able to adapt to the style of the new management, or they may resist change (Hatten, 1997: 153).
- The business may not have operated the way the entrepreneur liked and he or she could find it difficult to change (Hatten, 1997: 153).
- Outdated equipment and obsolete inventory may be acquired (Hatten, 1997: 153).
- The area where the business is situated may be starting to deteriorate (Brenner, 1990: 14).
- The personality of the business is a reflection of the previous owner; it might therefore take a long time to change the personality of the business (Brenner, 1990: 14).
- There is a possibility that the business is overpriced (Scarborough and Zimmerer, 1996: 200).
- The real value of accounts receivable may be worth less than their face value (Scarborough and Zimmerer, 1996: 200).
- The purchase is predictable upon the past, not on the future. Who will therefore know if the business being acquired is about to lose a major customer (Brenner, 1990: 14)?

Small businesses fail for many reasons. It is therefore important that great care is taken when buying a going concern. The entrepreneur needs to ensure that it is a real opportunity and not a problem that is being acquired. The past track record of an existing business surpasses the guesswork required to evaluate a fledgling business, but past records will not eliminate risk (Siropolis, 1986:98). The need for proper evaluation cannot be over-emphasized. According to Bekker and Staude (1996:31), an established business can be evaluated with reasonable accuracy because it has a recorded history. Therefore this advantage should be utilized. Financial data need to be carefully scrutinized to determine the performance of the business and the direction in which it is moving. Financial statements and tax returns may be used in order to assess the business (Longenecker, Moore, and Petty, 2003:130). Enough knowledge and experience is required in order to recognize specific details that are most relevant to the type of business being investigated. Emotions should not cloud the decision. Expert assistance should be sought to ensure compliance with all legal requirements, even if this is just to confirm the final calculations done by the entrepreneur.

3.2.3. Taking over a family business

The next entry route into small business entrepreneurship is taking over a family business. Family businesses are described as businesses in which two or more members of the same family control, are directly involved in the operation and own a majority of the business (Hatten, 1997: 170). The nature and extent of the involvement may vary. For instance, in some firms the family members may work part-time, whilst in others they may work full-time, serving as manager to receiving clerk or cashier. In South Africa, passing the business over to the next generation is more common amongst the Indian and Muslim communities, e.g. Asmals, Willowton Oil and others in Pietermaritzburg. This has made some of their businesses grow and flourish. "When it works right there is nothing, that succeeds like a family firm" (Scarborough and Zimmerer, 2000: 21). Family businesses have unique characteristics in that they have complex interrelationships. As the family business is composed of both family and business, these exist for fundamentally different reasons. The family goals include the fullest possible development of its family members, provision of equal opportunities and rewards, whilst those of the business as an entity are survival and profitability. This has a potential for conflict. (Longenecker, 2003: 168). The different ways in which different family members may be involved in the family business may complicate the management process and this may lead to conflict. The family business has its culture, whilst the family has also its culture. The family culture can cement relationships between business and employees, whilst on the other hand it may result in lack of professionalism lead to nepotism, and end up in conflict (Burns, 2001:358).

Another very challenging issue in family businesses is that of succession planning. Although it is continually acknowledged as important management succession planning is often ignored (Hodget and Kuratko, 1995: 64). Some of the reasons are:

- Owners are too busy with actual daily operations of the business and often ignore to plan for their own exit.
- Owners do not have confidence in the offspring who are supposed to take over.
- Owners do not often see family perpetuity as a major concern.

As death and retirement are events that are inevitable, for a profitable succession of an entrepreneur's pursuit, the process of succession must be planned properly. It needs to be noted that the process could be an emotional issue, because it does not only requires structural changes, but cultural changes as well. "The *family business* and the *business family* are two distinct components that must be dealt with and disentangled if progress towards succession is to be made" (Hodgets and Kuratko, 1995: 65).

In spite of these conflicts, a family business enjoys some competitive advantage. Individuals, work with and report to a family member in whom they can confide and, as for customers, the experience of dealing with a family member can reassure a customer as much as speaking to a large firm's president. There exists a sense of trust between family members and this has a potential of making family partners more secure, more open and more informed than any of the unrelated persons could be. Representing a family operation, owners can convey an image of stability (Hodgets & Kuratko, 1995: 56). Other important strategic advantages of family businesses are:

- A family business is capable of demonstrating higher levels of concern and caring for individual employees than would large corporations.
- Family businesses can take a long-run view more easily than corporate managers, who are judged on the basis of year-to-year results.
- Family businesses have a history of maintaining a tradition of providing quality and value to the consumer.

Amid the complex challenges they face, family businesses still succeed. Steers and Chicken Licken are one of those successes in the South African catering industry that have been so successful that they have grown and became strong franchising companies. The first reason for this, according to Hodgets and Kuratko (1995:56), is that family businesses have strategic freedom from demanding stockholders, who often want to dictate operating strategies. The second reason is their flexibility. They can easily respond to various challenges and opportunities in an unrestricted manner. Thirdly, their ability to sacrifice short-term profits for long-term gains really works for them. Lastly, family members, as employees, are known to be more productive than other employees. These features of family businesses can contribute to superior business performance if they are properly and fully exploited.

3.2.3.1 Advantages and disadvantages

As with other routes, there are advantages and disadvantages associated with family businesses:

□ Advantages

- Family businesses have a long-term orientation. They have a greater independence of action, as most of them enjoy less pressure from stock market and there is less risk of a take-over.
- The family culture, they maintain, is a source of pride. It inculcates strong identification, commitment and motivation and ensures continuity in leadership.
- They are known to have greater resilience in hard times and they have willingness to plough back profits.
- They are less bureaucratic and are more caring; they have greater flexibility and thus quicker decision-making.
- There are more financial benefits for members. Family members have an opportunity for early training and this ensures greater knowledge of the business (Hodgetts and Kuratko, 1995: 59).

□ Disadvantages

There are numerous disadvantages associated with family businesses and these need to be considered when taking over such businesses:

- Less access to capital markets may hamper their growth.
 - Family businesses are characterised by messy structures and no clear division of tasks and this may create conflicts.
 - Nepotism leads to tolerance of inept family members in control positions, inequitable reward systems and greater difficulty in attracting professional personnel.
 - High possibility of a “spoiled-kid” syndrome.
 - Possibility of endemic family disputes.
-

- They are often characterised by paternalistic and autocratic rule, resistance to change, secrecy and attraction of dependent personalities.
- The family business often experiences financial strains as a result of family members milking the business and disequilibrium between contribution and compensation.
- Succession dramas are common, as proper succession planning is seldom done (Hodgetts and Kuratko, 1995: 59).

These advantages and disadvantages need to be weighed properly to ensure success and prosperity of family businesses that are vital components of South Africa's economy. Nepotism and succession planning, in particular, need to be treated carefully. Concerning succession planning, a well-formulated strategy that will address issues such as contextual aspects of the plan, successor qualities and the way in which it is to be implemented, need to be put in place (Hodgetts and Kuratko, 1995: 74). In order to avoid such things as nepotism, general family business policies need to be in place; in other words, the family business needs to be proactive rather than reactive. Such policies could also help prevent problems like animosity from non-family employees that could negatively impact on motivation and productivity (Hatten, 1997: 172).

3.2.4. Franchising as an entry option

Franchising represents an opportunity for an entrepreneur to enter into a business with less risk and without experience and knowledge of the business as the product or service has already proven itself on the market and training is provided by the franchisor. It is an important strategy by which an entrepreneur (franchisor) can grow the business without personally committing excessive capital, as individual franchisees provide for their own start-up capital (Hisrich and Peters, 1998: 511). The franchise arrangement allows the entrepreneur starting the business to benefit from the accumulated business experience of the mother company, in this way reducing overall risk associated with buying an independent business or starting from scratch (Longenecker, Moore and Petty, 2003: 145). It is therefore a relatively safer entry route to business entrepreneurship, compared to other options.

The definition of a franchise business is “the entitlement of a franchisee by a franchisor to trade under the trademark of the franchise and to make use of a package comprising all the elements necessary to establish a business” (Kasselman, de Beer, and Vermeulen, 2002: 154). It is a well-established concept worldwide. South Africa has an annual growth rate of franchise systems of 32,5%, the largest being the retail sector (Kasselman, de Beer, and Vermeulen, 2002: 154). Compared to other countries it seems South Africa is still trailing behind. In the retail sector, for instance, South Africa currently commands only 7% of the retail market, whilst in countries like the USA, 40% of all retail sales are handled by franchising (Van Aardt and Van Aardt, 2000: 92).

When a service is franchised, the franchisee receives a licence for a trade name and that particular service that is to be sold. Similarly, when a product is franchised, the franchisee receives goods from the franchisor and sells them through a wholesale or retail outlet, e.g. auto dealers. The business operation, its décor, the merchandise and even the operating procedures are standardised. In order to maintain this standardized image and marketing approach, the franchisor usually maintains a strong formalized system of control over the business operation. The responsibilities of both parties are fully spelled out in the contract, to ensure ease of co-operation, and guidelines for the relationships are also clearly spelled out, as all these are crucial to the survival and prosperity of the established business.

The entrepreneur thus gets a ready-made business and that is what makes franchising so appealing. The fact that it benefits both the franchisee and franchisor enhances its appeal; it offers an opportunity with limited risk for the entrepreneur. In a franchising relationship, each party depends on the other for support. The ideal franchising relationship is thus a partnership based on trust and willingness to work together for the benefit of both (Hodgetts and Kuratko, 1995: 104). The next important reason that makes franchising thrive is because it merges the incentive of owning a business with the management skills of a corporate business (Siropolis, 1986: 127). As the trend of downsizing by major companies takes place, former managers get attracted to franchising because “They would like to be in a certain corporate setting and follow some corporate guidelines, yet control their destiny” (Hodgetts and Kuratko, 1995: 104). Franchising, therefore, offers almost the best of both worlds.

3.2.4.1. Drawbacks and benefits of franchising

As stated above, franchising is beneficial to both the franchisor and the franchisee. It offers the franchisor a quicker and cheaper way of expansion and an ongoing income in the way of royalties and franchise fees. However, the one major problem, especially for the franchisor, is maintaining the balance in the relationships, the balance between control and autonomy. “The franchise relationship has been recognised as one of tension between the franchisee’s desire for autonomy, on the one hand, and the franchisor’s need for control, on the other...” (Stanworth and Stanworth, 1999: 74). Attempts to enforce conformity can be very frustrating for both franchisor and franchisee alike. Thus, while this relationship is crucial for the survival and success of the enterprise it can be very fragile for the parties, especially for the franchisor, who must maintain the required standards in order to protect the image of the company.

□ Drawbacks for the franchisee.

While franchising has a number of benefits to the entrepreneur, these are available at a price that he or she has to pay. These therefore need to be explored carefully by the would-be entrepreneur when evaluating entry routes. Some of these are discussed below.

• Franchise fees

All franchise agreements involve some type of fees: franchise fees that are upfront payments and royalties that are ongoing and charged as a percentage of cost on turnover are in the range of 9% in most South African fast food franchisers. Higher franchise costs characterize the better-known and more successful franchises (Longenecker, Moore and Petty, 2003: 153). The disadvantage is that the entrepreneur has predetermined costs that can have a negative impact on profitability. Whether the business will make a profit or not, royalties have to be paid and they are charged on gross turnover, sometimes with a fixed minimum. It is therefore imperative that proper viability studies are done, including profit projections, in order that the expected returns are carefully compared with other investment options.

- **Strict Adherence to standardised operations**

Although the business is owned by the franchisee, the autonomy is not the same as that of an independently owned business. The relationship between the parties here, are governed by the franchise agreement (Scarborough and Zimmerer, 2000: 176). Normally, business individuals leave salaried employment for entrepreneurship because they dislike working under the supervision and control of others, which is one of the traits of entrepreneurs. In a franchise relationship such individuals may be frustrated because of franchisor control and supervision. The franchisor ensures conformity and adherence to set procedures and standards in order to protect their image (Longenecker, Moore and Petty, 2003: 153). Accordingly, it is imperative that the entrepreneur does thorough investigation when deciding to choose franchising as an entry route and ensures that the conditions of the franchise will not clash with his or her personal interests.

- **Restriction on business operations**

In an attempt to protect the image of their franchise, franchisors have a number of restrictions on how the business should be conducted and these are incorporated in the franchise agreement. They may include restrictions on sales territories, restriction on supplier choice, restriction on product/service lines and restriction of location choice (Longenecker, Moore and Petty, 2003: 153). While this serves the purpose of maintaining quality standards, it has also a tendency to give a favourable bargaining power to the preferred supplier, to the disadvantage of the franchisee. The next disadvantage to the franchisee is that these restrictions are laid down by the franchisor and are subject to unilateral change (Stanworth and Stanworth, 1999: 74).

- **Problems on termination or transfer**

Conflicts sometimes occur when the franchisee sees that the performance of the business is unsatisfactory and wishes to terminate the franchise agreement whilst, the franchisor might still be satisfied with the royalties that are only sales-based. Furthermore, the agreement can be terminated against the franchisee's will as the franchisor wields the greater power than the franchisee. This is why it is imperative that before entering the agreement these factors should be clearly spelled out. Most franchise agreements are

standard and are on the terms of the franchisor, the owner of the franchise, the franchisee has, in most cases, little to say. As a result the importance of scrutinising the franchise agreement with the help of a legal expert is crucial (Hatten, 1997: 130).

- **Restriction on freedom of creativity**

“The best franchisee, as far as many franchisors are concerned, is someone who is smart enough to understand and operate the system, but not smart enough to try to improve on it” (Siropolis, 1986: 130). The franchise environment can thus kill chances of innovation on the side of the franchisee.

Entrepreneurs should be aware of these drawbacks so that they can make the right choices after they have done thorough investigations, with the guidance and assistance from experts in the field of franchising.

- **The benefits of franchising.**

A number of advantages are associated with franchising. According to Burns, only about 10% of franchise businesses fail and one reason is that the franchisor shall have operated the business concept with success for a reasonable time before starting the franchise network (Burns, 2001: 128). Some franchises operate one or two of their own branches, for experimentation and training purposes. In this way they keep in touch with the markets. Some of the franchising benefits are discussed below.

- **Training and Guidance.**

One of the main causes of failure in small businesses is incompetent management and it seems franchisors are well aware of this, if one considers the kind of training and support they afford their franchisees. This ranges from management training right up to employee training, in fact, special training programmes are offered prior to the opening of a new outlet. These include training in theory, hands-on training at the franchisor's outlet and further training on site of the franchisee's new business. Start-up training is often supplemented by ongoing follow-up instruction and support. One of the greatest advantage of these training programs is that they provide the young entrepreneur, who

sometimes has only a limited amount of training in business, the opportunity to pick up a great deal of practical skills and knowledge that can spell the difference between success and failure (Hodgets and Kuratko, 1995:134). The importance of this training to the entrepreneurs is that it alleviates weaknesses in their management skills.

- **Established brand name**

The franchisee is acquiring an established brand name. The advantage of identifying the business with a widely recognized brand name has thus been gained and this has a drawing power that could impact positively on sales turnover. “Indeed, one of franchising’s basic tenets is cloning the franchisor’s success” (Scarborough and Zimmerer, 1996: 170).

- **Standardised quality of goods or services**

The franchisee is benefiting by acquiring proven quality products or services, of which customers are already aware and know what to expect. This is an important achievement for the entrepreneur, as building a sound business reputation could be costly and not easy to achieve in a short space of time. In order to protect standardised quality and service, therefore, franchisors conduct periodic inspections to ensure conformance. This is understandable, as any lowering of quality levels could impact negatively on the image of the entire chain (Scarborough and Zimmerer, 200: 170).

- **Marketing expertise**

The franchisee acquires a brand that is known nationally, or even internationally, through advertising campaigns that cost millions of rands. The franchisee does contribute to advertising but such advertising campaigns are organised and controlled by the team of experts from the head office and the costs are shared by the franchisor and all its franchisees.

- **Finance**

In a franchise business, it is easier to obtain finance than for own start-up, because of lower risk of failure and because the product or service has already proven itself on the market (Burns, 2001: 128). Some franchisors have standing arrangements with their bankers to provide start-up capital for their franchisees. This is crucial, as sufficient finance is one of the critical factors the successful start-up. The credit-worthiness of the young entrepreneur is normally weakest at this time and the association with a well-established franchise might enhance the aspiring chances of obtaining finance (Longenecker, Moore and Petty, 2003: 150).

- **Established format and proven products**

There is ease of entry, as the business format is established, and the entrepreneur does not have to build the business from scratch. Although taking up a franchise is by no means a cheaper option, the percentage of expensive errors made by individuals starting on their own is substantially reduced by adoption of a tried and tested format (Barrow and Golzen, 1994: 29). This enhances the chances of success, as standardized procedures and operations eliminate the inefficient trial and error learning (Scarborough and Zimmerer, 1996: 171).

- **Centralised buying power**

The more the number of outlets that are owned by the franchisor, the stronger the buying power and the advantages derived from this could be to the benefit of all the outlets in terms of good prices and potential for good profit margins (Scarborough and Zimmerer, 1996: 171). This, in turn, eliminates the economies of scale disadvantage that is typical to small and independently owned businesses.

- **Territorial protection**

Franchisees may enjoy territorial protection that can give them the exclusive right of distributing a brand-name product or services. Another important advantage is that the

franchisee has a backing of a well-known trading name when negotiating for good sites with letting agents or shopping centre or mall owners (Barrow and Golzen, 1994: 29).

- **Networking opportunities**

Being part of a franchise family offers a great opportunity for networking. There is no doubt that the franchisee will meet with fellow franchisees at their business meetings. Some franchises hold meetings quarterly, whilst others hold their meetings yearly. All these meetings enable franchisees to share their experiences and problems, and to have "... a useful platform to bounce things off on" (Hetherington, 2003: 1). It might also be easier to sell a well-known franchise brand to a fellow franchisee, as networking facilitates this.

In view of the above, franchising is one of the attractive entry routes to entrepreneurship. The success rate of franchising is much higher than that of independently owned businesses and raising start-up capital is much easier for the entrepreneur. Stanworth et al. (1998:57) suggest that some of the causes of failure that are common to small business, namely *under-capitalisation, absence of the economies of scale, lack of business acumen and the inability to survive intense competition*, should actually be reduced by franchising, because of the possible support that it enjoys from the franchisor. The franchisor not only provides the entrepreneurial expertise, but acts as a role model and mentor who contributes to successful entrepreneurship (Kasselman, de Beer and Vermeulen, 2002:155-156). Franchise businesses require a higher level of initial capital than independent businesses and that, in itself, should explain why franchises have a superior propensity for survival (Stanworth et al., 1998: 66). Mc Alpine, however, warns that one must not be blinded by the positives of franchising as most franchise statistics are supported by the successes of big franchising, companies like McDonalds, Kentucky and Wimpys. Even these big companies do face difficulties, as happened with McDonalds in South Africa, where they had to close 15 out of their 103 branches (Mc Alpine, 2003: 1). This underlines the importance of a thorough investigation into all franchise opportunities no matter what franchise company is involved. The following steps could be taken to minimise the risks of investing in a franchise:

- **Investigating the franchise**

As with all business opportunities, a franchise business needs to be thoroughly investigated. The entrepreneur needs to satisfy himself/herself that the chosen franchise is a business wherein his or her skills, expertise and financial resources can be fully utilised to generate wealth. The would-be entrepreneurs need to be realistic about the potential of the franchise, the risks of the franchise, and the returns that can potentially be achieved (Mc Alpine, 2003: 1). The following factors need to be considered:

Unproven versus proven franchise.

The unproven franchise may be less costly, but its lower investment costs are offset by a substantial amount of risk (Hisrich and Peters, 1998: 520). The proven franchise offers reduced risks and higher probability of success, although at a premium price. The entrepreneur therefore needs to weigh these options carefully.

Financial viability

The financial stability of the franchise should be assessed and long-term stability and profitability need be ascertained (Hisrich and Peters, 1998: 521). Other sources of information that need to be investigated include *existing and previous franchisees of the organisation*. These can be telephoned or personally visited to be interviewed, in order to establish how successful they are and to establish reasons for giving up the franchise from those who are no more trading. The viability of the franchise itself needs to be established. In countries like America, franchisors are required to provide franchisees with *disclosure statements*. In South Africa, according to The Franchise Association of Southern Africa (FASA) (2003: 31), their code of ethics provides, in their *Disclosure Document*, that their members provide franchisees with the disclosure statement. The franchisee therefore needs to establish whether the franchise is registered with the *Franchise Association*, in the case of South Africa with FASA, and obtain the information required to evaluate the financial viability of the franchise that is being investigated. In short, the aim is to establish how healthy the franchise organisation as a whole is and how attractive the particular franchise opportunity is that the entrepreneur is

pursuing. Do not take everything the franchisor says for granted; investigate and find the facts yourself! (Patricio, 2003:1).

Potential market for the new franchise

Market research will be necessary in order to assess attitudes and interest in the new business. Other issues that need to be investigated include checking *whether the product/service has unique features, how competitive is the product/service on the market and whether the market is growing, static or declining*. The *size of the market* needs to be estimated by evaluating the traffic and pedestrian flow and the demographics of the residents in the area. The demographics of the area can be determined from census data that are obtainable from libraries or municipal offices (Hisrich and Peters, 1995: 522). Competition from other franchise and non-franchise firms is an important factor in the success of the new venture and it therefore also needs to be investigated and evaluated.

Estimate profit potential for the new franchise

Projected income statements, balance sheets and cash flow statements need to be calculated. This will culminate in a business plan for the new business. This will enable the entrepreneur to compare returns from the new venture with other investment options. The impact of the franchise and royalty fees on profitability also needs to be carefully assessed.

Involve professional assistance

The franchisee should use the services of experts in the field of franchising, such as an accountant and an attorney who specialise in the franchise business. This could result in unbiased assessment and reporting on the proposed venture and these consultants should not be the choice of the franchisor (Van Aardt and Van Aardt, 2000: 76).

• **Self Evaluation**

Drawbacks discussed above indicate that franchising involves many risks to the entrepreneur and, like all other businesses, it requires hard work and commitment. Some

of its problems are unique, for example the loss of independence as the franchise business operates under a set of fixed rules that the franchisor has to enforce, and this sometimes infringes on the freedom of the entrepreneur and could result in conflicts. Not every franchise therefore will be right for every entrepreneur. Self-evaluation is thus important, in order to ensure that the characteristics of the entrepreneur really match the proposed franchise opportunity. It has also been seen that some of the causes of failure at the start-up phase have to do with the ability of management to take situationally appropriate decisions as the business evolves through its growth stages. The one disadvantage of small businesses is that their owners often manage them because they cannot afford the luxury of buying in specialist help, especially at the start-up stage, when financial resources are scarce and normally hard to come by (Burns, 2001: 78). Secondly, top management is usually a job for a team rather than one person and the tendency of one-person management is less willingness to change personal management practices as situations change. According to Drucker (1961: 150), one-man top management is a major reason why most businesses fail to grow. The entrepreneur needs to do these self-evaluations earnestly, as he or she is the vital ingredient for the success of the new venture. Additionally, he or she should be an all-rounder and able to adapt when change is called for by changing environmental situations.

3.3.0. STRATEGIC PLANNING FOR COMPETITIVE ADVANTAGE

Entrepreneurs entering the market, whether through franchising, start-up, acquiring a going concern or taking over a family business, need to establish a solid foundation on the market. Strategic planning becomes the key to the ultimate survival and success of the business, as it allows the entrepreneur to plan ahead and evaluate alternative courses of action (Scarborough and Zimmerer, 1996: 95). The entrepreneur needs to craft a game plan for moving the business into an attractive position on the market and building a sustainable competitive advantage. In order for the entrepreneur to achieve the effective strategic positioning, internal and external environmental scanning becomes critical, the firm therefore needs to make ... "choices that reinforce each other" (Hill, 1995: 171). This should be an ongoing process, as the environment is ever-changing and businesses need to adapt strategically to these changes. Start-up failures are due to the

inability of management to adapt to changes. This makes strategic management even more crucial to small businesses.

According to Pierce and Robinson (2000: 294), the two important sources of competitive advantage can be found in the firm's cost structure and its ability to differentiate its business from competitors. Businesses that create competitive advantage from one or both of these sources usually produce results that are above-average within their industry and tend to enjoy the highest levels of profitability. Businesses that lack a cost or differentiation advantage usually experience average or below-average profitability. Porter (1980: 41) advises that a firm that wishes to gain competitive advantage should make a choice among what he terms *generic strategies*, namely, overall cost leadership, differentiation and focus, and that the firm that is "stuck in the middle" is almost guaranteed low returns. The challenge for the business, therefore, is to provide a product or service perceived by customers to be unique and for which they are prepared to pay more or providing a good product or service at a lower price. All of and all this requires building competences and resource capabilities that are not readily matched (Thompson and Strickland, 1998: 135). The firm's resources need to be analysed in order to identify those that are critical sources of competitive advantage. There are characteristics that will determine whether the value of the resource or competence is capable of giving sustainable competition or not (Pierce and Robinson, 2000: 195-199). Some of these are discussed below.

- **Competitive superiority**

The resource must help fulfil a customer's need better than the firm's competitors, in other words the competence or resource set possessed by the firm should be superior to those of the competition.

- **Resource scarcity**

The firm should be in possession of a resource that is in short supply and that is central in fulfilling customers' needs and which the competition does not possess.

- **Inimitable resources**

These are resources that are unique, not imitable, and offering the business the capability to provide unique value to its target market. The degree of inimitability may vary from *cannot be imitated*, *difficult to imitate*, *can be imitated but may not be* and *easy to imitate*.

- **Appropriability**

These are resources that the business develops and controls and from which all the profits accruing are for the benefit of the business.

- **Durability**

This entails how rapid the resource will depreciate; the slower it depreciates, the more value it possesses.

- **Substitutability**

This is the test of how easy the product can be substituted, that is the creation of a similar product that could be perceived by customers to have the same value. The less the chance of substitutability, the more valuable the resource is to the firm.

Any long-term strategy should, derive from the firm's choice of its generic strategy or strategies. Its long-term or grand strategy must be based on this core idea about how it can best compete in the market place (Pierce and Robinson, 2000: 247). This is the generic strategy or strategies chosen in accordance with the unique competences that the business has identified to suit the opportunity pursued.

Although small businesses might not have the luxury that all their resources possess all these qualities, these could be built over time. The Pick and Pays of South Africa, for example, started small and have become giants of their industry by creating a very strong brand that is not easy to imitate.

3.4.0. CHOICE OF THE LEGAL FORM OF OWNERSHIP

The last topic in this chapter is the legal form that the new business may take, as this will have strategic implications. In South Africa the *sole trader*, *partnership*, *private company*, *the close corporation* and *the public company* are the most common forms of ownership and perhaps the first four are the most common amongst small businesses. Although the decision on the form of ownership is not irreversible once taken, changing from one form of ownership to another once a business is up and running can be difficult, expensive and complicated. It is therefore important that an entrepreneur makes the right decision on this at the beginning (Scarborough and Zimmerer, 2000: 70). What is important in choosing the right legal form is understanding the characteristics of each form and knowing how these may affect the strategic decisions of the business, because each one has its own unique characteristics. Also important to consider are the advantages and disadvantages of each form, as these may influence the planning and performance of the business. Some of these factors:

- **Tax Implications**

In South Africa there are different tax brackets for individuals and businesses. For individuals and sole traders the rate is currently 40%, whilst for companies and close corporations it is 30%. There is, however, an incentive for small businesses, where the tax rate is 15% for companies or close corporations whose members or director has no business interest in any other businesses and the turnover of the business is less than R5m and where the profit is less than R150 000. It is thus important to consider all these factors when deciding on the legal form of the new business.

- **The Liability Exposure**

Different forms of ownership will offer different protection from personal liability to the owner and the entrepreneur therefore needs to decide the extent to which he or she will be willing to assume personal responsibility for the business's obligations (Scarborough and Zimmerer, 200: 71). The sole trader and his or her assets, for instance, are considered as

one and the owner is thus personally responsible for all the obligations of the business (Bekker and Staude, 1996: 103).

- **Venture Capital**

Different forms of ownership will have different abilities to raise start-up capital and further financial needs as the business grows, for instance public companies are able to get equity funding, whilst with other forms their sources of funding are limited to their members and outside borrowing (Bekker and Staude, 1996: 104). The cost involved in creating the business may differ and some forms are more costly than others (Scarborough and Zimmerer, 200: 71).

- **Control**

It is important to decide early on how much control the entrepreneur wishes to retain, as, with some forms of ownership, the entrepreneur will definitely sacrifice some control (Scarborough and Zimmerer, 200: 71).

- **Consideration of Advantages and Disadvantages of Each Form**

Each of these forms of ownership has its own unique advantages and disadvantages and the entrepreneur needs to weigh them carefully so that the right choice is made. These are not discussed in this study, but almost all small business textbooks will contain these. It is important that the entrepreneur carefully considers them, weighing one against the other, to ensure that the choice of the legal form of the new venture is in alignment with its short and long-term strategic goals.

- **Management**

It is important that, when choosing the legal form of the business, the entrepreneurs look ahead to the day when they will pass their businesses on to the next generation, or sell them, as some forms may make the transition process much easier than others. The next crucial issue the entrepreneur needs to consider regarding management is assessing the abilities he or she possess to run the business, because if there is a shortage of skills, the entrepreneur needs to choose a form of ownership that will allow him or her to bring in

people who possesses the skills required (Scarborough and Zimmerer, 200: 71). This is one of the crucial points to consider, as management effectiveness is critical to the success and prosperity of the business. According to Drucker, management is indeed a problem typical to small businesses, because, although they are small, they may well require as much management competence as is required by big business, and yet they are not in a financial position to be able to pay ... "what a first-rate man can get in a large business even in lower-ranking positions." In small businesses, therefore, management positions may require greater versatility than the same position in large companies (Drucker, 1961: 207).

3.5. CONCLUSION

Careful preparation and the choice of a feasible strategy is very important before venturing into small business entrepreneurship. The entry routes to business entrepreneurship are numerous, ranging from a fresh start-up to buying a going business concern. Whatever entry route the entrepreneur chooses, the risks and challenges he or she will encounter are numerous. Every business has its own history and strategy. It is therefore important that, when building this strategy, every element is made to fit correctly, so that the business becomes a single robust unit, irrespective of size. The underlying aim therefore is that the new organization is so shaped that it fits the market gap that defines its identified opportunity, with a differential advantage. The business needs an appropriate winning strategy for its long-term survival.

In order to support entry into any market, testing the consumers' response is critical. The success and survival of any enterprise is dependent on this support. Chapter 4 deals with this issue in detail.

CHAPTER 4

RESEARCH DESIGN

4.0 INTRODUCTION

This chapter identifies the research objectives, hypotheses and design appropriate to assess whether opening a Chicken Licken franchise in Richmond is worthwhile. The study was considered descriptive and hence a personal interview technique was selected, amongst others. The chapter explains about the population, the sample and the development of the research instrument. The last section of the chapter provides the results of the pilot study.

4.1. BACKGROUND TO THE STUDY

This is a case study of divesting and investing as a strategic entrepreneurial option in the Midlands small business environment. One business was divested, in this case K. H. Foods Services CC, trading as Steers Longmarket, which was under-performing. The business was showing profits that were below the industry average, which is currently 15% ROI, according to the Chicken Licken Head Office. The underperformance was further confirmed by the opportunity loss, which revealed that the cost of capital, R635 000, that was invested in this business, was earning far less than what it could have earned if it was invested in a money market or a financial institution (see also Tables 6.1, 6.2, and 6.3 in Chapter 6).

According to Higgins & Vincze, (1993: 265), businesses that are consistently under-performing should be divested. This point will be further elaborated in the Grand Strategy Selection Matrix in the next chapter. Funds that were realised from the divestiture were to be re-invested and it was decided that starting a new business through franchising was one of the investment options to be considered. As the writer already owned a Chicken Licken business and a franchise relationship had already been established and was ongoing, this specific franchise was chosen. A market gap was identified in Richmond. In order to establish whether this was a real business opportunity

and whether the investment would be worthwhile, a feasibility study was conducted in the Richmond area.

4.2. RESEARCH OBJECTIVES

The bases of this study were small businesses and their significance to the economy and the main focus was on divesting and assessing a business opportunity for the purpose of re-investing funds that were realised from the divestiture. A Chicken Licken franchise opportunity was to be investigated in Richmond. The following objectives were the focus of the study:

To test consumers' response towards a Chicken Licken franchise.

To assess the viability of a Chicken Licken business in Richmond.

To take a decision, based on the findings, whether to open a Chicken Licken outlet in Richmond or not.

To formulate proposals and recommendations regarding the state of small business development in South Africa.

4.3. HYPOTHESES

This study investigates whether it is viable to establish a Chicken Licken franchise in the Richmond area. Therefore the following hypotheses were formulated, for empirical testing:

H₀: There is a real opportunity for a Chicken Licken outlet to be established in Richmond.

H₀: Consumers in Richmond are aware of the Chicken Licken brands.

H₀: The income groups fit Chicken Licken's target market.

4.4.0. RESEARCH DESIGN

The research design consists of methods and strategies used to conduct a study (McCall, 1998:312). The following subsections will describe the population and sample size, sources of data, instrument for data collection and the approach to data analyses.

4.4.1 The Research Population and Sample

The population, for the purpose of this study, was defined as all adult residents of the Richmond area who visit public eating-places. It is usually not possible to study the whole population. Accordingly, researchers chose to study a part of the population for drawing conclusions about the population (Sapsford, 1999:50). The selected part of the population is called the sample.

The question of sample size is very complex, since it depends on the time, money, and personnel available for the study. Owing to resource and time constraints, a sample of 120 people was chosen for this study. A purposive sampling method was used in order to be able to include the characteristics that were regarded to be important for the study. Since Richmond area is composed of a population of mainly workers, employees were targeted and visited in their places of employment. Most of them are nurses, teachers, police officers, taxi drivers, post office staff and bank staff. Interviewees were also picked randomly from the streets in Richmond.

4.5.0. METHODOLOGY

A survey approach with the aid of a questionnaire was used to gather relevant data about the population being studied. This type of research often provides the number of times something is likely to occur and lends itself to statistical calculations of the average number of occurrences. In this survey respondents in the Richmond area were interviewed using a structured questionnaire.

4.5.1 Secondary Sources

In order to obtain a wider view on the importance of small business, especially in the South African context, an extensive search of secondary data sources, namely the Internet, books, journals, newspapers and small business agencies' yearly reviews, was undertaken. In this way an in-depth understanding of the topic being studies was made possible.

4.5.2. Primary Sources

In order to determine whether a Chicken Licken franchise would be accepted and supported by customers from the Richmond area, the market was to be tested by using the way of a consumer survey. Choice of the data collection method is very important in surveys, as these may entail the use of personal interviews, telephone interviews, postal surveys or fax surveys. Each of these techniques has its pros and cons, however. Aaker, Kumar and Day, (2001:223) claim that telephone and mail surveys are dominant techniques. In mail surveys, questionnaires are mailed by post, fax, or e-mail, to the respondents. Mail surveys have the disadvantage of a poor response rate. Accordingly, personal interviews were considered to be more appropriate for the purpose of this study.

4.5.3. Interviews

According to Dunne (1995:3), interviews involve asking persons for information or opinions and recording these responses for decision-making. Interviews have the advantage of guaranteeing a high response rate and flexibility, as the researcher may include a supplementary question, avoid asking some questions that seem not relevant to the study, or clarify any ambiguity during the interview process.

In this study, personal interviews, with the support of questionnaires, were used to gather data. Although the response rate in personal interviews is high, the technique is relatively costly in terms of time and money and hence provides a limitation on the geographical coverage. Telephone interviews, mail surveys and Internet have the advantage of larger

geographical coverage. Owing to resource constraints these techniques were not utilised in this study.

4.5.4. Research Instrument

The questionnaire was developed in English. The questions incorporated in the questionnaire were designed using variables drawn from the literature review on the subject being studied. Appendix 4 shows that four questions were dichotomous, in which interviewees responded by a 'Yes' or 'No', four questions were in the form of ranks and respondents were asked to check the item that best suited their situation. In fourteen questions different options were formulated and respondents were to choose the item that best describes his/her response. The questionnaire contained 22 questions.

4.5.5. Pilot Study

A pilot study was initially carried out from 22-29 July 2003, in Richmond. The research instrument was pre-tested by interviewing thirty people. The pre-testing helped to identify and correct deficiencies of the questionnaire and ensure its acceptability, as well as its suitability for the purpose of this study.

As a result of pre-testing, the number of questions was reduced from 31 questions to 22. Seven questions were improved, eleven were deleted and two others were added. Of the eleven deleted, three were deleted for the reason that they were not contributing to the reliability of the questionnaire. Table 4.1 shows the results of the reliability test reflected by the Cronbach coefficient. The research instrument used had a Cronbach's $\alpha = 0.81$, which is considered as reasonably good.

Table 4.1 Results of the Reliability Test

	Scale mean if Item Deleted	Scale variance If Item Deleted	Corrected Item Total correlation	Alpha if Item Deleted
Qn.11	14.3917	26.2235	0.5386	0.8014
Qn. 12	13.8333	22.3922	0.3978	0.8438
Qn. 14	14.1917	23.4840	0.6010	0.7890
Qn. 15	13.9750	24.8985	0.5015	0.8032
Qn. 18	14.2417	29.5630	0.1468	0.8369
Qn. 20	14.2083	21.6957	0.7922	0.7588
Qn.21	14.3667	23.7468	0.7821	0.7706
Qn. 23	14.4833	23.3611	0.7410	0.7720

Reliability Coefficients

Number of Cases = 120.0 Number of Items = 8
Alpha = 0.8190

4.5.6. Data Analysis Strategy

Primary data was collected from a random sample of 120 people, to whom the questionnaires were administered. As places of work were also to be visited, letters were written to managers and officers-in-charge, to seek permission and to set up appointments or meeting with interviewees (*Appendix 4* on page 111). The interviews started on 1 August 2003 and were completed on 8 August 2003. On completion of data collection, the data was captured and analysed using the ‘Statistical Package for the Social Sciences’ (SPSS). The SPSS was used to undertake the reliability test, frequency tabulations, chi-square tests, correlation and regression analyses.

4.6. Limitations of the Survey

The focus of this survey was limited to business opportunity in Richmond. It was conducted in order to determine the attitudinal responses of potential customers of Chicken Licken in the Richmond area. The information was regarded to be important in the decision whether or not the Chicken Licken franchise was viable in the Richmond area. The study will therefore only give attitudes of this potential customer base in Richmond. Inferences made through the analysis of the questionnaire thus cannot give an all-encompassing analysis of the attitudes of any other area.

4.7. Conclusion

Chapter 4 has covered issues relating to the objectives of the study, hypotheses and research design. The chapter suggested the uses of a survey approach. The personal interview technique, with a structured questionnaire, was used to collect relevant data. The results of the pilot study revealed that the instrument was reliable ($\alpha = 0.819$

CHAPTER 5

RESEARCH FINDINGS, DATA ANALYSIS AND DISCUSSIONS

5.0 INTRODUCTION

Chapter 5 provides empirical data for deciding whether or not there is a need for a Chicken Licken franchise in Richmond. The chapter begins with a description of the socio-economic attributes of the surveyed respondents, in terms of age structure, location and gender. This is followed by an examination of the respondents' tendency toward visiting public eating places, their awareness of a Chicken Licken store and, more fundamentally, their interest in buying from the franchise. Section 5.3.0 shows the cross-tabulations between the respondents' monthly income and age, monthly income and gender, expenditure per visit and age, expenditure per visit and gender, expenditure per visit and location, also monthly income and location. Section 5.4.0 investigates whether there is any association between variables. Section 5.5.0 investigates the strength of association between selected variables and section 5.6.0 contains an attempt to fit a regression model.

5.1. STRUCTURE OF THE SAMPLE

The sample consisted of 120 respondents; of these 77.5 per cent were residing in Richmond and 22.5 per cent were from outside Richmond. *Table 5.1* shows that, of the surveyed respondents, 46.7 per cent were female and 53.3 per cent were male.

Table 5.1: Gender Distribution of the Sample

	Frequency	Percent	Cumulative Percent
Male	64	53.3	53.3
Female	56	46.7	100.0
Total	120	100.0	

With regard to employment status, only two were unemployed, four were employed part-time, and the remaining 114 were employed full-time. Of the 118 employed, 30 were drivers, 25 were in the police services, 23 were nurses and 22 were in other categories of employment.

The age structure shows that only 7.5 per cent of the respondents were younger than 25 years old, implying that 92.5 per of the sample consisted of adults who are likely to be earning some sort of income.

Table 5.2 Age Structure of the Sample

Age Group	Frequency	Percent	Cumulative Percent
Below 25 yrs.	9	7.5	7.5
26-33 yrs	31	25.8	33.3
34-41 yrs	45	37.5	70.8
42-49 yrs	27	22.5	93.3
50 and over	8	6.7	100.0
Total	120	100.0	

The respondents were asked to indicate their monthly income, as the higher their level of income, the greater the chances they would be able to buy Chicken Licken products. Of the sample surveyed (120), 13.3 per cent were in the income group below R1000, 21.7 were in the above R3001 group, while 65 per cent were in the income group between R1001 and 3000. The average monthly income for the sample was R 2403.95. The results suggest that most of the surveyed respondents were in the middle-income group.

Respondents were asked ‘Do you visit public eating places?’ As a summarisation, *Table 5.3* shows that 90 per cent answered “Yes” and only 9 per cent answered “No.” Of those who visit public eating-places, 59 usually visit the public eating-places daily, 12 visit once a week 13 twice a week, and 25 more than twice a week.

Table 5.3 Visit to Eating-Places

	Frequency	Percent	Cumulative Percent
Yes	109	90.8	90.8
No	11	9.2	100.0
Total	120	100.0	

Regarding awareness of the existence of a Chicken Licken store, interviewees were asked ‘Have you ever seen a Chicken Licken store?’ *Table 5.4* shows that 110 answered “Yes” to the question and only 10 answered “No”. The results suggest that the overwhelming majority of the respondents were aware of the existence of Chicken Licken franchises and its respective products.

Table 5.4 Awareness of Chicken Licken Stores

	Frequency	Percent	Cumulative Percent
Yes	110	91.7	91.7
No	10	8.3	100.0
Total	120	100.0	

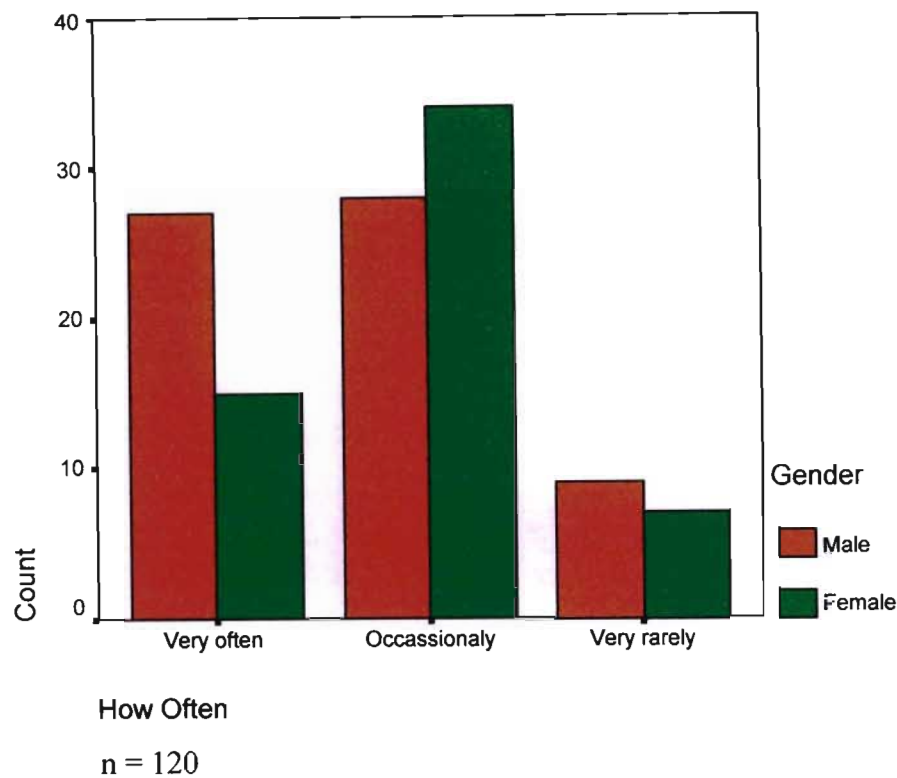
Regarding the frequency of visiting a Chicken Licken store, respondents were asked ‘Should a Chicken Licken franchise be opened in Richmond, how often are you likely to buy from that franchise?’ *Table 5.5* shows that 42 answered they would buy from the franchise very often, 62 answered occasionally and 16 answered rarely.

Table 5.5: Respondents’ Intention to buy from the Franchise

	Frequency	Percent	Cumulative Percent
Very often	42	35.0	35.0
Occasionally	62	51.7	86.7
Rarely	16	13.3	100.0
Total	120	100.0	

The cluster bar graph below (*Figure 5.1*) shows the relationship between the respondents’ intention to buy and their gender. Of those who would often buy from the franchise (42) 27 are men. Of those who will occasionally buy from the franchise (62), 34 are women. Nine men and seven women will rarely buy from the franchise. It was further found that there is no statistical association between the respondents’ intention to buy and their gender (chi-square = 3.743, df = 2, p = 0.154).

Figure 5.1: Frequency to buy from the Franchise and Gender



5.2.0 Cross-Tabulations

Cross-tabulations is one of the useful statistical analysis techniques for studying relationships among and between variables (Aaker, Kumar and Day, 2001:431). This technique is used to examine relationship between two variables at a time and these are presented in the following subsection.

5.2.1 Monthly Income and Age

The relationship between the respondents’ age and their monthly income is presented in Table 5.6 below. According to the Cross-tabs results for the monthly income and age groups; of 78 respondents who were earning between R100-3001, 25 are between 26-33 years of age, 36 are between 34-41, and 13 are between 42-49 years of age. The results suggested that 61.6 per cent of the potential customers who are earning between R1001-3000 are in the age group 26 – 49 years.

Table 5.6: Cross-tabulations Income Group (p.m.) and Age Group

Income/Age Group	less than 25 yrs.	26-33 yrs	34-41 yrs	42-49 yrs	50 and above	Total
R500-1000	4	3	4	2	3	16
R1001-3000	4	25	36	13		78
R3001 -5000	1	3	5	12	5	26
Total	9	31	45	27	8	120

5.2.2. Monthly Income and Gender

Table 5.7 shows the cross-tabs results for monthly income and gender. The results reveal that, of the 16 respondents with a monthly income between R500 -1000, 13 were females. Of the 78 respondents with monthly incomes between R1001–3000, 48 were males. The average income of the surveyed respondents was R2 403.95 on average, the surveyed males are earning R2395, while females are earning R2406.6. The results tend to suggest that females are in a slightly more favourable income group than the surveyed males.

Table 5.7 Cross-tabulations between Income Group (p.m.) and Gender

Income/Gender	Male	Female	Total
R500-1000	3	13	16
R1001-3000	48	30	78
R3001-5000	13	13	26
Total	64	56	120

5.2.3 Expenditure per Visit and Age

Table 5.8 shows that the majority of the respondents (68) are willing to spend between R23-33 per visit. Of these, 63 are over 26 years of age, while five are under 25 years of age. Moreover, of the 45 respondents within the 34-41 age group, 12 are willing to spend between R12-22 per visit, 26 are willing to spend between R23-33, while 7 are willing to spend over R34 per visit. The likely average expenditure on Chicken Licken products per visit is R26.7, the median and mode is R28.

Table 5.8: Cross-tabulations between expenditure per visit and Age

			Age Group			Total
Expenditure	Less than 25 yrs.	26-33 yrs	34-41 yrs	42-49 yrs	50 and above	
R12-22	3	8	12	5	1	29
R23-33	5	19	26	16	2	68
R34-54	1		4	4	2	11
R55 – 75		4	3	2	3	12
Total	9	31	45	27	8	120

5.2.4 Expenditure per Visit and Gender

Table 5.9 shows the allocation of expenditure per visit on the basis of gender. It shows that 53 male respondents are willing to spend between R12-33, and 11 are willing to spend over R34 per visit; 44 female respondents are willing to spend between R12-33, while 12 are willing to spend over R34 per visit. Likely expenditure per visit seems to be independent of the respondents' gender. The chi-square test indicates that the association between gender and the likely expenditure per visit is statistically not significant at the 0.05 level (Chi-square = 1.994, df = 3, p = 0.574).

Table 5.9: Cross-tabulations between Expenditure per visit and Gender

Gender			Expenditure		Total
	R12-22	R23-33	R34-54	R55 and above	
Male	13	40	5	6	64
Female	16	28	6	6	56
Total	29	68	11	12	120

5.2.5 Expenditure per Visit and Area of residence

Table 5.10 shows that of the respondents residing in Richmond (93), 59.12 per cent are willing to spend between R23-33 per visit, while of those residing outside Richmond (27), 48.15 per cent are willing to spend between R23-33. The chi-square test indicated that a possible association between area of residence and expenditure per visit is statistically significant (Chi-square = 17.698, df = 3, p = 0.001).

Table 5.10: Cross-tabulation between Area of Residence and Expenditure per visit

	Expenditure				Total
Area	R12-22	R23-33	R34-54	R55 and above	
Richmond	27(29.03%)	55(59.12%)	4(4.32%)	7(7.53%)	93(100%)
Outside Richmond	2(7.4%)	13(48.15%)	7(25.93%)	5(18.52%)	27(100%)
Total	29	68	11	12	120

5.2.6 Monthly Income and Area of Residence

Tables 5.11 shows that of the respondents residing in Richmond, 60 have monthly incomes between R1001-3000, while of those residing outside Richmond 18 have monthly incomes between R1001-3000. The chi-square test revealed no significant association between area of residence and monthly income (Chi-square = 2.32, df = 2, p = 0.891).

Table 5.11: Cross-tabulations between Area of Residence and monthly Income

Area	Below R1000	Income (p.m.) R1001-3000	R3001 and above	Total
Richmond	12	60	21	93
Outside Richmond	4	18	5	27
Total	16	78	26	120

5.3.0 Association between Support of Chicken Licken Franchise and other variables

Respondents were asked 'If the Chicken Licken franchise was opened, would you support the Chicken Licken shop in Richmond?' Three options were provided 'I will always support' or 'I will seldom support' or 'I will sometimes support', from which the respondents had to choose one. *Table 5.12* indicates that 60 respondents would always support the franchise if opened, 41 would seldom support it, and 19 would sometimes support it.

Table 5.12 Support for the Franchise

Support	Frequency	Percent	Cumulative Percent
Always	60	50.0	50.0
Seldom	41	34.2	84.2
Sometimes	19	15.8	100.0
Total	120	100.0	

The willingness to support the franchise if opened is not conclusive unless it is associated with the willingness to spend money, interest in buying from the franchise and a liking for cooked chicken. Using the chi-square technique, the associations between Support of the Chicken Licken Franchise and respondents' monthly income, Support of the Chicken Licken Franchise and respondents' expenditure per visit, Support of the Chicken Licken franchise and respondents need for a Chicken Licken shop were tested. The results are presented below.

5.3.1 Association between Support of the Chicken Licken Franchise and Respondents monthly income

To investigate the association between willingness to support the Chicken Licken franchise, if opened, and respondents' monthly income, the null hypothesis can be formulated as: H_0 : The respondents' willingness to support the franchise if opened in Richmond is independent of the monthly income. Using the chi-square test, if the

calculated statistic is less than the chosen significance level (0.05), the null hypothesis above is rejected at the 5 per cent significance level. Results of the chi-square test show that the calculated p-value is greater than the chosen significance level (Chi-square = 6.044, $df = 4$, $p = 0.196$). Hence, the null hypothesis above is accepted and one can conclude that the respondents' willingness to support the franchise if opened in Richmond is seemingly independent of their monthly income, but there appears to be more support among the low and middle income group (*Table 5.13*).

Table 5. 13 : Cross tabulation between Support of a Franchise and Monthly Income

	Income (p.m.)			Total
Support	R500-1000	R1001-3000	R3001-5000	
Always	6	41	13	60
Seldom	5	29	7	41
Sometimes	5	8	6	19
Total	16	78	26	120

5.3.2. Association between Support of the Chicken Licken Franchise and the Amounts Respondents spend in Restaurants

Respondents were asked "How much do you usually spend at a restaurant on each visit?" Five expenditure options were provided in the questionnaire: R12-22, R23-33, R34-54 and over R55. Frequency statistics show that 29 respondents are usually spending between R12-22 per visit, 68 are spending between R23-33, 11 are spending between R34-54, while 12 are spending over R55 on each visit (results in *Table 5.14*). The chi-square shows that the p-value is less than the 5 per cent significance level (Chi-square = 20.305, $df = 6$, $p = 0.002$). Therefore the null hypothesis of no association was rejected and a conclusion could be made that respondents' support of the chicken franchise is significantly associated with their expenditure in restaurants.

Table 5.14: Cross-tabulation Between Support of a Franchise and Amount Spend in Restaurants

Support		Expenditure			Total
	R12-22	R23-33	R34-54	R55 and above	
Always	12	38	8	2	60
Seldom	15	19	3	4	41
Sometimes	2	11		6	19
Total	29	68	11	12	120

5.3.3 Association between Support of the Chicken Licken Franchise and the need for a Chicken Licken shop

When respondents were asked “In your view, is there a need for a Chicken Licken shop in Richmond”? 105 answered “Yes” and 15 answered “No” to the question. The chi-square test results for association between willingness to support the Chicken Licken franchise and response to the question regarding the need for the shop revealed a statistically significant association between the two variables (chi-square = 64.556, df = 2, p = 0.000).

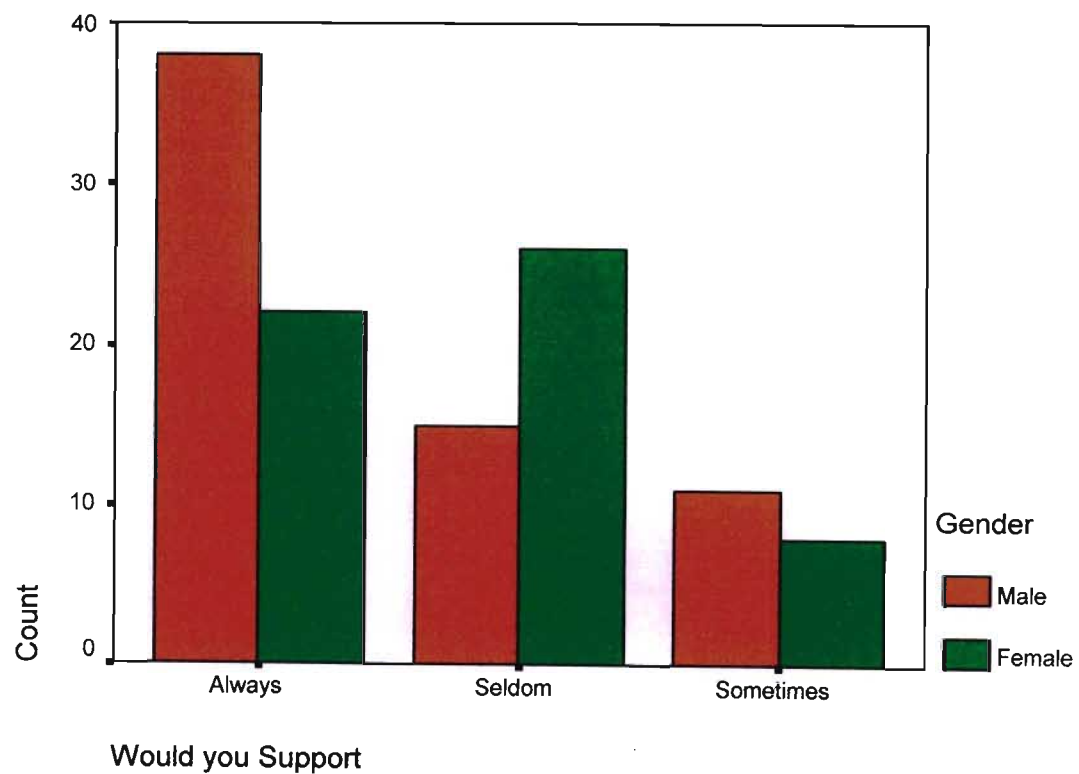
Table 5.15: Cross-tabulation between Support of the Chicken Licken Franchise and the need for a Chicken Licken shop.

	The Need for a Shop		Total
Support	Yes	No	
Always	59	1	60
Seldom	40	1	41
Sometimes	6	13	19
Total	105	15	120

5.3.4 Association between Support of the Chicken Licken Franchise and Gender

Figure 5.2 shows the cluster graph for the respondents' willingness to support the Chicken Licken Franchise if established; and gender. Of the respondents who will always support the new franchise (60) 38 are males. Of those who will seldom support the new franchise (41) 26 are females, 11 and 8 males and females, respectively, will sometimes support the new franchise. The chi-square test indicates that there seems to be a statistical dependence between willingness to support the new franchise, if established, and gender (chi-square = 7.190, df = 2, p = 0.027). More males appear willing to support the franchise than females.

Figure 5.2: Respondents' willingness to support the Chicken Licken franchise if established; and gender



5.4.0 Correlation Analyses: Strength of Association between Support of Chicken Licken Franchise and other variables

The chi-square approach does not measure the strength or direction of the association between variables. The measurement of the strength of associations requires the use of the correlation technique. Heiman (2001:251) argues that the correlation approach can, among other uses, be used to discover new relationships. For this study, correlation coefficients were calculated for the dependent variable 'support of Chicken Licken shop' and the independent variables, the respondents' income per month, expenditure per visit, like to eat chicken, need for a shop and interest in buying from the shop.

5.4.1 Support of Chicken Licken franchise and Respondents' monthly Income

The Pearson's Correlation analysis (*in Table 5.16*) shows that there is a positive relationship between willingness to support a chicken licken franchise and the respondents' income. However, the relationship is found to be relatively weak ($r = 0.050$) and not statistically significant.

5.4.2 Support of Chicken Licken franchise and expenditure per visit

The correlation results (*in Table 5.16*) indicate a statistically significant correlation between support of a Chicken Licken shop and expenditure per visit ($r = 0.16$ at the level 0.05, one-tailed test). Since the correlation coefficient is positive, one could argue that, as expenditure per visit increases, support for the franchise will also increase, other things assuming to remain constant.

Table 5.16: Pearson Correlation Results for Selected variables

		Would you Support	Income	Expenditure per Visit	Like Eating Chicken?	A Need of a Shop	Interest in Buying
Would you Support	r	1					
	Sig. (1-tailed)	.					
Income Group (p.m.)	r	.050	1				
	Sig. (1-tailed)	.294	.				
How much Spend	r	.160*	.075	1			
	Sig. (1-tailed)	.041	.208	.			
Like Eating Chicken?	r	.396**	.019	.375**	1		
	Sig. (1-tailed)	.000	.418	.000	.		
A Need of a Shop	r	.586**	.118	.332**	.606**	1	
	Sig. (1-tailed)	.000	.099	.000	.000	.	.000
Interest in Buying	r	.795**	-.004	.246**	.598**	.788**	1
	Sig. (1-tailed)	.000	.481	.003	.000	.000	.
	N	120	120	120	120	120	120

* Correlation is significant at the 0.05 level (1-tailed).

** Correlation is significant at the 0.01 level (1-tailed).

5.4.3 Support of Chicken Licken franchise and Respondents' Like of eating chicken

The correlation results in *Table 5.16* show a statistically significant and positive association between support of a Chicken Licken franchise and the respondents' preference for eating chicken ($r = 0.396$ at the level 0.01).

5.4.4 Support of Chicken Licken franchise and Respondents need for a new Shop

The correlation results (in *Table 5.16*) show a statistically significant relationship between support of a Chicken Licken franchise and the respondents' need for a new shop in Richmond ($r = 0.586$ at the level 0.01).

5.4.5 Support of Chicken Licken franchise and Respondents' interest in buying from the shop

The correlation results in *Table 5.16* indicate a statistically significant and positive correlation between support of a Chicken Licken franchise and the respondents' interest in buying from the shop ($r = 0.795$ at the level 0.01).

5.5.0 REGRESSION ANALYSIS

Although there are several other factors that may influence the need for a new Chicken Licken shop in an area the, researcher attempted to use the data available to fit a regression model. The objective of the model is to test the null hypothesis H_0 : There is no real need for a Chicken Licken shop in Richmond. Three independent variables were hypothesized to influence the need for a new eating-place in Richmond. The selected independent variables are: monthly income, expenditure per visit and interest in buying.

Therefore the regression model to be fitted can be presented as follows:

Need for a shop = $B_0 + B_1(\text{monthly income}) + B_2(\text{expenditure per visit}) + B_3(\text{interest in buying}) + \text{Error term}$

Where : B_0 is a constant,

B_1 , B_2 , and B_3 are coefficients.

It is assumed that the coefficients of each variable are positive.

5.5.1 Coefficient of Determination

Table 5.17 shows that the selected model has an R square = 0.654 and an adjusted R-square = 0.645. The R-square indicates that about 65 per cent of the variation of the dependent variable is explained by the independent variables in the model. The table also shows a multiple correlation coefficient R = 0.809, indicating that there is a positive and stronger relationship between the observed and predicted values of the dependent variable. With the R-square =0.654, adjusted R-square = 0.645, and R = 0.809, one could conclude that the model does reasonably fit the data.

Table 5.17 Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.809	0.654	0.645	0.19780

Predictors: (Constant), Income per month, Interest in Buying, Expenditure per visit

5.5.2 Adequacy of the model

To test the adequacy of the model, SPSS’s analysis of variances (ANOVA) was used. The adequacy of the model is tested by formulating a null hypothesis H0: At least one or all the coefficients in the model equal to zero. The objective can be achieved by using F-statistics. If the calculated F-statistics are greater than the respective F-table value at a specified level of significance and degree of freedom, the null hypothesis is rejected. Table 5.18 shows that the calculated F-statistics (73.154) is greater than the F-table value (0.000), with the degrees of freedom (3,116), Therefore the null hypothesis that each of the coefficients is equal to zero is rejected. A conclusion is made that, on the basis of the adjusted R square and the F-statistics, the model is adequate for predicting the need for a Chicken Licken outlet in Richmond.

The estimated regression model explains about 65 per cent (adjusted R square 0.645) of the total variation in notional demand for the firm. A multicollinearity diagnostic was conducted to test for multicollinearity. The variance inflation factor (VIF) of the predictors was 1.1, 1.0, and 1.0, respectively. Normally, if the VIF is greater than 4, then one suspects that multicollinearity might be a problem (Thomas, 1992). Overall, therefore, the regression model was reasonably good.

Table 5.18: ANOVA

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	8.586	3	2.862	73.154	0.000
	Residual	4.539	116	0.039		
	Total	13.125	119			

Predictors: (Constant), Income per month, Interest in Buying, Expenditure per visit

Dependent Variable: Need of a Shop

5.5.3 Test of Coefficients

Usually the F-test and t-test will give the same result if the independent variable is one and it is not the case when the model has two or more independent variables. This observation makes it necessary to carry out a t-test for each of the independent variables included in the model. Likewise, it is hypothesised that $H_0: B_1 = 0$, $H_0: B_2 = 0$, or $H_0: B_3 = 0$, H_0 is rejected if t-statistic is greater than t-table value. Table 5.19 below shows that t-statistics for $B_1 = 2.031$, $B_2 = 2.436$, and $B_3 = 13.403$. As the t-statistic value is greater than the cut-off t-table values 0.045, 0.016, and 0.000, respectively, H_0 is rejected. That is, all the three independent variables are found to be significant predictors of the need for

a Chicken Licken shop in the Richmond area (at the 5 per cent level of significance). With the finding in the subsections above, the null hypothesis, ‘There is no real need for a Chicken Licken shop in Richmond’, could be rejected. A conclusion is drawn that there is a real need for a Chicken Licken shop in Richmond. The overall regression result of a need for a Chicken Licken shop is summarised as:

$$N = 0.371 + 0.111(\text{Income})_{t = 2.031} + 0.138(\text{Expenditure})_{t = 2.436} + 0.755 (\text{Interest})_{t = 13.403}$$

Where N = Need for a Chicken Licken shop in Richmond

Table 5.19: Test of the Coefficients

		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
Model		B	Std. Error	Beta		
	(Constant)	0.371	0.092		4.049	.000
	Expenditure	5.325E-02	0.022	0.138	2.436	.016
	Interest in Buying	0.227	0.017	0.755	13.403	.000
	Income p.m.	6.281E-02	0.031	0.111	2.031	0.045

Dependent Variable: Need for a Chicken Licken shop

5.6. CONCLUSION

Chapter 5 has covered four main issues. Firstly, frequency statistics were computed and found that: the sample was about equally distributed in term of gender, it consisted of 53.5 per cent male and 46.7 per cent female respondents. Of the respondents, 95 per cent were employed and 92 per cent were at least 26 years of age. One could conclude that the sample mainly consisted of adults who were earning some sort of income. Moreover it was found that 110 respondents were aware of the existence of Chicken Licken stores and 104 intended to buy from a Chicken Licken franchise if established in Richmond.

Secondly, the frequency statistics were followed by the examination of whether there is any association between the respondents' support for the Chicken Licken shop and the amount respondents usually spend in restaurants, also with the need for a Chicken Licken shop. Results indicated that there is some sort of association between the respondents' support for a Chicken Licken shop and the amount respondents spend in restaurants (Chi-square = 20.304, $df = 6$, $p = 0.002$). Also there is a statistical association between the respondents' support of a Chicken Licken shop and the need for a new shop. The chi-square results, to some extent, supports the need for establishing a new Chicken Licken shop in the Richmond area.

Thirdly, the correlation analysis was carried out to establish the strength of relationships between the respondents' support of a Chicken Licken shop and their preference for eating chicken the respondents' support of a Chicken Licken shop and the need for that shop in Richmond area the respondents' support of a Chicken Licken shop and their interest in buying from that shop.

A positive and significant correlation was found between the respondents' support of a Chicken Licken store and their preference for eating chicken ($r = 0.396$). A statistically significant and positive relationship was found between the respondents' support of a Chicken Licken store and the need for that shop in the Richmond area ($r = 0.586$). Also, a significant and positive association was found between the respondents' support of a

Chicken Licken store and their interest in buying from that shop (0.795). All the correlation results above reinforce the need for a chicken Licken Store in Richmond.

In the last part of the chapter a regression model was fitted. It indicated that the need for a Chicken Licken Shop = f (Expenditure per visit, Interest in buying from the shop, Income). The regression model, chi-square tests and correlation results indicate that there is a real need for a Chicken Licken Store in Richmond.

DIVESTING AND INVESTING AS STRATEGIC OPTIONS

6.0. INTRODUCTION

This chapter deals with the divestiture and investment as a strategic entrepreneurial decision in a small business environment. In both cases, a proper cost-benefit analysis should be undertaken, or otherwise the financial losses could be very heavy. An investment that is not properly evaluated may fail to generate expected returns, whilst a delayed or poorly planned divestiture could fail even to recoup the initial capital invested in the business. Indeed, entrepreneurs may experience strains and stresses when divestiture becomes the only strategic option, because they have personal ties with their businesses. It is still important, however, that reasoning takes precedence over emotions, as divesting poorly performing businesses is one of the best ways of freeing unproductive assets for redeployment, (Thompson and Strickland,1998:26). The strategic challenge facing entrepreneurs finding themselves in a divesting situation is to steer those resources out of low productivity areas into high opportunity areas and hence the need for strategic analysis.

Similarly, commitment of any funds in any kind of investment, including new venture via a start-up, an acquisition, or otherwise, should result from thorough investigations assessing properly whether that investment is a better option amongst other possible options and whether it will yield sustainable profits.

In chapter 6 analyses underpinning the divesture and investment decisions are carried out. Suitable frameworks that guide the selection of appropriate strategies are used in order for the most strategic positioning.

Profits from K.H. Foods Services CC for the period 1999 to 2003 were used (*Table 6.1*), in order to compare these with the interest that the initial capital could have earned if it was invested in a money market in 1999 (as shown in *Table 6.2*). These comparisons were further done to determine the present value of the initial capital of R635 000 invested in the business K.H. Foods Services CC, in March 1998, and to assess whether there was an *opportunity loss*. The profits were used to benchmark the performance of

K.H. Foods Services CC with the industry ratio averages, as shown in *Table 6.3*. The Strategy Selection Matrix, *Figure 6.1*, was then used to guide the proper selection of a suitable strategy, given the situation of K.H. Food Services CC at that time.

As funds from the divestiture were to be re-invested, another investment opportunity was to be investigated. A lump-sum investment from Old Mutual Insurance Company shown in *Table 6.4*, a money market investment from a financial institution in *table 6.5*, and profit projections for a new venture through franchising in, *Table 6.6* were investment options to be examined. The future value and the payback methods were used to compare the investments, in order to be able to select the investment that offers a higher future value and a shorter payback period.

In order to position the new venture for competitive advantage, market analyses were undertaken, using Porter's Five Forces Model, to assess the level of competition in the industry. The Life Cycle/Portfolio Matrix was then used as a framework for guiding the selection of suitable strategies, given the competitive position of the new business and the stage of the industry. As Chicken Licken was a favoured franchise, its competitive position in the food industry was examined, using the frameworks mentioned. The resources underpinning the chosen strategies were to be assessed for suitability and the Resource/Competences Matrix was used for this purpose.

6.1. DIVESTITURE

Sub-par performances by some businesses may occur, thereby raising questions of whether to keep those businesses or to divest them. If the weaknesses of the business are a major obstruction to success in the industry and the costs of overcoming them are unaffordable, or are not justified by cost-benefit analysis, then eliminating the business must be considered and divestiture offers the best possibility for recouping the firm's investment (Pierce and Robinson, 200: 316). Thompson and Strickland (1996: 232) state that the divestiture needs to be done as fast as practical if the business can still realize its market value, unless time is needed to get it in a better condition to sell.

In this case study, the business under divestiture was K.H. Foods Services CC, trading as Steers Longmarket. This business was established by the present author in Pietermaritzburg, in March 1998, and operated as a close corporation, K.H. Foods Services CC. It was under a Steers franchise.

When this business was established, its viability study was undertaken by a private consulting firm appointed by the franchisor. Projected sales figures, according to their studies were to be in the region of R3.6 million per annum. However, these figures were not attained, in spite of aggressive national and local marketing efforts.

Although the business showed some improvements in turnover these did not match the budgeted sales and expected returns. Other factors that contributed to the poor performance were:

- McDonalds opened a branch in Pietermaritzburg in 1999 and they had a far-reaching competitive advantage in terms of price and ambience. K.H. Foods Services CC was relatively disadvantaged, as the premises were leased from a private owner who was unable to improve them, and the business, being a franchise, had everything, including pricing, controlled nationally by the head office.
- Location became a disadvantage. Although ideally situated, opposite the bus and taxi rank, it only attracted commuters who mainly made individual purchases. This, coupled with the fact that 90% of the clients were made up of the population group that currently has a low purchasing power, influenced low customer expenditure. As a result, although the number of clients was growing, its influence on turnover was minimal.
- Yearly increase in turnover did not warrant the yearly increase on fixed costs especially rental, (please refer to *Appendix 1 on page 108*).

Endemic to all small businesses is financial constraint. This was the case with the business in question and the strategies sought were solely those that required limited additional resources.

6.1.1. Divestiture Analysis

The decision to divest the business was taken after the financial situation of the business was reviewed and compared with a possible investment option that could have been made during that year, namely an investment in the money market, as shown in *Tables 6.1 and 6.2*. A high opportunity loss was identified, which justified a divestiture. A Strategy Selection Matrix was used as a guide to confirm the divestiture strategy, selected on the basis of the variables used in the matrix, as shown in *Figure 6.1*. Common industry ratios were further used to benchmark the performance of the business. These also revealed that the business was under-performing and thus justified divestiture (see *Table 6.3*)

Table 6.1

K.H. Food Services CC Five-year Performance

Year of Trading	Capital Invested (R)	Turnover	Cost of Sales (R)	Expenses (R)	Expense % to Turnover	Net Profit (R)	Net Profit %	ROI
1999	635 000	924 810	(438 648)	(537 639)	58.1%	(51 278)	(5.5%)	(8.7%)
2000		1193 461	(537 537)	(640 725)	53.7%	15 692	1.3%	2.5%
2001		1035 097	(460 206)	(548 607)	53%	26 284	2.5%	4.1%
2002		1191 815	(559 167)	(603 980)	50.7%	28 668	2.4%	4.5%
2003		1211 795	(564 426)	(618 021)	51%	32 348	2.7%	5.1%

According to *Table 6.1*, capital gain after five years from the above investment was equal to $(32348+28668+26284+15692-51278)$ **R51714** and this is equivalent to an average Return on Investment of **1.6%**, which is far below the industry norm shown in *Table 6.3*.

Table 6.2

The present value of R635 000 with Money Market Interest at 14%

Year Ending	Initial Capital (R)	Cash Flows (R)	Capital Growth (R)
1999	635 000	88 900	723 900
2000		101 346	825 246
2001		115 534	940 780
2002		131 709	1072 489
2003		150 149	1222 638

If the same initial capital of R635000 had been invested in a financial institution without any risk, the future value of the above investment project would have been **R1222638**, and total interest earned would amount to $(88900+101346)+115534+131709+150149$ **R587638** as shown in Table 6.2.

Opportunity Loss

According to Redelinghuis, Julyan and Benade, (1997: 132), the opportunity loss is the profit which is foregone if the best alternative in respect of each event is not selected. This represents the difference between the highest profit that can be earned from a particular event and the profit that is actually earned.

At a money market rate of 14% for an investment in 1998, the total interest earned from that investment after five years, according to Table 6.2, could have been **R587638** or **18.5%** return on investment and the present value of **R1222638**. As the money was not invested in this project, but in a business venture that only earned **R51714** profit in five years, the opportunity loss is $(587638-51714)$ **R535924**. Clearly, a better return would have been obtained if the capital had been invested in a financial institution instead of taking up a Steers franchise. However, going into business is a high risky activity and

one should be prepared to take these risks and divest at the right time for high profit opportunities.

Table 6.3

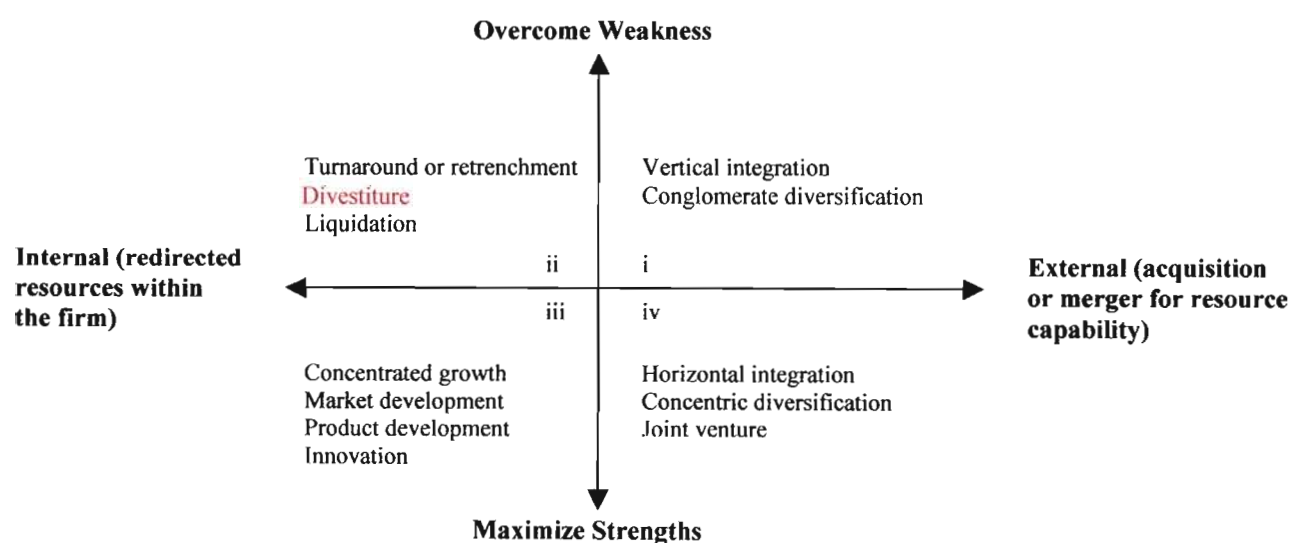
Benchmarking with Industry Norms

	Expenses on Turnover	Profit margin (%)	Return on Investment
Industry Norm	35%	15%	30%
K.H. Foods Services	53.3%	3.3%	1.6%

Source: Chicken Licken Head Office

Table 6.3 shows ratios that other similar businesses in the industry achieved in recent years. This benchmarking reveals that the performance of the specific Steers franchise business was performing below even the industry norms, clearly indicating a need for strategic review. The Grand Strategy Selection Matrix is used to determine a suitable strategy for this business, as shown in Figure 6.1.

Figure 6.1. Grand Strategy Selection Matrix



Source: (Pierce & Robinson, 2000: 315)

According to Pierce and Robinson (2000: 315), the *Grand Strategy Selection Matrix* can be used as a valuable guide to select a suitable grand strategy. The selection process is based on two variables. The first one is the principal purpose of the strategy, which could be the deployment of the resources to overcome weaknesses or to maximise strengths. The second variable is a choice between deploying internal resources or external resources. In the case of K.H. Foods Services CC, the choice was to use internal resources to overcome weaknesses, in which case the suitable strategy was a divestiture, as shown in quadrant ii of the matrix. The reason for selecting the divestiture is that the retrenchment strategy was implemented, when the number of staff was cut down, indicated by the improvement of expenses over turnover from 58.1% in 1999 to 51% in 2003, as shown in *Table 6.1*. However, this failed to accomplish a real turnaround. The divestiture strategy allows for the business to be sold as an attractive going concern, allowing for a chance of finding a buyer willing to pay a price above the value of the assets.

6.1.2. Summary of the Divestiture Analysis

The outcome of the analysis using the results from K.H. Food Services CC income statements for the five-year period of trading indicates that the business is indeed under-performing and that, although there has been small improvements in turnover and profitability over the period, these do not justify continuance of the business.

The opportunity loss of R535 924 and the failure of the business to meet or exceed industry norms, further confirm the above. All other available strategic alternatives had been exhausted, including the *concentration strategy* that was adopted when marketing efforts were increased and that resulted in a slight improvement of turnover, as shown in *Table 6.1*, and the turnaround strategy that was implemented through costs cutting, as is indicated by a decline in expenses to turnover from 58% in 1998 down to 51% in 2002, as *Table 6.1* further indicates.

In view of these analyses and the strategic direction indicated by the Strategy Selection Matrix, it was felt that the business justified divestiture.

The business K.H. Foods Services CC was thus sold to a buyer who converted it into a business suited to the area and the initial capital invested in the business, namely R635 000 was recouped and a decision was made that these funds should be re-invested in a new venture and that proper investigations needed to be done.

6.2. Investment

According to Mott (1993:1), important in an investment decision is the awareness of the factors influencing the profitability of that investment. This would help entrepreneurs to channel their resources to more profitable investments. It is also important to weigh investment options against other available options in order to ensure that a high profit yielding option is eventually selected. Longenecker, Moore and Petty (2003:120) point out that for an opportunity to qualify as a good investment, it is the market that must be the ultimate arbiter. This means that there are important factors in the investment decision that need not be overlooked and some of these are listed below.

- A clearly defined market must exist for the product or service and the timing must be right.
- The proposed business must be able to achieve a sustainable competitive advantage, hence the need for appropriate positioning.
- The economics of the venture must be rewarding in terms of profit margins and return on investment.
- A fit must exist between the entrepreneur and the opportunity, that is to say that the opportunity must be captured by somebody with appropriate skills and experience and it must be someone who has access to critical resources that are necessary for the venture to grow and prosper.
- There must be no fatal flaw in the venture and hence the importance of proper investigations, ensuring that every weakness is identified and that successful strategies are implemented to overcome those identified.

6.2.1. Investment assessment

The feasibility study for the assessing the new investment of R635 000 will include a market survey for the purpose of testing the response of the primary decision-makers.

Three alternative investment opportunities will be evaluated, namely a lump-sum insurance investment from Old Mutual, a money deposit and a new venture through franchising. The payback method will be used in investment options to determine the period it will take to recover the initial investment. Competitive analysis will be done and the industry condition will be investigated in order to ensure appropriate entry strategies that will give the venture competitive advantage. Chicken Licken was the preferred franchise. The investment options that were examined:

Table 6.4

Old Mutual Lump-sum Investment

Year Ending	Capital Invested (R)	Cash Flows (R)	Capital Growth (R)
2004	635 000	63 466	698 466
2005		69 808	768 274
2006		76 786	845 060
2007		84 460	929 520
2008		92 902	1022 422

For the above investment, please see also *Appendix 3* on page 110. According to *Table 6.4*, this investment will earn a profit of $(1022422-635000)$ **R387422** in 5 years time, or an average of **12.2%** return on investment per annum.

Table 6.5
The Future value of R635000 with Money Market interest at 11.3%

Year Ending	Initial Capital	Cash Flows	Capital Growth
2004	635 000	71755	706 755
2005		79 863	786 618
2006		88 888	875 506
2007		98 932	974 438
2008		110 112	1084 550

The current money market rate quoted by banks is 11.3%, Assuming that this would be an average quoted rate for the five-year period, the investment would have earned **R449550**, as shown in Table 6.5, or a **14.2%** return on investment, with a future value of **R1084550**

Table 6.6
Chicken Licken Richmond Five-year Profit projections

Year of Trading	Capital Invested	Turnover	Cost of Sales	Expenses	Expense % to Turnover	Net Profit	Net Profit %	ROI
2004	635000	1134810	582810	427639	37.7%	124361	11%	19.6%
2005		1393461	710665	487711	35%	195085	14%%	30.7%
2006		1365097	688897	473688	34.6%	202512	14.8%	31.9%
2007		1491815	760826	514676	34.4%	216313	14.4%	34.1%
2008		1511795	755898	517034	34.2%	238863	15.8%	37.6%

The expected total profits of the Chicken Licken store in Richmond, according to the projections in Table 6.6, are (124361+195085+202512+216313+238863) **R977134**, or an average of **30.8%** return on investment.

Table 6.7**The Payback Period**

Year	Insurance Annual Cash flow	Insurance Cumulative Cash flow	Money Market Annual cash flow	Money Market Cumulative Cash flow	Chicken Licken Annual Cash flow	Chicken Licken Cumulative Cash flow
0	-635000	-635000	-635000	-635000	-635000	-635000
1	+63466	-571534	+71755	-563245	+124361	-510639
2	+69808	-501726	+79863	-483382	+195085	-315554
3	+76786	-424940	+88888	-394494	+202512	-113042
4	+84460	-340480	+98932	-295562	+216313	+103271
5	+92902	-247578	+110112	-185450	+238863	+342134

The payback method measures the number of years it is expected to take to recover the cost of the initial investment. Despite its shortcomings, it is a method that is often used by large and sophisticated companies, especially when making small investment decisions (Ross et al, 1996: 186). According to Mott (1993:17), 92% of the UK firms use the payback and it is regarded as a primary method of evaluation. In this study it was chosen because of its simplicity and user-friendliness. It is thus suitable for use in a small business environment.

Applying the payback method to this investment decision, as shown in *Table 6.7*, it was found that the franchise business envisaged in Richmond is the only option with a quicker payback period of 3,5 years.

Table 6.8

Comparison of the Three Investment Options

Type of Investment	Investment	Total Yield	Total Future Value	Return on Investment
Insurance	635000	387422	1022422	12.2%
Money Market	635000	449550	1084550	14.2%
Chicken Licken	635000	977134	1612134	30.8%

6.2.2. Summary of the Investment Decision

According to the summary in Table 6.8, one can conclude that the Chicken Licken project appears to be a worthwhile investment. Its future value, profits and the return on investment are much higher than those of other investments. It is the investment with the shortest payback period.

This investment is further supported by the results of the consumer survey undertaken in Richmond, which indicated overwhelming support from that market.

6.3. Entry Strategies for Competitive Advantage

According to Johnson and Scholes (1997: 107), the idea underpinning strategy is the search for an opportunity to identify bases of advantage. There is therefore a need for the business to identify factors that will influence its capability of positioning itself to such an advantage.

Having tested the market for support and assessed the viability of the venture by analysing and evaluating various investment options, the key remaining factor is identifying competition. According to Pearce and Robinson (2000: 85), the essence of strategy is coping with competition. This exercise will not be completed until positioning strategies for securing competitive advantage are identified.

In this case study, *Porters Five Forces Model* will be used as it allows for an in-depth analysis of the competitive environment in the industry. The *Life Cycle/Portfolio Matrix* will be applied in order to determine a suitable strategic positioning for Chicken Licken, based on its competitive strength in the food industry, as well as on the stage of the industry. In order for the strategy to be viable, suitable resources are needed. Accordingly, the *Resource/Competencies Matrix* will be used to identify critical resources required to support the selected strategies. In the following section these frameworks are applied to the Chicken Licken case study in order to determine the strategies suitable for this business.

6.3.1. Porters Five Forces and Chicken Licken in Richmond

This model is based on the insight that the state of competition in an industry is a composite of five forces, namely *threat of new entrants*, *powerful suppliers*, *powerful buyers*, *substitutes and industry competitors*, and certain characteristics are critical to the strength of each force. The model assumes that competition in an industry can be evaluated by assessing these forces. These will be briefly discussed in relation to the Chicken Licken opportunity in Richmond.

- **Threat of new entrants**

According to a Markinor survey (Sunday Times, 29 September 2002: 29), Chicken Licken ranks second to Kentucky Fried Chicken in terms of weighted awareness, weighted trust/confidence and brand loyalty. Except for the weighted awareness, Kentucky holds a minimum lead of seven points in trust/confidence and three points in brand loyalty. The implication of this is that the business that will have an early entry in Richmond could have a chance of a leadership advantage. The size of the market of Richmond, however, may not be able to support more than one franchise, especially if one considers its set-up costs, of which sales from the current market size may not warrant, if shared. On the other hand, as violence has subsided in Richmond and the spirit of the government is the promotion of entrepreneurship and empowerment of disadvantaged groups through franchising, this market is still open for new competitors to enter.

The threat of new entrants is therefore moderate now with a potential to become stronger if the market in Richmond becomes really attractive to lure other major players of the industry. There seem to be no real barriers to entry except for set-up costs.

- **Powerful Buyers**

According to Pierce and Robinson (2000:90), the impact of powerful buyers could influence low prices and higher quality or service, all at the expense of industry profits. These writers state that customers are more price sensitive if the products they purchase are undifferentiated. In the case of Chicken Licken, the brand is differentiated and there are currently no other similar branded products on this regional market. The high support revealed by the consumer survey conducted in Richmond showed that these consumers are already aware of the Chicken Licken brand.

In view of the above, one can conclude that this is a moderate to strong force. Consumers can still patronise other food outlets in Richmond. However Chicken Licken has a strategic advantage of a branded product. This force has still a potential to be strong if big players like Kentucky decide to enter the Richmond market.

- **Powerful Suppliers**

Chicken Licken commands a network of 250 outlets, giving it a strong buying power. As Chicken Licken Richmond will be part of the group, the business will enjoy this strategic advantage. Suppliers have a stronger bargaining power if the products they supply are unique or differentiated. Chicken Licken's main product is chicken, which makes up more than 90% of their purchases. Of main concern, would be quality, reliable delivery and price, but there are other suppliers of chicken on the market and, with the strengthening of the brand, even imported chicken could be an alternative. Sellers herefore have no real bargaining power.

- **Substitute Products**

Buyers' propensity to substitutes is subject to their availability, their quality, their performance and their price relative to industry products. In the case of Chicken Licken Richmond, substitutes in the form of traditional foods from local restaurants and eating at home will be only a moderate threat, because consumer surveys have shown that Chicken Licken is a strong brand.

• **Competitive Rivalry**

This force relates to competition between existing players in the industry. These are usually the strongest threat, yet in Richmond the industry’s strong players have not yet entered the market, because of the past history of the town and perhaps because of the current size of the market. There are local places that sell food and which are privately owned. According to the results of the market survey the most popular one is Fatima’s Take Away. It is felt that, being a national brand, Chicken Licken will have a strategic advantage over the local food places such as Fatima’s Take Away.

6.3.1.1. Overall Summary of the Five Forces

It is evident that the market in Richmond presents an opportunity for Chicken Licken. The decline in violence, coupled with the minimum wage legislation for domestic and farm workers, has further enhanced the prospects of this market. The results of the market survey confirmed the existence of the middle-income group in Richmond that is the Chicken Licken target market.

The five forces model reveals that the overall food industry in Richmond is moderately competitive, with a potential of strong competition should major players decide to enter the market, because at this stage there are no barriers to entry.

The overall food industry has consolidated, with clear leaders of the market, as the Markinor survey has indicated. It is therefore recommended that Chicken Licken should hasten its entry into the Richmond market in order to secure a first mover advantage ahead of competition. See also *Figure 6.2* below.

Figure 6.2
Summary of Porter’s Five Forces

	Porter’s Five Forces	High	Moderate	Low
1	Threats of New entrants		X	
2	Powerful Buyers		X	
3	Powerful Suppliers			X
4	Substitute Products			X
5	Competitive rivalry		X	

Figure 6.2 summarises the current level of competition in Richmond, according to Porter’s Five Forces Analysis. The overall market is moderate, with a potential for becoming competitive if other players decide to enter the market. A strategic analysis for Chicken Licken:

Figure 6.3 The Life Cycle/Portfolio Matrix

The Life Cycle/Portfolio Matrix				
Competitive Strength	Stage of Industry Maturity			
	Embryonic	Growth	Mature	Ageing
Dominant				
Strong			Strategic Position for Chicken Licken	
Favourable				
Tenable				
Weak				

Source: (Johnson and Scholes, 1997:322)

According to Johnson and Scholes (1997: 322), the life cycle/portfolio matrix consists of two dimensions, the market situation and the competitive position. The former is described in four stages, that range from embryonic to ageing and the latter is described in five categories that range from weak to dominant. The purpose of this matrix is to establish the suitability of particular strategies, given the position of the business and the stage of the industry. What is crucial in this exercise is establishing where the business is currently positioned on the matrix and hence what strategies are likely to be most suitable.

According to the matrix in Figure 6.3, Chicken Licken is in a strong market position in a matured market, and suitable generic strategies in that position are *cost leadership*,

differentiation and *focus*. However, critical resources that will underpin the business’s ability to pursue these strategies need to be identified.

The Matrix in *Figure 6.4* is used to identify the resources and competencies that are available and critical for selected strategies. These are identified and ranked according to their status regarding competitive advantage.

Figure 6.4 Resource Matrix

Assessing Resource/Competency Suitability for a Market Strategy						
A Resources and Competences Underpinning Strategy	B Likely to create Cost Reduction	C Likely to Create Added value Per- ceived by Customers	D Status of Resource or Competence			
			Valued	Rare	Comple x	Tacit
Brand		✓			✓	
Secret Recipe		✓			✓	
Branch Network (250)	✓					✓
Technology	✓					✓
Research and Marketing		✓				✓

Adapted from: (Johnson and Scholes, 1997: 324)

The above matrix helps to identify key resources that are critical for competitive advantage. These resources will give an indication of whether the business is capable of supporting a particular positioning in its market. In the case of Chicken Licken, its resources support cost and differentiation strategies, as shown in *Figure 6.4*. This further confirms the choice according to the Life Cycle Portfolio Matrix in *Figure 6.3* above. The resource matrix helps to identify the status of the resource or capability in order to ascertain the viability of the strategy and, in the case of Chicken Licken, their brand and secret recipe are its strategically important resources.

According to the Resource Matrix, Chicken Licken’s resources and competences favour positioning for both cost leadership and differentiation. Positioning for differentiation

seems to be the most suitable of the two strategies, as competences favouring this positioning are stronger and not easy to imitate.

In view of the analysis done and the survey conducted regarding the investment of R635 000, which is the amount acquired from the divestiture, the business opportunity seems to be a worthwhile investment. One can further conclude that franchising is the appropriate mode to enter the Richmond market. Besides the generic advantages of franchising, the franchise, Chicken Licken, will give the new venture a strategic advantage through cost and differentiation, as revealed by the Life Cycle/Portfolio matrix and the Resource Matrix. This investment is therefore recommended.

6.4. SYNTHESIS

Through the literature review, this study looked at small businesses and their significance in most world economies. Special emphasis was paid to the South African situation. The aim was to establish how far the government's developmental initiatives have taken the sector thus far and what the remaining challenges were. The conclusion was that the government has taken great strides, but that there are areas that still need much attention. Studies indicate that there are still too many failures at the start-up phase and that more attention is needed to foster the entrepreneurship culture amongst the country's citizens.

The focus of this study was on investment and divestment as strategic options for small businesses. As a case study, these two situations were investigated. One business, K.H. Foods Services CC, operating as a Steers franchise, was divested, as it had shown poor financial results for five consecutive years. Funds obtained from the divestiture were to be re-invested in a new business venture, a Chicken Licken franchise in Richmond.

6.4.1. The divestiture.

Cost benefit analyses were undertaken to determine the profitability of the business relative to other opportunities that were available at the time that the investment was made.

- Firstly, the performance of the business in terms of ROI, profit margin and total expenditure to turnover ratios were compared to industry averages. All these ratios gave a clear indication that the business was under-performing, as they were below these averages.
- Secondly, the five years' profits from the business were compared to a financial institution's investment, at a money market rate at that time. The aim was to determine the future value of the initial investment, which was R635 000, in order to establish an *opportunity loss*. The analysis revealed a very high opportunity loss.

On the basis of these analyses, it was decided that divestment was the better strategic option for the business. The Strategy Selection Matrix further supported a divestiture decision. The business was then sold.

6.4.2. The Investment

As funds from the divestiture were to be re-invested, alternative investments were examined in order to select one that promised better profits, future value and return on investment.

- Quotations were obtained from Old Mutual for a lump-sum investment.
- Using the current money market rate, a financial institution investment was examined as a second option.
- A business opportunity in Richmond, through a Chicken Licken franchising was investigated as a third option. A market survey and profit projections were undertaken to test the viability and profitability of this business.

The future values of the three investment options were compared and these indicated that the Chicken Licken business was the better investment option in terms of profit, future value and return on investment.

A payback method was used to determine the period it would take for each investment to pay back the initial capital. This method favoured the new Chicken Licken venture, as its payback period was shorter than the other options.

The Chicken Licken franchise business was further supported by the consumer survey undertaken in the Richmond area. Statistical analyses indicated that there was an overwhelming support for this business in Richmond. The regression analysis indicated that there was a significant and positive support and need for a Chicken Licken franchise in Richmond.

Finally, on the basis of the overwhelming results of the survey and the cost benefit analysis, the investment of a Chicken Licken franchise in Richmond was considered a better investment option.

6.5. POLICY DIRECTIONS AND RECOMMENDATIONS

In spite of all evident efforts by the South African government, the country is still faced with tremendous challenges with regard to job creation, economic growth and participation by all citizens in the mainstream economy.

It is quite apparent that the objectives of the 1995 White Paper regarding these important issues have not yet been realised. Disparities still exist and unemployment is still a dire problem, indicating that the economy is still unable to supply enough jobs. Blacks are the main consumers of jobs and yet they still make a small number of job creators. Future job projections indicate that the situation may even get worse if these trends continue.

It is without doubt that the small business sector is a suitable vehicle for addressing these issues and that it can act as a catalyst for creating an entrepreneurial society in South Africa. The small capital that small businesses can utilise enables them to create jobs at a low cost. This factor further enhances their ability to promote ease of entry into the mainstream economy that is critical in the new South Africa. In order to be able to play their role effectively, more needs to be done to give small businesses a further boost.

Failure at start-up, lack of opportunity entrepreneurs, and start-up capital due to perception amongst some financial institutions, seem to be critical areas in the development of small businesses in South Africa. Studies show that entrepreneurial activity is nearly twice as high for men as for women in South Africa, indicating that gender inequalities are still prevailing in the country (S.A. Survey 2002-2003: 205). Indeed, new and creative strategies are urgently required in terms of policy and non-governmental support.

Perhaps it is also time for small business owners and managers to start thinking strategically. The perception needs to be changed that strategy is for big business. The law of nature prescribes that living organisms must be able to understand nature and adapt to the environment in order to survive. This applies to business, big or small, because a business that is not geared for continual improvement is destined for failure or extinction (Moyanga, 2003:40). According to Drucker (1980: 207), the 'bottle neck is at the head of the bottle'. No business is likely to be better if its top management has no vision or plans. With knowledge-based economies, the rate of change gets ever-faster. The managerial theorists see a firm as making a series of transitions from one stage to another, with these transitions being triggered by an external event. A failure to make that transition, in the event of the external shock, is seen as leading to a business failure (Storey, 1994: 91). As this places a greater test upon the skills and capabilities of the owner or manager of the business, skills assessment for suitability becomes critically important when entering business entrepreneurship.

Small business owners, because of the nature of their businesses, are required to be versatile. Skills assessments may enable identification of skills shortages, so that any weaknesses could be compensated by either undergoing more training, by utilising expert services or by using services of retired corporate business personnel.

There is no doubt that franchising offers an excellent means for an enterprise to succeed. However, it also needs to be stressed that franchising is not a guaranteed success and that it has its own unique challenges. It is also of the utmost importance that entrepreneurs wishing to enter the world of business by way of franchising do their own investigations. Franchisors, motivated to increase their franchisee network, may overlook some

important aspects in their viability studies. At the end, it is franchisees that stand to lose most if the franchise business fail.

It needs to be emphasized that going into business is in itself a risky undertaking, but if proper analyses and environmental assessment are properly conducted, these can be minimised, and venturing into business can still be an attractive investment option. It also needs to be remembered that divesture is a failed investment. If prevention is better than cure, then proper evaluations for every investment opportunity become very crucial.

It needs also to be noted that what underpins profit is consistent consumer support and hence the need for proper market surveys to ensure that the business will continuously enjoy this support. The testing of the market should be an ongoing process because there are competitors out there.

Similarly, when entering new markets, appropriate positioning strategies are key to sustainable profitability. The market needs to be assessed for attractiveness and the level of competition. The possibility exists that, in the industry, the market leaders may be so well entrenched and so well resourced that any attempt of entry into the market could be futile (Barrell, 1990: 34). Thus both the stage of the industry growth and the intensity of competition are critical for competitive advantage.

Resources and competences need to be assessed relative to positioning strategies. Effective strategies are driven by suitable resource competences. If your competitive position is weak or tenable, selecting niche markets could be a better option if competition is too fierce and when market players are likely to retaliate.

In this study the Life Cycle/Portfolio Matrix was used for identifying appropriate strategic positioning, based on factors of competition and industry growth stage. According to Pierce and Robinson (200:305), competitive advantage can be enhanced if managers take industry conditions into account when strategising. The all-encompassing Porter's Five Force Model was found to be a valuable tool in identifying the level of competition in the Richmond market for the new venture.

Johnson and Scholes (1997: 324-325) state that assessing the relationship between the selected generic strategy or strategies and the strategic capability of the business in terms of resources and competencies is a critical factor. The configuration of resources of the business is not only concerned with identification of resource requirements, but also with those competences that are needed to underpin particular strategies selected for competitive advantage. In this study the Resources/Competence Matrix was successfully used.

It needs to be underlined that in any entrepreneurship venture, cases of divestiture may occur. It is important that entrepreneurs do not despair. It is known that entrepreneurs regard their businesses with great pride, as it is their own creation. This should not be allowed to unnecessarily prolong divestiture decisions, to the detriment of the invested funds. A strategic response, on time, to a situation needing divestiture could enable the entrepreneur to sell the business and recover the initial capital invested. There are still attractive opportunities in the business environment and entrepreneurs need not be stuck with under-performing businesses.

Finally, economic theory tells us that the consumer reigns supreme. It is the sovereignty of the consumer that decides whether the business can survive and stay in operation or not. This is valid in marketing as well. Consequently, it is the consumers' and monetary expenditure that brings in sales and, ultimately, profit. The effectiveness of any strategy in the long term is bringing in sustainable profits, to the extent that consumers' interests are optimally looked after.

APPENDIX 1

Agreement pertaining to rent for K.H. Foods Services CC

5. **RENEWAL:**

- 5.1 The lessee shall have an option to renew this Lease for a further period of 5 years on the same terms and conditions as are contained in this lease (except for the renewal option), failing such an agreement on the rental for the period of renewal that it shall be referred to an arbitrator.
- 5.2 If the parties cannot agree on an arbitrator within the lapse of 10 days after the 30 day period, then the President for the time being of the Institute of Realtors of South Africa (KwaZulu Natal branch handling Pietermaritzburg region) shall be requested to make such an appointment.
- 5.3 The arbitrator's decision shall be final and binding on the parties.
- 5.4 In the event of the lessee desiring to exercise such option to renew, it shall do so by delivering to the lessor notice in writing at least 3 calendar months prior to the expiration of the initial period.
- 5.5 The aforesaid option to renew shall be conditional upon the lessee having duly and faithfully carried out and performed all the terms and conditions in this Lease.

6. **RENTAL :**

- 6.1 In addition to the rates and taxes payable in terms of Clause 8 hereunder, the rental payable by the lessee to the lessor in respect of the leased premises during the initial period shall be:-
- 6.1.1 1 May 1998 to 30 November 1998 - R7 700,00 (SEVEN THOUSAND SEVEN HUNDRED RAND) plus VAT of 14% in the sum of R1 078.00 per month; Further, the Lessee shall be liable for the pro-rata rates in the amount of R535.00 per month.
- 6.1.2 1 December 1998 to 30 November 1999 - R8 470.00 (EIGHT THOUSAND FOUR HUNDRED AND SEVENTY RAND) plus VAT of 14% in the sum of R1 185.80 per month; Further, the Lessee shall be liable for the pro-rata rates in the amount of R535.00 per month, or to be adjusted should the rates payable be increased.
- 6.1.3 1 December 1999 to 30 November 2000 - R9 317.00 (NINE THOUSAND THREE HUNDRED AND SEVENTEEN RAND) plus VAT of 14% in the sum of R1 304.38 per month; Further, the Lessee shall be liable for the pro-rata rates in the amount of R535.00 per month, or to be adjusted should the rates payable be increased.
- 6.1.4 1 December 2000 to 30 November 2001 - R10 248.70 (TEN THOUSAND TWO HUNDRED AND FORTY EIGHT RAND AND SEVENTY CENTS) plus VAT of 14% in the sum of R1 434.82 per month; Further, the Lessee shall be liable for the pro-rata rates in the amount of R535.00 per month, or to be adjusted should the rates payable be increased.

Handwritten signature and initials:
A. J.
M R

3.1.5 1 December 2001 to 30 November 2002 - R11 273.57 (ELEVEN THOUSAND TWO HUNDRED AND SEVENTY THREE RAND AND FIFTY SEVEN CENTS) plus VAT of 14% in the sum of R1 578.30 per month; Further, the Lessee shall be liable for the pro-rata rates in the amount of R535.00 per month, or to be adjusted should the rates payable be increased.

6.2 The rental payable by the lessee in accordance with this Agreement shall be subject to adjustment in the circumstances contemplated in clause 10. of this agreement. The lessee shall not be entitled to make any deductions from, or withhold any of said rental, for any reason whatsoever.

6.3 Rental shall be paid monthly in advance, without deductions or demand and free of bank exchange to the lessor at 294 Longmarket Street, Pietermaritzburg, or at such address as the lessor may from time to time in writing appoint.

7. **USE OF LEASED PREMISES :**

The lessee shall :

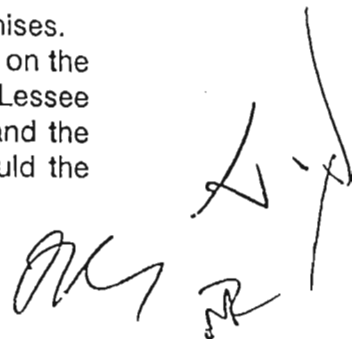
7.1 use the leased premises for the purpose of conducting a Fast Food business, and shall at all times during the term of this lease keep the leased premises open for its normal trading activities during normal business hours, and shall timeously apply for the grant and renewal of any necessary trading licences. The premises shall not be used for any other purpose than for that which trading licence was issued. Under no circumstances may the premises be used for the sale of any vegetables or green groceries, excepting salads and other prepared foodstuffs.

7.2 not store, harbour, or permit the storage or harbouring of any article in the leased premises, or do or suffer or permit any act or omission to be done, as a result whereof any insurance of the leased premises may be vitiated, or as a result of which the premiums may be increased above normal;

7.3 conform to all laws, by-laws, ordinances, proclamations and regulations affecting the lessee or affecting the conduct of its business in, or occupancy of the leased premises and not contravene or permit any contraventions of the conditions of title whereunder the property is held by the lessor;

7.4 carry on its business in such a manner as not to be or become a nuisance to any person.

7.5 not store or sell any alcohol of whatsoever nature in the leased premises. Further, the Lessee shall not permit the consumption of any alcohol on the premises not the storage "in transit" of any alcoholic liquor. The Lessee acknowledges this to be a material term of the Lease Agreement and the Lessor reserves the right to summarily cancel this agreement should the Lessee breach the terms of this clause.

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APPENDIX 2

Estimated distribution of private sector enterprise by population group, sector and size/class.

Estimated distribution of private sector enterprise by population group, sector , and size/class

Sector	Survivalist		Micro (1-4)		Very Small		Unspecified	
	Africans, Asians and Coloureds	Whites	Africans, Asians and Coloureds	Whites	Africans, Asians and Coloureds	Whites	Africans, Asians and Coloureds	Whites
Agricultural, forestry and fishing	14781	1462	15649	29061	409	18620	918	6300
	91%	9%	35%	65%	10%	90%	20%	80%
Mining and Quarrying	1214	77	2922	777	335	1590	334	325
	94%	6%	79%	21%	23%	77%	52%	48%
Manufacturing	19075	3366	33059	19415	1587	16390	2329	4401
	85%	15%	63%	37%	15%	85%	37%	63%
Construction	21000	875	45008	16647	1500	11710	2465	2999
	96%	4%	73%	37%	19%	81%	45%	55%
Trade	101445	10033	146502	78885	6903	32950	11398	18998
	91%	9%	65%	35%	32%	68%	39%	61%
Catering and Accommodation	1883	697	4471	6706	408	2993	315	1400
	73%	27%	40%	60%	20%	80%	20%	80%
Transport, storage and communication	7880	328	45543	8037	2072	3956	1712	1150
	96%	4%	85%	15%	40%	60%	60%	40%
Financial and Business services	5589	2511	11641	16752	2117	38313	900	7000
	69%	31%	41%	59%	10%	90%	14%	86%
Community, social and other personal services	14106	6046	40062	25614	4118	22169	3222	5985
	70%	30%	61%	39%	18%	82%	29%	71%
Total	187803	25615	347357	205094	19569	149779	22813	49048
	88%	12%	63%	37%	12%	88%	32%	68%

Source: NTSIKA, 2001: 52.

APPENDIX 3

Investment quotation from Old Mutual Insurance Company.



F A I R B A I R N
C A P I T A L

Fairbairn Capital (Pty) Ltd
PO Box 617, Howard Place, Cape Town 7450
Mutualpark, Jan Smuts Drive, Pinelands 7405
Tel: 0860 300 000; Fax: 0860 400 000
E-mail: service@fairbairncapital.com
Visit: <http://www.fairbairncapital.com>

FAIRBAIRN CAPITAL

Investment Frontiers Capital Portfolio

Investment proposal prepared for	Mr. K H NGCOBO
Investment proposal prepared by	Old Mutual
Code	
On	02/09/2003
Omuquote Version	4.20
Quote Reference number	QR00001

INVESTMENT DESCRIPTION

The Investment Frontiers Capital Portfolio offers a comprehensive and diversified range of investment options that can be selected to construct a portfolio suitable for the Individual Investor.

INVESTMENT DETAILS

Investment Receipt Date	02/09/2003
Tax Status	Individual

Initial Investment Amount Paid	R	635,000.00
Less: Initial Adviser Fee	R	18,097.50 (Note 1)
Initial Investment Amount Received	R	616,902.50
Less: Initial Administration Fee	R	10,100.00 (Note 2)
Net Investment Amount	R	606,802.50

Notes

1. Initial Adviser Fees are paid to the adviser on the investor's behalf, and include VAT (where chargeable).
2. Initial Administration Fees are calculated as a percentage of the Initial Amount Paid.

INVESTMENT OPTION ALLOCATION

INITIAL INVESTMENT

Selected Investment Option	Asset Mgt Fee (p.a.)	% of Initial Amount	Amount Paid (R)	Administration Fee ¹ (R)	Adviser Fee ² (R)	Net Investment Amount ³ (R)
FRONTIER FUNDS and UNIT TRUST				(1.59%)	(2.85%)	
Optimised Balanced Fund	1.00%	50.00%	317,500.00	(5,050.00)	(9,048.75)	303,401.25
Secured Fund	0.00%	50.00%	317,500.00	(5,050.00)	(9,048.75)	303,401.25
						606,802.50

Notes

1. The Initial Administration Fee has been increased by the applicable Initial Unit Trust Fee.
2. This amount is inclusive of VAT for advisers who are registered for VAT.
3. The Buy/Sell spread of 0.7% is assumed for Illustration purposes for Frontier Funds. This will be deducted from the Net Investment Amount.

ANNUAL INVESTMENT FEES

Annual Administration Fee	0.56 % p.a.
Annual Adviser Fee	0.57 % p.a.

Notes

- The Annual Administration Fee and Annual Adviser Fee are not applicable to Fixed Bonds and Secured Index Bonds.
- The Annual Administration Fee is based on a sliding scale and is deducted monthly.
- The above Annual Administration Fee is the annual rate applicable to this investment in the first month. This may change depending on the value of the funds.
- The Annual Adviser Fee is negotiated between the investor and the adviser and is payable monthly. The Annual Adviser Fee includes VAT,

- the investor has switched from the fund(s) originally invested in;
 - any benefit has been paid or claimed;
 - an Income Tax Certificate has been issued (or such other requirements as may be determined by SARS in terms of practice or legislation);
 - the relevant retirement fund which transferred the investment amount does not accept the refund.
- Note: Additional investments may not breach the 20% Rule of Section 54 of the Long Term Insurance Act of 1998, as this would invoke liquidity limitations.
 - The charges outlined above are the full expenses that will be charged to your policy. These charges are used by Old Mutual to cover all costs of administration as well as the commission payable to the Adviser, Broker and to Private Wealth Management.
 - Advisers employed by Old Mutual Personal Financial Advice receive remuneration partly in the form of reduced commission and partly in the form of other benefits.
 - The Private Wealth Management financial consultant is a permanent employee of Private Wealth Management, a business unit of Old Mutual. The consultant is remunerated by way of salary and performance bonus.

Contacting Fairbairn Capital: If you have any queries regarding investments, or would like assistance in claiming there under, please contact your Adviser or contact the Fairbairn Capital Service Centre directly on 0860 300 000.

Complaint Resolution Process: Old Mutual provides a complaint resolution process which aims to address any dissatisfaction you may have with your transaction. You can write to our Centralised Complaint Administration Department at PO Box 201, Mutualpark, 7451, fax us at (021) 509 0506 or e-mail us at speakyourmind@oldmutual.com. In the unlikely event of a dispute that cannot be resolved, you have the right to contact the Life Assurance Ombudsman for assistance, by writing to: Ombudsman for Life Assurance, PO Box 45007, Claremont, 7735

Notes

1. This quotation is only valid if prepared using the latest version of Omuquote.
2. Please note that Fairbairn Capital and/or Old Mutual does not accept any liability whatsoever for incorrect quotations produced, as a result of any computer system problems.
3. The assets and agreements entered into by Fairbairn Capital and/or Old Mutual in respect of certain portfolio constituents are subject to governmental and regulatory factors. In the event and to the extent that any of these factors impact on the return generated by the assets and agreements, Fairbairn Capital and/or Old Mutual reserves the right to revise the benefit under a portfolio constituent accordingly.
4. Old Mutual does not guarantee that these funds will remain available for the duration of the contract. Should the client reach the maximum total investment into offshore funds of R25m or should Fairbairn Capital and/or Old Mutual close their international funds to investment, we reserve the right to terminate investment into these funds.

APPLICATION PROCESS

All correspondence must be faxed to Fairbairn Capital at 0860 400 000. Confirmation of receipt of the fax remains the responsibility of the sender.

To finalise investments, all requirements must be received by the Fairbairn Capital Service Centre by 16H00, Monday to Friday.

This includes :

- Fully completed investment application form
- Payment method -
 - Signed debit order, or
 - Copy of A.S. receipt, or
 - Copy of Standard Bank deposit slip.

The investment amount will be invested after all requirements have been met and the application has been accepted by Fairbairn Capital, at the first investment opportunity and at the price applicable then.

PLEASE NOTE THAT BACKDATING IS NOT ALLOWED UNDER ANY CIRCUMSTANCES.

In instances where the money / requirements are received on a Saturday, the following week's prices will apply (This should specifically be noted for Fixed Bonds, where the rates are applicable from Monday to Friday).

APPENDIX 4

Questionnaire and letter to employers

CONSUMER RESEARCH QUESTIONNAIRE- RICHMOND

University of Natal, Pietermaritzburg

School of Business

Questionnaire Number

DATE

Identification

1. Gender

Male (....)(1)

Female (....)(2)

2. Area of residence

Richmond (....)(1)

Outside Richmond (....)(2)

3. What is your occupation?

Unemployed (....)(1)

Employed part-time (....)(2)

Employed full-time (....)(3)

4. What is **the nature** of your job?

- | | |
|----------------------------|-----------|
| Teacher | (....)(1) |
| Nurse | (....)(2) |
| Police | (....)(3) |
| Driver | (....)(4) |
| Other (State please) | (....)(5) |

5. Please indicate which of the following **age groups** do you belong to?

- | | |
|--------------|-----------|
| 16-25 years | (....)(1) |
| 26-33 years | (....)(2) |
| 34 –41 years | (....)(3) |
| 42-49 years | (....)(4) |
| 50-65 year | (....)(5) |

6. Please indicate which of the following **monthly income** (gross) groups do you belong to?

- | | |
|-------------|-----------|
| R500-1000 | (....)(1) |
| R1000-3000 | (....)(2) |
| R3001- 5000 | (....)(3) |

7. **Do you visit** public eating-places?

- | | |
|-----|-----------------------|
| Yes | (....)(1) Go to Qn.10 |
| No | (....)(2) |

8. **How often** do you visit a public eating place for a meal?

Daily (....)(1)

Once a week (....)(2)

Twice a week (....)(3)

More than twice a week (....)(4)

Once a month (....)(5)

None of the above (....)(6)

9. How much do you **usually spend** at a restaurant on each visit?

R5-12 (....)(1)

R12-22 (....)(2)

R23-R33 (....)(3)

R34-R54 (....)(4)

R55 and above (....)(5)

10. On visiting an eating-place, which of the following **do you do most often?**

Take-away a meal (....)(1)

Eat-in a meal (....)(2)

All the above (....)(3)

None of the above (....)(4)

11. For take-away meals, which of the following **do you do often?**

Eat at home (....)(1)

Eat at work place (....)(2)

All the above (....)(3)

None of the above (....)(4)

12. Would you **like eating chicken** at the eating-place?

Yes (....)(1)

No (....)(2)

13. How would you generally **rate the quality** of the chicken meals of restaurants in Richmond?

Excellent (....)(1)

Good (....)(2)

Fair (....)(3)

Poor (....)(4)

None of the above (....)(5)

Please state why.....

.....

14. How would you generally **rate the overall service** of restaurants in Richmond?

Excellent (....)(1)

Good (....)(2)

Fair (....)(3)

Poor (....)(4)

None of the above (....)(5)

Please state why.....

15. Have you **ever seen** a Chicken Licken store?

Yes (....)(1)

No (....)(2)

16. If the answer is 'Yes' in Qn. 20 above, **where did you see one?**

Pietermaritzburg (....)(1)

Outside Pietermaritzburg (....)(2)

17. Please name any **Chicken Licken meal** that you know

18. In your view, **is there a need** for a Chicken Licken shop in Richmond?

Yes (....)(1)

No (....)(2)

19. If a Chicken Licken outlet were to open in Richmond, would you **be interested** in buying from that outlet? Which of the following statements would best describe your response:

(i) I will certainly buy meals from Chicken Licken (....)(1)

(ii) I will very probably buy meals from Chicken Licken (....)(2)

(iii) I may buy meals from Chicken Licken (....)(3)

(iv) I probably will not buy meals from Chicken Licken (....)(4)

(v) I will certainly not buy any meals from Chicken Licken (....)(5)

20. Should a Chicken Licken franchise be opened in Richmond, **how often are you likely to buy** from that franchise?

- | | |
|--------------|-----------|
| Very often | (....)(1) |
| Occasionally | (....)(2) |
| Very rarely | (....)(3) |
| Never. | (....)(4) |

21. Indicate roughly, **how much** would you be prepared to spend on each visit in new Chicken Licken franchise to be opened in Richmond? Which of the following statements would best describe your response.

- | | |
|--------|-----------|
| R5-10 | (....)(1) |
| R10-19 | (....)(2) |
| R20-29 | (....)(3) |
| R30-50 | (....)(4) |

22. If the Chicken Licken franchise were opened, **would you support** a Chicken Licken shop in Richmond?

- | | |
|----------|-----------|
| Always | (....)(1) |
| Seldom | (....)(2) |
| Sometime | (....)(3) |

THANK YOU VERY MUCH FOR YOUR COOPERATION

University of Natal,
School of Business
Pietermaritzburg.

I am an MBA student at the University of Pietermaritzburg, School of business and I am currently working on my thesis.

As my study involves a Chicken Licken business venture in Richmond, I would like to interview your employees on the 1st and 2nd August 2003 during their lunch hour.

I would very much appreciate it if you could grant me access during these days.

Thank you,

Yours faithfully,

.....
K.H. Ngcobo

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