

# **Impact of SMEs on Economic Development: A Systematic Review of Literature**

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## **Abstract**

*SMEs are considered the driving force of the country's economic growth via the entrepreneurship process. SMEs also impact economic development based on various aspects such as competitive market orientation, employment generation, capacity building and technology innovation. Therefore, using a systematic review approach, the current study will investigate the SME's impact on developing economies. The systematic review will adopt database searches based on keywords, authorship, citations, titles, journal lists, and topmost enterprises in the context of Bahrain. The review will be analyzed using various database tools such as EDS, Scopus and Web of Science to collect sample of n=8 peer reviewed journals published between 2018 to 2022. The findings shows that SME's plays an essential role in economic development through capacity development, technological innovation, employment creation and competitive orientation.*

**Keywords:** Economic Development, SMEs, Capacity building, Technology innovation.

## **Introduction**

Enterprises development is a significant part of the business economic development via the entrepreneurship process (Guerrero et al., 2021). Entrepreneurship has been a driving force of economic restructuring, decentralization and movement towards a market economy (Varga et al., 2021). Besides, Small and Medium Enterprises (SMEs) are considered a significant factor in developing the country's economy (Muthuraman et al., 2020). The majority of the SMEs are small and subsistence firms; however, there are very few small businesses that can reach medium-sized enterprises, which further few of them have the potential to develop into large-sized enterprises based on the entrepreneurs and establisher of these enterprises.

SMEs, are essential important element of the economy, also significantly impact the country's economic development (Surya et al., 2021). The impulsion of economic growth is the development of SMEs because these small and medium enterprises are deliberated as more flexible than large-sized enterprises in a competitive environment. Recent studies found that an important share in production infrastructure related to works, goods and services of market economies has been employed mainly by SMEs, as demonstrated by gross domestic product size (Petrunenko et al., 2021). The countries with economies in change are presently developing SMEs in the framework of providing support in financing activities, implementation of significant laws and regulations

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and ensuring the involvement in developmental programs by leading global organizations. The business development concept is to make an individual with the required information and knowledge, which is vital for constructing the enterprise and developing entrepreneurial skills.

SMEs represent the central part of business companies in the country's economic development and enhance the market economies' competitiveness. However, the revolution in the global business, such as the open innovation model, internationalization, fiscal policies, networking and mass customization, impact all other countries. Therefore, SMEs confront a competitive environment because of globalization and innovative technologies, including the developing role of CSR in the processes and inter-firm collaboration (Sroka & Szántó, 2018). Moreover, SMEs face various problems and challenges compared to large enterprises (Iqbal et al., 2018). There are various factors of SMEs that greatly influence the economic development (Surya et al., 2021); such as competitive market orientation, capacity building, and employment generation (Muthuraman et al., 2020) and innovative technological performance (Tehseen et al., 2019). Considering the aims, the objectives of the current research is to investigate the role of SME's in economic development and what an antecedents of economic development which are influenced through SME's creation.

## Literature Review

According to (Portes & Böröcz, 1988), the structuralist theory argues that private enterprises should be considered a significant part of global economic development that assists in minimizing labour costs and input, indirectly enhancing the competitive market of large enterprises. Another labour supply theory proposed by (Pedersen, 1998) argues that SMEs growth is recognized in response to the high unemployment rate and performs as employees' solution who cannot be engaged in the economic concepts have presented that when employments increase in SMEs, economic development is probable to rationalize as SMEs drive to search employments in the private enterprises (Matsongoni & Mutambara, 2018).

Define the SMEs concept; there is no proper definition for Small and Medium Enterprises (SMEs) because there are no constant criteria for the number of employees, capital amount, fixed capital investment, revenues, technology and market share. The differences among SMEs are mainly investigated from industry to industry and country to country based on studies (Gherghina et al., 2020).

Considering the concerns related to economic growth, (Muthuraman et al., 2020) claimed that SMEs play a significant role in this process of economic development because these organizations produce the foundation of economic development for global countries. (Šebestová' & Sroka, 2020) argued that SMEs are considered the driving force of the country's economic growth and also one of the implements to accomplish SDGs. On the other hand, (Hernita et al., 2021) proposed that SMEs mainly contribute to the modernization and diversification of the global economy because it influences the reserve turnover growth and the formation of the customer market in circumstances of limited assets and economic decline.

SMEs are competent to rapidly implement changes in customer demand, thus ensuring the required balance in the customer market, reported (Lu, 2018). Another finding of (Tambunan, 2019) found that private entrepreneurship and small businesses play a significant role in addressing the unemployment issues by providing new job opportunities. There are various benefits that the

SMEs to develop the economy, such as economic contribution to productivities of goods and services and the formation of employment at comparatively low-cost assets. For instance, (Oláh et al., 2019) claimed that Small and Medium Enterprises (SMEs) are a tool for minimizing the income disparities and enhancing the association among the country's economy's social, economic and geographic sectors and providing employment by 68.1% in Poland. In other words, SMEs are considered a major socioeconomic and economic development vehicle, as reported by (Šebestová & Sroka, 2020).

Abu-Aisheh (2018) studied the impact of small enterprises on economic growth and revealed positive influences on entrepreneurship and economic development. The study's findings showed that the share of small enterprises positively influences the output of the businesses and is responsible for better performance. In addition, (Melwani, 2018) investigated the significance of separate enterprises for economic growth. The findings revealed that changes in the business market encourage private and small enterprises and are a tool to increase economic development. The findings of Sigala (2018) on the developing economies of countries proposed that entrepreneurship has evolved as a vital factor in economic organizations. Contrary to this, (Dvouletý et al., 2018) studied the role of entrepreneurship in economic development. The study's findings revealed that entrepreneurship levels, such as SMEs, positively influence economic development.

Other findings of (Tirmizi, 2022) highlighted the fact that enterprises assist in producing new employments for the nationals and therefore facilitate economic growth. Additionally, (Bonito et al., 2017) found the interconnectivity between enterprises and economic development. (Surya et al., 2021) studied economic growth and the impact of government policies and strategies on the developing productivity of Small and Medium Enterprises (SMEs). The study's findings revealed that business asset support, government policies and HR capacity positively influence SMEs development by 97.6% of the determination coefficient.

Various scholars and investigators have recently made major efforts to reduce the challenges of measurement concerns by constructing capacity-building measures. In light of the capacity-building definition by (Park et al., 2022), the study has focused more on the ability of enterprises to build, integrate and reconfigure the internal proficiencies. Nevertheless, there is limited literature on the internal competencies to integrate and develop the external proficiencies. The strategic management theory demonstrates that the organizations practice alliances to obtain technology innovation, build capacity, and develop core business undertakings, as reported by (Khurana et al., 2021).

(Ikupolati et al., 2017) investigated SMEs as a major source of capacity building by accessing SMEs' human resources, innovativeness and technology and found that SMEs' operatives are mainly vital to capacity building. Another finding of the same study demonstrated that most respondents (91.9%) approved that SMEs are mainly the source of capacity building. The study also recommended that employees and entrepreneurs be trained in innovative technology that can increase the productive capacity building of SMEs, leading to employment generation.

According to (Yaskun, 2021), entrepreneurship recognizes the market opportunities and the market positioning are demonstrated as consumer-led practice. The findings of (Hai et al., 2021) found that the market positioning needs the organizations to observe instantly altering consumer demands and requirements, recognize the influence of these alterations on the customer satisfaction, and increase the innovation achievement and competitive advantages of the enterprises. (Movrianda et al., 2022) claimed that to understand the current and future customers' needs is critical for the enterprises to incentive the innovation culture in the firms; therefore, it must be required to

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constantly enhance and develop the products and services that need consumer needs and requirements.

Contrary to this, the competitive market includes operative monitoring of inclusive current and potential competitors in the business market and accumulates competitive intelligence to identify competitors' approaches, as reported by (Ksa, 2021). According to (Rincon et al., 2022), the main purpose of market-oriented enterprises is to remain intent on the activities of competitors and reflect this as a concept source for innovative product development. The better consideration of competitive market orientation may often minimize the decline of innovative products.

The study by (Muthuraman et al., 2020) revealed that the potential of SMEs is to produce employment and, therefore, minimize the joblessness in the country's economy. The contribution of employment within small businesses has mainly focused on the policy regulators at all economic levels. (Quaye & Mensah, 2018) analyzed the database of 99 countries and revealed that small enterprises having less than 100 workforces and more than ten years older organizations have the broad total employment share and employment generation capability along with the initial small enterprises participating in employment generation.

The study's empirical findings revealed that Small and Medium Enterprises (SMEs) play a significant role in employment generation, reduction of unemployment and economic development. The huge benefit of SMEs is employment potential with low-cost resources. The SMEs having intense work greatly influence their employment. SMEs with extreme workload intensity produce more employment with low asset costs compared to large enterprises. According to (Sarmah et al., 2021), it is significant for the developing economies with a high rate of unemployment to generate employment in SMEs.:

Innovation is "any idea, practise or object perceived to be new by an individual or other unit of adoption" (Rogers, 1995). Consequently, the innovation can be inside-oriented under being used by the operations internal to businesses or externally focused on the consumers external to the organization, stated by (Gherghina et al., 2020). According to (Zeb et al., 2021), there are four categories of innovations in businesses: process, product, organizational, and marketing.

Innovation can be referred to as radical innovation associated with innovativeness, while incremental innovation is linked to the development of current advances (Aljanabi, 2017). The main aim of driving an organization is to revolutionize and enhance its competitiveness in target markets to get enhanced business performance (Gherghina et al., 2020). Hence, the organizational innovation must be evaluated by the impact on the market position, that is, its innovative performance through technology, as reported by (Tehseen et al., 2019). According to (Aljanabi, 2017), technological innovation is often demonstrated by the patents' number attained by the enterprises. Most SMEs are not determined the patentable innovations because most technological innovations are incremental; therefore, they face various challenges in terms of innovation.

(Surya et al., 2021) studied open innovation, economic growth and the impact of government policies and strategies on developing the productivity of Small and Medium Enterprises (SMEs). The study's findings revealed that economic development associated with technological innovations enhances the economic enterprises' productivity and increases social welfare. Te business asset support, government policies, and HR capacity positively influence SME development by 97.6% of the determination coefficient.

## **Research Methodology**

The current study uses a deductive approach to review previous literature related to SMEs and economic development. The current study is based on a narrative approach to literature review proposed by (Denyer & Tranfield, 2009). A narrative review of the previous literature has been used to analyze the current knowledge comprehensively, and critically and come up with an objective analysis of the current knowledge (Ramdani et al., 2021).

The narrative review aims to define the capacity building, competitive market orientation, employment generation, and technology innovation in the Small and Medium Enterprises (SMEs) research and evaluate the research prospects to improve the current knowledge. A narrative review of literature provides critical evaluation for the development of a theoretical model by gathering, critiquing and summarizing existing literature published in journals.

The current study will use search keywords based on the terms SMEs, technological innovation, competitive market orientation, employment generation and capacity building using Google Scholar which publications are filtered using articles from 2018 and onwards. Moreover, journal lists have been evaluated based on ranking and the number of articles for each journal as findings are proposed using a sample of n=8 articles published in various journals.

## **The Finding**

(Malesios et al., 2018) conducted a study to investigate the impact of social, environmental and operational practices of SMEs on financial Performance where primary data was gathered using quantitative research methods from the dataset derived from 119 British, French and Indian firms. Data gathered was analyzed using regression analysis. Findings show that social, environmental and operational practices reported highly significant covariates. (Abisuga-Oyekunle et al., 2021) conducted a study to investigate the role of SMEs in poverty reduction and sustainable employment using a systematic review of studies conducted in Sub Sahara in Africa. Findings show that SMEs play an essential role in employing the majority of the citizens contributing to sustainable employment. (Rota et al., 2019) conducted a study to investigate the impact of SMEs on employment in the EU-28 region. Using quantitative research methods, the proposed study used panel data from the 2005 to 2016 period. The findings of the study show no significant relationship between SMEs and employment in Eu-28 countries. (Gherghina et al., 2020) conducted a study to investigate the impact of SME investments and innovation on the territorial economic growth of Romania. Using quantitative research methods, panel data was analyzed from the period 2009 to 2017 and data was analyzed using log–log-linear regressions. Findings show that SMEs have no significant statistical impact on turnover but have a significant statistical impact on territorial economic growth. (Al-Haddad et al., 2019) conducted a study to investigate the impact of SMEs on unemployment in an emerging country. Primary data was gathered using questionnaires from SMEs comprised of Marble manufacturers and analyzed using SPSS. Findings show that there is a positive relationship between SMEs and unemployment reduction. (Chege & Wang, 2020) conducted a study to investigate the role of technology innovation in job creation through small businesses in developing countries. Findings were proposed based upon the narrative literature review on technology innovation by SMEs and its role. Findings of the study suggest that Technological innovation aided by SMEs has a significant impact on employment creation which positively affects economic development. (Abdelhamid & Sposato, 2020) conducted a study to

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investigate the role of SMEs' organizational learning policies and their implications on workforce agility using qualitative research where semi-structural interviews of various HR managers in SMEs in Dubai were conducted. Findings show that organizational learning practices in SMEs promote workforce agility through capacity development of the workforce. (Rashidirad & Salimian, 2020) conducted a study to investigate the relationship between different dynamic capabilities, competitive strategies and SMEs' value sources. Using quantitative research methods, primary data was gathered using a survey which was distributed amongst 441 UK-based SMEs. Research findings suggest that sensing, learning, integrating and coordinating capabilities play a significant role in SMEs' value creation, and competitive strategy mediates the impact of dynamic capabilities on value creation.

### **Discussion and Conclusion**

In a nutshell, evidence from the narrative review of literature (Abisuga-Oyekunlea et al., 2021); (Rota et al., 2019); (Gherghina et al., 2020); (Al-Haddad et al., 2019); (Chege & Wang, 2020); (Abdelhamid & Sposato, 2020); (Rashidirad & Salimian, 2020) suggests significant impact of SME's in promoting economic development in various spheres of development indicator whether its building innovative capability amongst the workforce, providing employment opportunities for local population, increase in productivity and improve competitive orientation of economy. All these factors have subsequently contributed in improving the standard of living in terms of social and economic realm. SME's plays a vital role in decreasing income inequalities impeding from concentration of wealth through widespread equal distribution of income and wealth. Regardless of the level of economic growth, SMEs are vital for social and economic order in terms of numerical and job creation capacity.

In summary, SMEs are considered an important element of the economy and significantly impact the country's economic development. The proposed study aimed to investigate the antecedents of SME's influencing economic development using narrative approach to literature. Evidence from the findings suggests SMEs plays an essential role in economic development through competitive market orientation, capacity building, employment and innovative technology in SMEs significantly impact economic growth. In a nutshell, SME development authority must provide inductive environment to promote ease of doing business to promote diversification in economic activities through various financing options.

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