

THE IMPACT OF INNOVATION ON PERFORMANCE OF SMALL AND MEDIUM ENTREPRISES (SMES) IN ALGERIA

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Abstract: Small and Medium-Sized Enterprises (SMEs) face tremendous challenges in their attempt to pursue innovations. Innovation has been considered as a key element for the growth of small and medium sized enterprises (SMEs) for a long time. This field of research has been a subject to numerous studies. In Algeria, however, very few researches have dealt with this subject. The aim of this paper is to explore the effects of the organizational, process, product and marketing innovations on the different aspects of small and medium-sized enterprises (SMEs) performance.

Keywords: Small and Medium-Sized Enterprises, innovation, enterprises performance.

JEL: M21, O31.

Introduction

Performance of small and medium-sized enterprises is affected by the innovations. The sector of small and medium-sized enterprises has become a key pillar in the equation of getting development and obtaining a satisfying rate of economic growth. Over the last 3 decades of the twentieth century, especially in the developed countries, the attention has been drawn to this sector in order to lead the wheel of development and to bring new

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vitality to the economies worldwide. However, it is not only the developed countries that have put their eyes on this sector, but the developing countries like Algeria have also provided sustainable efforts to take care of the SMEs. In fact, the statistics refer to information related to SMEs' efficiency in terms of job creation and reducing the average rate of unemployment, achieving growth, bringing direct foreign investment and participating broadly in the GDP, studies estimate that 90% of the world enterprises are SMEs ones and they are separated approximately over all the fields. Therefore, success or failure in innovation should be viewed as a necessary but not sufficient cause of business performance and survival. This paper is designed to make a retrospective review of existing empirical literature on the impact of Innovation Activities on SMEs performance across countries. The paper adds to the stock of academic works.

This study attempts to probe, within a multi-dimensional perspective, the nature and type of daily innovation practices of small- and medium-sized enterprises (SMEs) located in Algeria; the relationship between innovation and organizational performance will also be explored.

1. The goal of the research and Research methodology

Is studying the performance of SMEs and the factors affecting performance to propose performance measurement concept encouraging the sustainable development of SMEs and to suggest performance evaluation approach?

The study was carried out with the purpose of revealing the existing empirical works, which examine the impact of SMEs on the firm's performance around the globe. In order to achieve this, the author conducted a rigorous review of literature and documentary information related to the subject matter.

The paper is purely based on desktop and library research methodology. In this regard, articles selected from top Enterprises journals, research papers, diagnostic study reports have been surveyed in making this study. The review is mainly on Innovation on Performance researches conducted around the world between 2005 and now. These previous studies emphasized on the factors that influence innovation showed clearly how innovation affects business performance particularly among SMEs.

2. Empirical studies on innovation and performance of SMEs

This section presents the empirical studies worldwide on innovation and firm's performance across industries. This aims to enlighten the research on the existing results and conclusions thereon, which is useful in research gap identification. This section is in addition to discussing the concepts of Small and Medium Enterprises (SMEs) and innovation and the measurement of performance in this context. The section is therefore divided into three parts: the description of the concepts of innovation and SMEs, the measurement of performance and existing results of empirical studies in this context.

The term Small and medium-sized enterprises has no standard definition. It has been identified differently by various individuals and organizations, such as: an enterprise that is considered small and medium in one country is viewed differently in another country. Some common indicators employed in the various definitions include total assets, size of the labour force employed, annual turnover and capital investments. In addition, no single definition of SMEs exists among officials of multilateral development institutions [1], as represented in Table 1.

*Table 1
SME Definitions Used by Multilateral Institutions*

Institution (region or country)	Max of employees	Max revenue or turnover	Max assets
EU	10 - 250	40 million Euros	-
WB	300	15,000,000\$	15,000,000\$
IMF-IADB	100	3,000,000\$	-
African Development Bank	50	-	-
Asian Development Bank	No official definition. Uses only definitions of various national governments		
UNDP	200	-	-
OECD	20-500	-	-
Algeria	10 - 250	>20 million Euros	-
China	> 2000 employees	300 million yuan	400 million yuan

Source: Asma Benzazoua Bouazza, Diabate Ardjouman, *Establishing the Factors Affecting the Growth of Small and Medium-sized Enterprises in Algeria*, *American International Journal of Social Science* Vol. 4, No. 2; April 2015, p 112

According to the Algerian ministry of commerce, Small and Medium Enterprises define regardless of its legal status in terms of providing either goods or services or even both, by setting some characteristics, which are:

- Not more than 250 employees;
- Annual turnover does not exceed 02 billion dinars or whose annual balance sheet total does not exceed 500 million dinars;
- It should match with the criteria of independence.

Table 2
Definition of SMEs in Algeria

Enterprises	Employees	Turnover (dinars)	Total assets (dinars)
Micro	1-9	< 20 million	< 10 million
Small	10-49	< 200 million	< 100 million
Medium	50-250	200million- 2 billion	100 - 500 million

Source: Algeria's Ministry of Industry, Small and Medium Enterprise and Investment Promotion.

Algerian SMEs exhibit the following specific characteristics that distinguish them from large firms.

➤ **Algerian SMEs are dominated by private enterprises:** The Algerian SME sector is dominated by private enterprises according to the Algerian Ministry of Industry, SME and Investment Promotion. By the end of 2012, 99.92% of all SMEs were private and the remaining 0.08% were public. These percentages indicate that job and wealth creation in the Algerian SME sector are based on, and rely on private SMEs.

➤ **Algerian SMEs are concentrated in north Algeria:** In Algeria, a disparity exists in the spatial distribution of SMEs, with a higher concentration recorded in the north, followed by the highlands, and finally the greater south.

➤ **Algerian SMEs are concentrated in the service and construction sectors:** Algerian SMEs have a strong presence in the service sector (particularly transport) and account for nearly half of all SMEs, followed by the building, construction and hydraulic sector at 33.85% SMEs (building in particular). The manufacturing sector comprises 16.07% of all SMEs, and the agriculture and energy sectors account for only 1.09% and 0.49%, respectively, of total SME activity [2].

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Small and medium enterprises have fulfilled many tasks in their history, they manufactured products, which were ignored by large enterprises and offered various specialized services. Up to the present, they have played an important role in GDP creation, in the process of employment, labour productivity increase and in regional development; they are viewed as an important source of new ideas and innovation.

Among the characteristics of small and medium enterprises that have made them able to play an important contribution to the economic and social development as well as contribute to reduce the rate of unemployment. The following characteristics are presented [3]:

- Enhancing the initiative spirit of individuals and groups by initiating economic activities for goods or services that didn't exist before, as well as the revival of economic activities, which have been abandoned such as the traditional industries.

- Reintegration of the demobilized employees from their positions due to the bankruptcy of some public institutions or the employment reduction in some organizations, as a result of restructuring and privatization, which would support the possibility of compensation of some of the activities.

- Generating new job offers both directly via enterprise establishers and indirectly, through recruiting other jobless individuals within enterprises, which can lead to a rapid response to social demands in the field of employment, as these enterprises seek to provide work positions intended for individuals who do not meet the needs of large organizations. These enterprises pay less wages than the large organizations do, as the average qualifications are inferior to those obtained by employees working for large organizations. Small and medium enterprises can establish an effective tool for activities resettlement in the remote areas, leading them to be an effective tool for a significant enhancement of local wealth and means of domestic regions merging and integrating.

3. Challenges faced by SMEs

A number of studies have been performed on challenges faced by SMEs in developing countries as well as in Algeria. Small and Medium Industries Development Plan (SMIDP) in its 2001-2005 report (SMIDEC,

2002) and SME Master plan (2012) identified many challenges faced both at domestic and international levels. These challenges can be summarized as the following:

- innovation and technology adoption (low commercialization, poor technology uptake);
- Human capital development (lack of job readiness of employees and effectiveness of training);
- Access to financing (limited non-banking avenues, poor credit worthiness and lack of know how/resources);
- Market access (information barriers for exports, low marketing and branding);
- Legal and regulatory environment (Licensing and permits issues, compliance to regulations); and infrastructure (trade clearance and facilitation system and low/infrequent trade volumes) [4].

The majority of small and medium enterprises in Algeria are private. Since 2000, the number of these enterprises has become very important by facilitating the proceedings of establishment, as well as the spread of the entrepreneurial spirit among young people, especially university graduates. This increase is more than double, as all available statistics indicate that more than half of small and medium enterprises were established between 2001-2007 after the issuance of the guiding law on small and medium enterprises in 2001 [5].

Referring to Table 3 below, we note that the number of small and medium enterprises at the end of the year 2012 show a remarkable development by creating 687386 enterprises, compared to 288587 enterprises in 2003, contrary to public enterprises that record a decrease of 217 during the first decade of the third millennium as a result of the privatization of troubled enterprises [6]. As for traditional handicraft enterprises, they have recorded an increase higher than 79850 in 2002 to 169080 enterprises in 2009, but they fluctuate till 2012.

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Table 3
Evolution of the number of small, medium and traditional handicraft enterprises (2003-2012)

Enterprise's nature	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Private E.	207949	225449	245842	269806	293946	392013	455398	618515	511856	532 702
Public E.	788	778	874	739	666	626	591	557	572	561
Traditional handicraft activity	79 850	86 732	96 072	106222	116347	126887	169080	135623	146881	154 123
Total	288587	312959	342788	376767	410959	519526	625069	754695	659309	687 386

Source: Made according to the Ministry of Small and Medium Enterprises publications.

The number of SMEs in Algeria has indicated an important growth, especially after the transition from the socialist economy towards market economy at the beginning of the last decade of the 20th century.

The statistics show that the amount of SMEs in the first semester of 2013 was 747.934, in which 90% are very small enterprises, whereas the number of the same sector was 455.398 in 2009. The statistics indicates a huge growth of SMEs in Algeria, which is due mainly to the policy of Algerian authorities aiming to promote this sector and turn it into a resource of wealth. Despite the tremendous efforts provided by the government to enhance the performance of this sector, the facts point out the disability of this sector to cover the huge shortage that big enterprises can't take into account [7].

The following data delivered by the Ministry of Industrial Development and Investment Promotion present the number of jobs held by the SMEs in the first semester of 2013.

Table 4
Statistical bulletin of Algerian SMEs for the first semester of 2013

SMEs period	Number of SMEs	Number of jobs creation	Number of entities created per year	Job's creation by new entities	SMEs cessation of activity
2012	687386	1776461	27736	99892	2182
1st semester of 2013	747 934	1 915 495	34 811	177 010	2 661

Source: ministry of industrial development and investment promotion, *Statistical bulletin of SMEs for 1st 2013*, N:23, November 2013, p 07.

4. Understanding the concepts of innovation and its determinants

Innovation is the generation and/or acceptance of ideas, processes, products, or services that the relevant adopting unit perceives as new; it can be new to either the firm or the firm's customers. Depending on their "newness," innovations can be incremental (continuous) or breakthrough (discontinuous).

Incremental innovations refer to minor changes in technology, simple product improvements or line extensions that minimally improve the existing performance [8].

Innovation described as "the introduction of new or improved processes, products or services based on new scientific or technology knowledge and/or organizational know-how". An invention is the first occurrence of an idea for a new product or process whereas innovation is the act of putting it into practice.

There are different types of innovation in business. However, it can be related to new products or services, new production processes, new marketing techniques and new organizational or managerial structures. Innovation may also involve technology, intellectual property, business, or physical activity [9].

The significance of innovation as firms' resources has been shown in the literature by a wide range of definitions. Some argued that innovation "is the coming up of ideas and bringing them to life". Others defined innovation as 'the renewal and enlargement of the range of products and services and the associated markets; the establishment of new methods of products, supply, and distribution; the introduction of changes in management, work organization, and the working conditions of the workforce'. The Innovation Union classified innovation as "change that speeds up and improves the way we conceive, develop, produce and access new products, industrial processes and services [10]". 'Innovation is intrinsically about identifying and using opportunities to create new products, services or work practices'.

What is more, the report has shown that firms' decisions to expand on innovations has brought improvement to workers capabilities, better

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wages and salaries and a decisive prospect for employees. Consequently, these effects of innovations on firm performance vary in scale from sales, market share and profitability to output and efficiency.

Innovation has been a dominant factor in maintaining worldwide competitiveness. It fuels organizational growth, drives future success, and is the engine that allows businesses to sustain their viability in the global economy. For companies pursuing excellence in this era of hyper-competition, restructuring, lowering costs, and enhancing product or service quality are no longer sufficient. Porter and Stern (2001) argued that companies must be able to create and commercialize a stream of new products and processes that extend the technology frontier, while at the same time, keep a step or two ahead of their rivals.

Innovation pressures apply to large companies as well as small- and medium-sized enterprises (SMEs). Scholars have noted that SMEs are often more fertile than larger firms in terms of innovation. Their comparative advantages over large firms in innovation are their flexibility and speed of response. As a result, SMEs generally make a valuable economic and social contribution because of their innovative capacities [11].

The literature on the concept of performance is extensive and the selection of references and disposition have been made, so that the broad spectrum of differences, as well as similarities between different meanings is as clear as possible. The review indicates that defining performance of small and medium enterprises (SMEs) is a challenge across the world.

Performance of small and medium enterprises (SMEs) have been defined in various ways in the literature, and in any business. The related parties always want to see good performance in their business.

A wide variety of definitions of company performance have been proposed in literature by researchers in this field. (Ajanthan et al. 2013; Korir & Imbaya, 2013, Uadiale & Fagbemi, 2012) defines performance as a measure of how well a company can use its assets from its primary mode of business and generate revenues. On the other hand, in the modern literature performance is defined as the results of the activities of a company or investment over a given period. Performance can also be defined as the accomplishment of specified business objectives measured against known standards, completeness and cost [12].

According to March & Sutton (1997) Performance is so common in research about small and medium enterprises (SMEs) management that its structure and definition are rarely explicitly justified; instead its appropriateness, in no matter what form, is unquestionably assumed. However, performance can also be defined as the accomplishment of specified business objectives measured against known standards, completeness and cost, the level of success of a company within the small and medium enterprises (SMEs) sector is measured through its performance based on a selected period of time. In business studies, the concept of success is sometimes used to refer to a company's performance [13].

Given that small and medium enterprises (SMEs) often play a significant role in improving the economy of a country and lead to economy development globally, this makes performance one of the key issues for small and medium enterprises (SMEs), where management is concerned. A company's performance is usually seen from the extent it manages to achieve its purposes and goals. Earlier researchers have attempted to provide a clear definition of performance, but they had yet to come to an agreement over a common definition, particularly regarding some aspects of terminology issues, analytical levels, and the conceptual basis for assessment. Performance of a company can be defined in various ways, depending on the questions in mind when we inquire about a company's performance.

The findings of many studies have not managed to provide a common definition to indicate or ascertain performance; based on the findings of earlier research, performance encompasses three specific areas of company outcomes:

- **financial performance** (profits, return on assets, return on investment, etc.);
- **market performance** (sales, market share, etc.);
- **share holder return** (total shareholder return, economic value added, etc.) [14].

Performance of a firm is related to the ability of the firm to gain profit and growth in order to achieve its general strategic objectives, it is a consequence of the interaction between actions taken in relation to competitive forces that allow the firm to adapt to the external environment,

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thereby integrating competence and usefulness, emphasizes that the firm's innovation performance depends on the opportunities provided by its external environment. This implies that SMEs become very competitive in an emerging market when they give importance to innovative activities that build their reputation in the market environment. Essentially, the key reason for innovativeness is the desire of firms to obtain increased business performance and increased competitive edge [15].

However, in measuring firm performance, different concepts are used to include sales per employee, export per employee, growth rates of sales, total assets, total employment, operation profit ratio and return on investment in the end, all the innovative activities of the firm must result in better performance of the firm compared to companies that do not innovate. In this respect, the performance in this context is also measured in similar ways in assessing the impact of innovation activities on SME performance [16].

One of the primary research areas in the recent innovation literature aims to find out the acknowledged relations between innovation types and firm performance. Although there are quite numerous conceptual studies, analytical and empirical studies are limited, both in terms of numbers and the extent and depth of the analysis. Only a few studies have intimately examined the relationship between innovation types and performance of the firm, as Jin et al. (2004) stated. The empirical studies focused on the relations between a few dimensions of innovation types and/or a single performance aspect [17].

The impact of innovation on corporate performance has been the subject of an intensive study, especially among smaller firms, where there are severe data problems, and, often - inconclusive literature. Literature about smaller businesses is often based on small or data restricted samples, suggests positive relationships between innovation and employment or turnover growth, but weak or absent relationship with profitability[18].

Innovation activities can be generated within SMEs, wherein the internal environment determines how resources are used and delegated in the organization. However, innovation activities can occur in cooperation with a group of SMEs, in a networking setting through innovation systems and even through the economy of an entire region or a country. These activities can even take place on a global scale [19].

That is why, in my opinion, it is necessary to look at both perspectives if one wishes to tackle the issue of SME's performance and relate performance to the topic of innovation.

5. Conclusion and Implication

SMEs are known to account for a substantial share of every country's economy. The relative importance of this segment of the economy needs an examination of their enterprises' performance. Therefore, the fact that the SMEs performance strongly relies on their innovativeness attracts active importance to the analysis of innovation activities and their effects.

Innovation's positive impact on the efficiency and performance of firms requires clarification on two points. The first point is that investments in innovation and technology should be treated as positive inputs into the efficiency of the firm rather than as cost figures that exhaust the firm (as they are often treated in the classical approach of finance and accountancy). The second point is that such investment need to be related to the production costs to reflect the true utilization of the firm's resources. A higher ratio is an indication of the firm management's high level of commitment to investment in innovation and absorption of new technologies, while a lower figure indicates the opposite, and actually points to an old style, non-innovational approach to firm development strategies.

The purpose of this study is to investigate the worldwide empirical research evidence on the impact of the innovation and innovative activities related to the performance (measured in different ways) of the small and medium enterprises. The study is based on a desktop and library review. The issue of innovation and how it relates to firm's performance and, especially SMEs, is yet to be exhaustively explored. Yet, the results from the reviewed literature are mixed and difficult to generalize as it has been shown in the four discussions.

The paper is a "wakeup call" for empirical studies that assess the impact of innovation on SMEs performance in Africa and Algeria, in particular, where the studies of this nature are rarely found in the review of literature conducted in this paper.

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