

Challenges for Pakistani SMEs in a Knowledge-Based Economy

Muhammad Khalique¹, Abu Hassan Md. Isa² and Jamal Abdul Nassir Shaari³**Abstract**

Purpose: Attempt is made to identify the major issues of knowledge-based economy, which are facing SMEs in Pakistan. **Literature review:** literature review reveals that Small and Medium Enterprises (SMEs) are playing very important role in the development of economy in Pakistan. Despite of the important contribution to economy, SMEs are still facing serious issues. These issues create serious threats for the survival of SMEs in Pakistan. After twenty first century, the economy transformed from production based to a knowledge-based economy. In a knowledge-based economy intellectual capital appeared as a critical factor for the successes of organizations. **Methods:** this research is based on the previous researches' findings. **Conclusion:** It is concluded that at the beginning of the twenty first century the concept of intellectual capital has gained a significant attention in a knowledge-based economy. There is no doubt, present economy is a knowledge-based economy and it stand on intellectual capital. Therefore, it is indispensable for SMEs in Pakistan to revolutionize and adopt the concept and applications of intellectual capital in order to dilute the emerging economics challenges. **Recommendations:** SMEs in Pakistan need to strengthen the concept and applications of intellectual capital in their organizations in order to achieve the competitive edge in the market.

JEL. Classification: D21; D23; D24; D83; E24; O31; O33; O33;

Key words: Knowledge-based economy, Intellectual capital, Challenges of SME

1. INTRODUCTION

The contributions of small and medium enterprises (SMEs) considered backbone of economic growth in developing as well as developed nations. SMEs in Pakistan is playing critical role in the economic growth, progression of technological innovation, sourcing to large industries and promoting economic renewal and social development. Like other developing countries, Pakistan's economy is also largely based on SMEs. Minniti, Bygrave and Autio (2005), Hodgetts and Kuratko (2004), Schlogl (2004) and Ahmad, Rani and Kassim (2011) argued that SMEs have major contribution to the development and competitiveness of the economy. According to the Small and Medium Enterprises Development Authority (SMEDA), Pakistan, SMEs represent nearly 90% of all the enterprises in Pakistan. It almost employed 80% of the non-agricultural

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labor force; and shared approximately 40% in the annual GDP of the country (Malik, Khan, Bhutto and Ghouri 2011). The importance of SMEs in economy cannot underestimate because SMEs are main source to reduce poverty, expansion in the national economy, foundation of employment and social uplifting (Akhtar, Raees and Salaria 2011).

There is no doubt to say that SMEs are playing significant role in the development of economy. However, on the other side, the collapse ratio of SMEs is alarming for developing as well as developed countries. Past studies identified that a significant numbers of new SMEs fail within first five years of their business operation (Zimmerer, Scarborough and Wilson 2008; Hodgents and Kuratko 2004). Several studies from Australia, USA and England showed that approximately 80% to 90% of SMEs fails within 5-10 years (Zimmerer et al. 2008; Hodgetts and Kuratko 2004; Peacock 1985; Ahmad et al. 2011). In the same way, In Malaysia there is lack of literature and information, so for the estimated failure rate of SMEs is approximately of 60% (Portal Komuniti 2006; Ahmad and Seet 2009). However, the failure rate of SMEs in Pakistan is approximately 90-95% at initial stages (Ullah, Shah, Hassan and Zaman 2011). It indicates that SMEs in Pakistan has great threats for their survival as a competitive enterprise. That is why to evaluate it and get better recommendations for improving it this study is carried out, which is based on literature review.

2. DEFINITION OF SMES IN PAKISTAN

There is no uniform definition of SMEs are available in literature. In USA employees fewer than Five hundreds (500) are considered as SMEs. In case of European Union, businesses having less than 250 employees are deemed as small and medium business. In Pakistan, according to Small and Medium Enterprise Authority (SMEDA) provided definition, SMEs are defined as enterprise having up to 250 employees and paid up capital up to Rs. 250 million and annual turnover of Rs. 250 million.

3. BUSINESS CHALLENGES IN A KNOWLEDGE-BASED ECONOMY

Twenty first century is likely to be the century in which the economies will grow on the creation and application of knowledge, technology and information (Verma 1995). The difference between evolving knowledge economies from the traditional economies is that the traditional economies have been based on quantitative input factors such as land, labor and capital. While the new economies namely knowledge-based economy will flourish from the qualitative input factors namely human capital and technology innovation (Gardner, Verma and Payne 2006). Literature from all over the world described that the issues of SME's are same around the boundaries of the countries. For example Muhammad, Char, Yasoa and Hassan (2010); Saleh and Ndubisi (2006), Samad (2007); Abu Bakar, Mad and Abdull (2006); Aris (2006); Harvie (2004); Wafa, Noordin and Kim-Man. (2005); Ritchie and Brindley (2000); Decker, Schiefer and Bulander (2006); Foon (2006); Alam (2010); Ullah (2011); Malik et al., (2011); Jaffari, Saleem, Zain-Ul-Abideen, Kaleem, Malik and Raza (2011) identified various challenges facing SMEs in a globalized environment. They mainly focused on facing recession, barrier from global sourcing, low productivity, lack of managerial capabilities, lack of financing, difficulty in accessing management and technology, heavy regulatory burden, etc.

Most of the researchers identified potential operational problems in SMEs at very initial stages. These problems mostly related to the production base or industrial base economy. There is no doubt that SMEs have such kind of problems in their business operation particularly in Pakistani context. However, in a knowledge- based economy, knowledge and intellectual capital is recognized as the most important source of

competitive advantage particularly for SMEs (Daud and Yusoff 2010; Shaari, Khalique and Isa 2010; Khalique, Shaari, Isa and Ageel. 2011). The knowledge-based economy is based on sharing of knowledge and intellectual capital. In this economy competitive advantage will go to those countries that having the capacity to deliver fast and innovation in their work and services (Wickramasinghe and Sharma 2005). In a Knowledge-based economy intellectual capital appeared as the critical component for the success of organization. Ramezan (2011) argued that organizational knowledge is the base of intellectual capital therefore, it is considered as the heart of organizational capabilities. Many researchers such as Bernhut (2001); Luthy (1998); Marr (2008); Steenkamp and Kashyap (2010) argued that intellectual capital is one of three critical resources (the other two being physical and financial capital/assets) of organizations. In the same way, previous studies indicated that intellectual capital is positively and significantly associated with the organizational performance (Bontis 1998; Bontis, Chua and Richardson 2000; Huang and Wu 2010). Ngah and Ibrahim (2009) founds that intellectual capital is the most important resource for the success and survival of SMEs.

4. CHALLENGES OF SMES IN PAKISTAN

Research on SMEs in Pakistan is at initial stages. The health of SMEs is at their alarming stage. Political instability, lack of intellectual capital and infrastructure, and energy crises are the general and serious threats, which are facing SMEs adversely. In other hand, Memon, Rohra and Lal (2010) argued that SMEs in Pakistan have serious shortage to implement the concept of performance management system (PMS). Due to lack of implementation of PMS the SMEs are less competitive and efficient. In addition, they identified that SMEs do not apply human resources policy in recruitment, generally pursue tradition methods for selection. Akthar et al. (2011) identified that SMEs in Pakistan have major challenges such as difficult entry and fear of entering and performing well in foreign markets. Due to lack of competences, SMEs do not able to compete in national as well as international level. Therefore, SMEs have fierce challenges for their survival in competitive environment. Ullah et al. (2011) observed that the major challenges for the success of enterprises are the lack of entrepreneurial skills, education and characteristics. In addition, they argued that in Pakistan there is a lack of concept of proper training and basic education before starting the business. The deficit of training and education is the main cause to be the failure of these enterprises.

Now the world is moving from a production-based economy to a knowledge-based economy (Drucker 1993;; Huang and Wu 2010). In a knowledge-based economy, intellectual capital is a key driver for the success of the organizations. A Knowledge-based economy is transferring the ideas into products and services (Khalique et al., 2011). The knowledge workers are prerequisite for the generation of new ideas, products and services to take competitive advantages. Drucker (1999) emphasized that in the 21st century; the knowledge worker productivity will be the biggest managerial challenges for the organizations to achieve the competitive advantages. Knowledge productivity is mainly based on the organizations ability. Knowledge workers are the main sources for the organizations ability. In the same way, Khalique et al. (2011) stated that in a knowledge-based economy intellectual capital is appeared as the critical factor for the success of organizations.

5. CONCLUSION AND FUTURE RESEARCH

Based on the abovementioned notions and previous researches' findings, it could be concluded that at the beginning of the twenty first century the concept of intellectual capital has gained a significant attention in a *Challenges for Pakistani SMEs in a Knowledge-Based Economy* 76

By M Khalique¹, AHM Isa¹ and Jamal AN Shaari¹

knowledge-based economy. There is no doubt, present economy is a knowledge-based economy and it stand on intellectual capital. Therefore, it is indispensable for SMEs in Pakistan to revolutionize and adopt the concept and applications of intellectual capital in order to dilute the emerging economics challenges. SMEs in Pakistan also need to strengthen the concept and applications of intellectual capital in their organizations in order to achieve the competitive edge in the market. The importance of intellectual capital is highly acknowledged in order to improve the organizational performance. Presently, in Pakistan there is limited literature is available to find the role of intellectual capital in SMEs. The researcher believes that the research in intellectual capital could be significant for SMEs.

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