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How Critical was the COVID-19 Pandemic? Exploring The Effects on Small Business Finance

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ABSTRACT

A plethora of obstacles frequently confront small business enterprises. Still, many business owners were caught off guard by the unexpected COVID-19 outbreak. This research is a survey of small businesses in the city of Jos, Nigeria. The objective is to determine the financial exposure of small businesses to the COVID-19 epidemic. We obtained primary data from respondents using Likert scale questionnaires. Descriptive analysis was used to address the study questions with the data collected. Our findings showed that liquidity was the worst-hit aspect of business finance. This was closely followed by profitability, while debt management was the least impacted of the three domains. The theoretical argument of the study suggests a pragmatic approach to assessing how external environmental factors affect business entities. The authors recommend that business owners should make concerted efforts to get a financial education.

Keywords: Business environment, Business Finance, Business Management, COVID-19, Entrepreneur, Osaz hypothesis, PESTEL, Small business

Introduction

The phrase *health is wealth* is one of the most used cliches of the century. However, the truth of this adage has persisted in drawing interest from authorities, institutions, households, and the general society. In December 2019, the coronavirus pandemic broke out in China (Akpan *et al.*, 2020), bringing the world to a standstill. According to the World Health Organisation (2023), there have been over 769 million confirmed cases of the virus infection and over 6.9 million deaths as of August 2023. Naseer *et al.* (2023), mention that the pandemic is the worst humanitarian crisis faced by humanity since World War II. The first case of coronavirus in Nigeria was reported in February 2020 (Enesi and Ibrahim, 2021).

Among the 17 Sustainable Development Goals (SDGs) that the United Nations launched, health is ranked third. The foregoing buttresses the importance of human health and the priority it occupies on a global scale. Health is crucial because it affects many other areas of life, including the financial well-being of the economy (Ridhwan *et al.*, 2022). The active participation of households, businesses, and the government in economic activities is responsible for driving economic growth. When these economic agents suffer, the economy also suffers.

There is abundant evidence that the COVID-19 pandemic has been a major catastrophe for the global economy (United Nations Development Programme and National Bureau of Statistics, 2021). The global economic effects of the pandemic include job losses (Thomas, 2020), increased poverty (Naseer *et al.*, 2023), debt explosion (Kose *et al.*, 2021; World Bank, 2022), widening income inequality (World Health Organization, 2023), and declining business revenues (Kalogiannidis, 2020). According to Jabeen *et al.* (2022), global stock markets suffered losses running into trillions of dollars. Also, there has been an unprecedented disruption of local and global supply chains (Xu *et al.*, 2020) due to lockdown restrictions implemented in various jurisdictions to curb the spread of the virus.

Businesses have not been spared amidst the health crisis. Bourletidis and Triantafyllopoulos (2014) assert that small businesses suffer the most in periods of crisis. According to Belesky *et al.* (2021), the pandemic has had a greater impact on small businesses compared to larger entities. Bartik *et al.* (2020)

found large-scale downsizing and closures among small businesses in the United States just a few weeks into the pandemic. Entrepreneurs and small businesses play a crucial role in the economy (Adeosun and Shittu, 2021). According to the World Bank (2023), SMEs make up approximately 90% of businesses and are responsible for more than 50% of employment worldwide. Ezigbo (2023) reports that SMEs contribute 96%, 84%, and 48% to business formation, employment, and Nigeria's Gross Domestic Product (GDP), respectively. Despite the high rate of failure of small businesses, the focus of many economies in recent years has been to pursue economic growth and development through initiatives to support and empower small businesses (Edmiston, 2007).

Empirical studies have advanced many reasons for small business failure. Prominent among these causes is poor financial management (Abiola *et al.*, 2021; Amankwah-Amoah and Wang, 2019). The entrepreneur's basic financial management includes profitability, liquidity, and leverage. These crucial aspects of a small business are not to be taken lightly, as they can make or mar a business. An inherent complexity exists when we consider that the entrepreneur is at the mercy of the interaction between these financial management domains. An action in one area can influence outcomes in another area (Kontuš and Mihanović, 2019). It would be interesting and insightful to gauge the effect of the pandemic on these financial dimensions of the small business enterprise.

Jos is the capital city of Plateau State, located in the North-Central geopolitical zone of Nigeria. The city is famous for its agriculture and tourism potential, as well as its unique temperate climate that stands out from the rest of the country. Small businesses and entrepreneurs abound in the city. According to a World Bank survey of the ease of doing business in 37 key areas in Nigeria, Plateau State came in at number 25 (The World Bank, n.d.). The foregoing suggests that there are considerable constraints on business survival and growth in this area.

Our study attempts to zero in on small businesses in Jos. The objective of the study is to examine the extent to which the health crisis has affected the finances of small businesses in the area, given its already poor position in the pecking order of business friendliness ratings in Nigeria. It is hoped that the insights gained will provide valuable information for policy formulation, government intervention, and business strategy.

Conceptual Review

The Small Business

There is no universal definition of a small business (Margaretha and Supartika, 2016). One distinguishing attribute of many small businesses is that they are intricately linked to the entrepreneur (Tisu *et al.*, 2023). As much as formal business procedures and systems may try to separate them, there is overwhelming evidence that a strong relationship exists between the entrepreneur and his small business. According to Erhomosele and Obi (2022), the definition of a small business is typically determined by national or institutional standards, taking into account widely accepted criteria including revenue, profit margin, staff size, and firm size.

Table 1

Classification of Small businesses

Category	Employment size	Turnover (NGN 'M)
Nano/homestead enterprises	1-2 persons	< 3
Micro enterprises	3-9 persons	3 < 25
Small enterprises	10-49 persons	25 < 100
Medium enterprises	50-199 persons	100 < 1,000

SMEDAN and NBS (2022)

In Nigeria, the Small and Medium Enterprises Development Agency of Nigeria (SMEDAN, 2017), has previously used the acronym MSMEs, which stands for *Micro, Small, and Medium Enterprises*. In a 2022 report published by SMEDAN and the Nigerian Bureau of Statistics (NBS), small businesses were reclassified, giving birth to the acronym NMSMEs (*Nano, Micro, Small, and Medium Enterprises*). This segregation was based on the criteria of the number of employees and annual turnover, as shown in *Table 1*.

Profitability

Profitability is a non-negotiable objective in the realm of business. The performance of every business entity will ultimately be evaluated based on its profitability. According to Toshniwal (2016), profit fundamentally represents the excess of output over input and may be classified as either accounting profit, economic profit, or social profit. The focus of this study is the accounting profit of small businesses. Small businesses make a profit when their income exceeds their expenses. Profitability is crucial for small business growth and survival (Yazdanfar, 2013), particularly in this region of the world where the business failure rate is as high as 80% (Kippa, 2022). Profitability measures the ability of the entity to efficiently utilise available resources.

Numerous studies have investigated the factors that affect business profitability. A popular perspective is to view these factors as either internal or external to the entity. Inherent influences include firm size (Yazdanfar, 2013), age, leverage, management efficiency (Prijadi and Desiana, 2017), and technology adoption. External determinants of business profitability comprise variables such as the nature of the industry, competition, trade regulations, and so on. A second perspective we have postulated categorises profitability determinants as either *prevailing factors* or *shock factors*. Prevailing factors describe those influences that are either already known, predictable, or both. Shock factors, on the other hand, are one-off or scarcely occurring influences capable of impacting the profitability of a business. A prime example of what we have identified as a shock factor is the COVID-19 pandemic.

Liquidity

In finance cycles, the long-age argument for supremacy between profits and cash flow persists. The fact, however, is that both are vital (Ehiedu, 2014) to any business and interrelated (Bashir and Regupathi, 2021; Rajapaksha and Weerawickrama, 2020) in financial management. The importance of liquidity to small businesses is buttressed by McMahon and Stanger (1995), who liken it to a matter of life and death. While there has been tremendous growth in the credit system within the global economy, cash remains king. This is especially true in Africa and other similar parts of the world, where the economy is still largely based on cash flow. The foregoing suggests that developed economies may be in a better position to absorb liquidity shocks compared to their less developed counterparts.

Liquidity highlights the ability of the firm to meet its current maturing obligations as and when due. It hints at how efficiently assets can be converted to meet the financial needs of the entity. According to Airout *et al.* (2023), small businesses are more susceptible to liquidity challenges when compared to larger businesses. This means that events such as the COVID-19 pandemic can have a significant impact on the liquidity management of small businesses and, by extension, their survival and growth.

Debt Management

Generally, debt is neutral. However, debt may be considered from either a positive or a negative perspective, depending on the circumstances under which it is secured or how the debt is utilised by the debtor. Access to additional capital for a business creates value by boosting the earning capacity of the business (Badi and Ishengoma, 2021; Manyanga *et al.*, 2023). However, injecting new capital into a business does not automatically translate into business success. Unplanned and poorly managed capital is more likely to produce negative effects than it is likely to spur growth. One thing is clear: debt management influences business performance (Githaiga, 2015).

It is safe to hypothesise that the lockdown period may have forced small business owners to seek additional capital due to the tie-down of capital in inventory, the need to settle incidental expenses, or even persistent drawings made for personal use. All things being equal, a global health pandemic like the COVID-19 crisis can derail small business owners whose structures are not as formal or institutionalised, and who may not have buffer funds to fall back on compared to their larger counterparts (Nicolas, 2021). In addition, small business entrepreneurs often lack the knowledge and skills to manage business capital (Addaney *et al.*, 2016; Mühlböck *et al.*, 2017).

Empirical Review

It is not unexpected that most studies focus on the negative impacts of COVID-19 on small businesses. However, a few studies have found some positives amid the gloom. Harel (2021) found that 8% of sampled industrial small businesses recorded an increase in revenue. The Swiss School of Business Research (2021) suggests that the pandemic may have spurred growth in the areas of digital technology adoption, cost savings, innovation, productivity, and business community expansion. According to Engidaw (2022), small firms experienced industry-specific problems and possibilities because of the COVID-19 crisis. Some industries benefited from the crisis, while others bore the brunt of the pandemic.

According to SMEDAN and NBS (2022), 79.4% of participants in their survey from 2021 said that COVID-19 had no beneficial effects on their companies. In addition, the survey revealed that the number of small businesses and their contribution to the GDP of Nigeria had declined by 4.5% and 3.5%, respectively, between 2017 and 2020. Nonetheless, a modest proportion of the respondents claimed that the pandemic had some positive impacts on their businesses, including increases in sales revenue (7%), new business opportunities (5%), and reduced costs of inputs (2.2%).

Individual and institutional researchers continue to explore the effect of COVID-19 on businesses in different parts of the world. While some have taken a sectoral approach (Dua *et al.*, 2020; Harel, 2021; Nordhagen *et al.*, 2023), others have been more generic in their investigations. In terms of methodology, many studies use a survey research design to answer research questions, accomplish research objectives, and test research hypotheses. The foregoing may be the case because the impact of the pandemic, though global, is contextual. Other studies have shed light on the various coping mechanisms of businesses during the health crisis (Adam and Alarifi, 2021; Mishrif and Khan, 2023; Rahman *et al.*, 2022).

Theoretical Synopsis

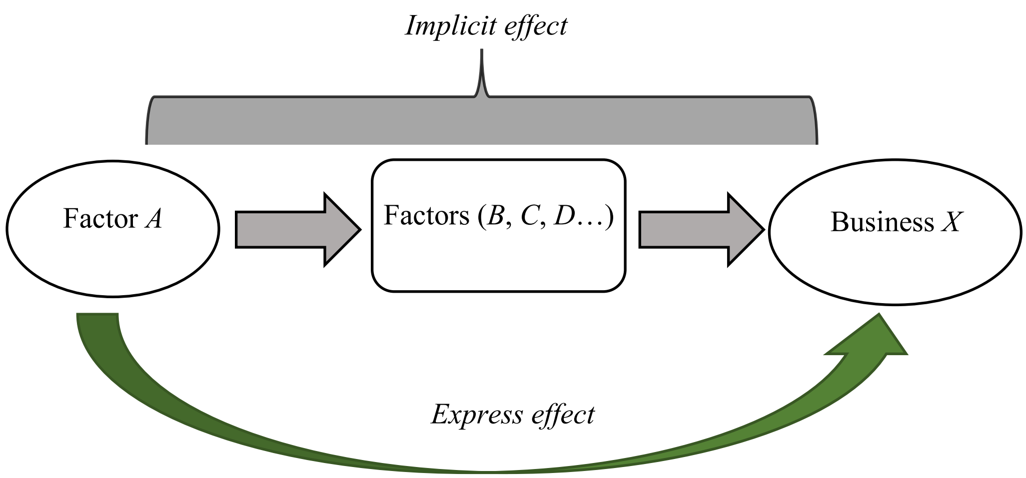
The business environment is a popular concept in business and management literature. The business environment is classified in a few different ways However, an overarching consensus is that the business environment can generally be segregated into internal factors and external factors. Conditions existing within the organisation that influences its operations are referred to as the internal environment. External factors, on the other hand, describe influences from outside of the organisation that impacts its operations.

PESTEL (political, economic, social, technological, environmental, and legal) analysis is one of the most popular techniques for assessing the external business environment. PESTEL can be traced back to Aguilar (1967), whose work focused on improving strategic management through environmental scanning. Since then, many authors have advocated for the use of PESTEL analysis by managers to understand the business environment and address the attendant threats and opportunities. These elements have long been assumed to have a one-dimensional impact on the firm. We propose a better pragmatic approach that considers these factors as having the potential to affect the firm on two fronts. We have termed the foregoing postulation the *Osaz Hypothesis*.

While the pandemic, at first sight, would easily be written off as an environmental factor, research and experience suggest that the effect of the COVID-19 crisis was multifaceted. Events such as government lockdowns had an *express effect* on small businesses. Meanwhile, (1) economic factors such as rising interest and inflation rates; (2) technological advancements such as the emergence of new technologies; and (3) political and legal actions such as trade restrictions could be classified as *implicit effects* of the pandemic on small businesses because they were mostly precipitated by the global health crisis. *Figure 1* is a simple diagrammatic representation of this idea.

Figure 1

Environmental Factor Impact Hypothesis



The significance of our proposition emphasises the importance and benefit of a root cause analysis. A single environmental component may act alone or operate indirectly through other factor dimensions within the environment. Decision-making and action in management need to be tied to establishing a root cause. Managers and entrepreneurs may make ineffective decisions and take invalid actions due to the lack of an established root cause. Adopting this approach to applying the PESTEL model has huge implications in the fields of finance and strategy management.

Methodology

This exploratory study aims to determine the proportion of small businesses affected by the breakout of the COVID-19 pandemic and the subsequent actions or lack thereof of the authorities and other relevant stakeholders. A simple percentage analysis was used to answer the following research questions:

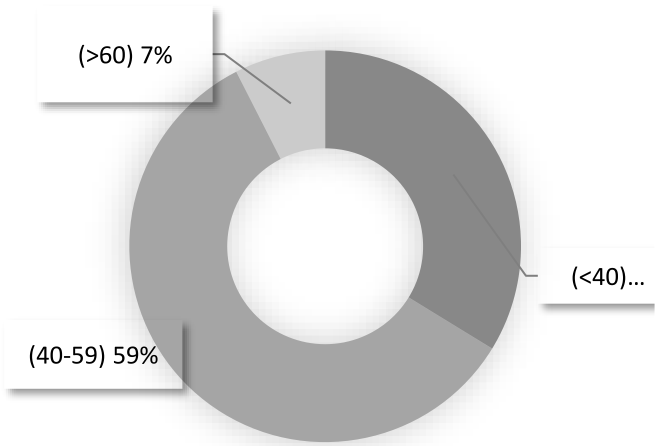
1. What percentage of Jos's small firms suffered a decline in earnings due to the COVID-19 pandemic?
2. What proportion of small enterprises in Jos metropolis experienced liquidity challenges due to the COVID-19 pandemic?
3. In terms of business debt, what percentage of Jos's small firms suffered because of the COVID-19 pandemic?

The sample points were selected without any consideration for the type of industry or the level of financial education of the business owners. These factors may have a moderating effect on the results obtained, thus constituting a limitation of our methodology. The data used for this study was collected through a survey conducted at the tail end of 2021, a period that arguably marked the start of recovery from the effects of the pandemic. The data collection instrument was a standard Likert scale questionnaire. The instrument items addressed three domains of business financial management, including profitability, liquidity, and debt management. A total of 80 businesses were surveyed using a simple random sampling technique. Nano and micro enterprises, according to the definitions by SMEDAN and NBS, were the focus of the study.

Results and Discussion

Figure 2

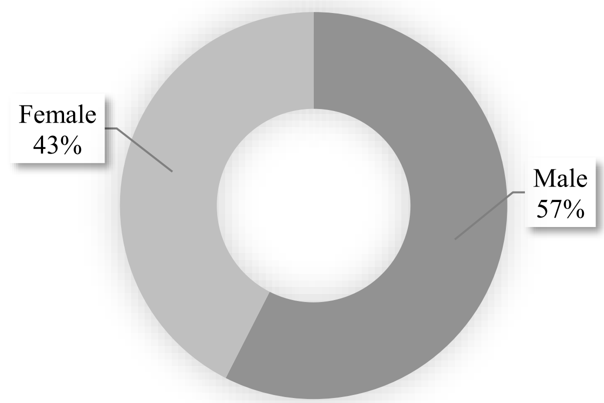
Age Distribution of Respondents



Field survey (2021)

Figure 3

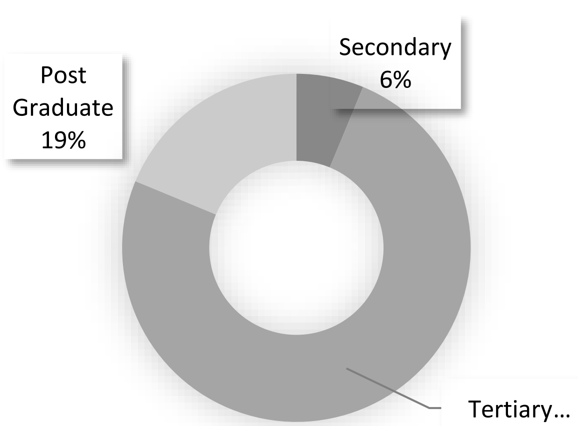
Gender Distribution of Respondents



Field survey (2021)

Figure 4

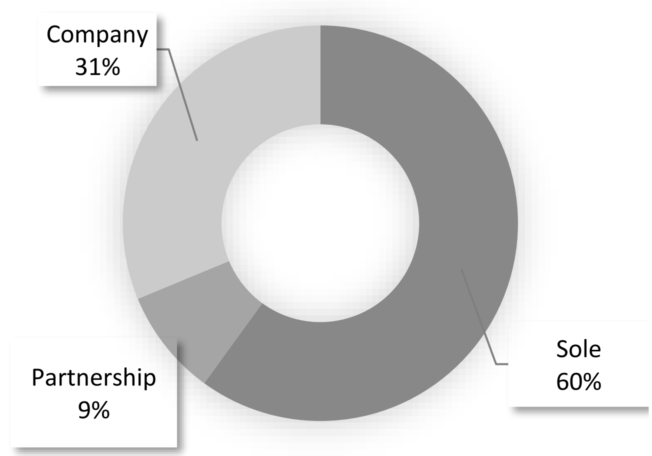
Highest Education Status of Respondents



Field survey (2021)

Figure 5

Business Legal Status



Field survey (2021)

Figure 2 reveals that more than half of the businesses surveyed were owned by entrepreneurs between the ages of 40 and 60 (59%). Above the age of 60, there is a sharp decline in the number of entrepreneurs. The foregoing is not unexpected, given the obvious limitations of individuals in this age group. When considering the ownership of small businesses by gender (*Figure 3*), males are slightly in the lead, with a ratio of 57% to 43% for females. *Figure 4* reveals that the sample was dominated by small business owners with qualifications higher than secondary education but lower than postgraduate education. This may suggest that tertiary institutions play a significant role in instilling an entrepreneurial mindset, as suggested by Aladejebi (2018) or it may point to the high rate of unemployment prevalent in Nigerian society (O'Leary, 2022). With regards to ownership structure, *Figure 5* shows that sole proprietorship is the most popular form of business, with 60%. This is lower than the 79% proportion reported for the same category by SMEDAN and NBS (2022). The sole proprietorship business form is likely preferred due to the ease of formation and operation.

Table 2

Response Analysis

							Mean	**Rank**
Profitability	Items	*Q1*	*Q2*	*Q3*	*Q4*	*Q5*		
	Proportion (%)	93	96	20	16	5	58%	2
Liquidity	Items	*Q6*	*Q7*	*Q8*	*Q9*	*Q10*		
	Proportion (%)	83	48	51	77	34	59%	1
Debt management	Items	*Q11*	*Q12*	*Q13*				
	Proportion (%)	89	30	20			46%	3

Table 2 is an analysis of the research instrument items. Q1–Q5 measured the impact of COVID-19 on profitability. Meanwhile, cash flow and debt were measured by items Q6–Q10 and Q11-Q13 respectively. The responses for each research item were analysed to determine the proportion of small businesses that were affected by the pandemic. Item Q11 recorded the highest negative impact on SMEs, indicating that over 89% of owners of SMEs in the sample were forced to inject personal funds into their businesses to keep them running during the COVID-19 pandemic. The least negative effect observed was in item Q5, under the profit domain, indicating that only 5% of the SMEs surveyed shut down business due to declining sales during the COVID-19 pandemic. The rank column indicates that the most significant area of impact of the COVID-19 pandemic on SMEs in the Jos metropolis was in the cash flow domain (59%). The least impact was observed in the debt management domain (46%).

Conclusion and Recommendation

The COVID-19 pandemic is largely considered a human catastrophe. The health crisis precipitated large-scale, dynamic changes in all facets of human life. Businesses and marketplaces may have suffered a massive blow from a global viewpoint. Nonetheless, there seem to have been some pockets of success and innovations to learn from. Like every shock, the pandemic brought with it new challenges and new opportunities. Challenges can be surmounted, and opportunities can be leveraged. Small business owners must get a financial education. This will help them survive and leverage the challenges posed by the business environment. When the odds are down, sound financial management is key to survival. In addition, adaptation and agility are the new characteristics that business owners must build into their structures and systems. The VUCA (volatile, uncertain, complex, and ambiguous) nature of the business environment will continue well into the foreseeable future. Are we ready?

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