

Effect of Social Capital on Transaction Costs of Small Enterprises in Sri Lanka

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Small Enterprises (SEs) have a higher failure rate due to various limitations mostly reflected in Transaction Costs (TCs). They fail to govern TCs in an economizing manner by using either 'Market' or 'Hierarchy' as suggested by the Transaction Costs Economics (TCE) due to the information and resource limitation. Instead, SEs develop informal and personal relationships with different members of the network expecting supports in order to overcome their resources and information limitations. The network relationships lead to build Social Capital (SC) (values of social relationships; i.e. Inter-personal trusts, relational norms, flexibility, integrity, common understand etc.) and thereby facilitate access to information and resources which have an influence on mitigating TC. However, the dearth of academic work studying how SC affects the TC, represents a significant gap in literature. Therefore, the study attempted to explore the effect of SC on TC particularly SEs in Sri Lanka. The study mainly employed the survey method and the data were collected from 373 SEs, selected using multi-stage sampling method to represent all Provinces in Sri Lanka, conducting face-to-face personal interviews with the respondents. The data were analyzed using Partial Least Squares-Structural Equation Modelling.

Results revealed that structural, relational and cognitive SC have a significant negative effect on TC of SEs. All the dimensions of SC have a negative significant impact on opportunism of exchange partners, positive significant effect on rational ability of the Owners of Small Enterprises (OSEs), significant negative influence on transaction uncertainty, positive significant impact on transaction specific assets and transaction frequency. The results further explained that the reasons for the TC and the determinants of TC have a significant mediate effect on the relationship between SC and TC of SEs. Thus, the study has provided sufficient evidences to conclude that SC has a significant impact on mitigating TC of SEs in Sri Lanka. The study contributes to theoretical knowledge by synthesizing all the dimensions of SC and all the variables of TC into a new framework and testing it empirically. This empirical contribution extends the TCE in the context of SEs in a LDC. The study contributes to the methodology quantifying SC of SEs using a multi-dimensional conceptual model. The study provides important insights for policy makers to focus their strategies to new direction rather than conventional supporting approaches to develop SEs.

Keywords: Small Enterprises, Social Capital, Transaction Costs