**Assessing The Influence of Economic Fluctuations on Performance of Small and Medium Enterprises in Hargeisa Somaliland**

**Abstract**

*This study examines the impact of economic fluctuations on performance of small and medium enterprises (SMEs) with particular focus on Hargeisa, Somaliland. SMEs are the backbone of Somaliland’s economy, providing the majority of employment and income, yet they remain highly vulnerable to economic cycles, internal conflicts, droughts, and trade disruptions. The research employs qualitative methodology, drawing insights from in-depth interviews with six SME managers across different sectors. The findings reveal that economic fluctuations-manifesting as exchanging rate volatility, inflation and reduced consumer demand – directly undermine SME profitability, operational stability and growth prospects. The research underscores the importance of government support, access to capital, and strategic adaptation to enhance SME resilience amid ongoing economic uncertainty. These insights contribute to a deeper understanding of the challenges facing SMEs in volatile economies and inform policy recommendations aimed at strengthening their sustainability and growth*

**Keywords:** *Fluctuation*, *exchanging rate volatility, uncertainty, consumer demand, currency depreciation*

**Introduction**

Both national and international economies grow and shrink like any living thing. The term "economic fluctuation" describes these shifts in a country's economy; an economy is considered to have grown or expanded when its national income rises, and to have contracted or receded when it falls (Robu, 2013). The GDP of Somaliland, an unrecognized country, is projected to be $1.4 billion, making it one of the world's poorest economies (World Bank & Ministry of National Planning and Development 2014).

With an estimated population of four million, the nation has the fourth-lowest GDP per capita income (PCI) in the world, ahead of Burundi, Malawi, and the Democratic Republic of the Congo, with an estimated PCI of $347 in 2012. Since import taxes and export levies accounted for more than half of total revenue in 2012, trade is vital. Meanwhile, Somaliland has one of the lowest budgets of any unrecognised nation in the world, with only a small portion going towards social development and the majority going towards defence (Mohamed, Mohamoud, & Farah, 2024). Somaliland's economy is highly unstable and susceptible to a variety of causes, such as internal conflicts, draughts, and embargoes on the export of cattle (Mal, 2017).

One important pillar of Somaliland's economy is SMEs. The economy is mostly dependent on SMEs because the little country is severely undeveloped and trailing behind in industrialisation. The majority of Somaliland's workforce is employed by SMEs, which also provide the majority of the country's disposable income and means of subsistence (Mohamed, Mohamoud, & Farah, 2024).

**Global and Regional Trends of Economic Fluctuations**

Global economies are dynamic and continuously go through cycles of expansion and contraction, as was previously mentioned. At the national level, employment, output, prices, investment, wages, and salaries all have an impact on these cycles. Events that occur locally, regionally, or internationally, such as draughts, disease outbreaks, conflicts, and changes in exchange rates, frequently contribute to these swings (Nguyen, Schinckus, & Thanh, 2020). SMEs must come up with creative ways to lessen the effects of these unfavourable circumstances and emerge from the recession. Advanced economies know how to survive during recessions, when demand and production levels decline (Benabed & Grunbichler, 2023).

Economic cycles are universal, according to a study that examined the G-7 nations, India, Malaysia, China, and the entire world during the Great Depression and the past 40 years. Each of the countries under study saw both positive and negative growth rates, typically spanning more than one year, during the study period. The study clarifies that, with the exception of times of severe worldwide economic downturns like the Great Depression, the departures from the typical course of economic fluctuations are not synchronised across nations (Gupta, 2003).

**The Impact of Recessions on SMEs**

The jobs, livelihoods, and security of a great number of people are negatively impacted by recessions and, more generally, by negative economic swings. In addition, it is a primary cause of SMEs' failure. The overall intensity of these swings has decreased recently, and national and international stabilisation policies have differing degrees of success in reducing this problem (Gupta, 2003). During recessions, one might anticipate a decline in sales, stagnant inventories, a bad return on investment, tighter financing, unpaid invoices, and insolvency. To survive during the challenging recession, it is the responsibility of each individual SMEs to have backup strategies for these risks.

Due to their smaller customer base, restricted loan availability, and limited resources, SMEs are particularly badly hit in these times. Since fixed expenditures like rent, electricity, and payroll can be far more difficult for SMEs to control than for bigger corporations with contingencies and fail saves specifically for these purposes, SMEs frequently face the challenge of managing their operating costs. SMEs have less bargaining power, or negotiation leverage, than larger companies, and are frequently more susceptible to supply chain interruptions.

**Riding the waves of economic boom: Opportunities for SMEs in Growth Periods**

In prosperous times, there are many opportunities for SMEs to grow, prosper, and make money. Consumer spending peaks in the early stages of economic recovery, when growth is high (Ludvig, 2004). In prosperous times, there is ample access to capital, whether from investors, credit, or grants. Francis Chittenden's article, which examined the financial structure of SMEs with a focus on growth and access to capital, concluded that growth of SMEs is directly correlated with access to capital (Chittenden, Hall, & Hutchinson, 1996). These opportunities can be used to improve small businesses' prospects for the future and establish their position in the market.

When the economy is doing well, it's a good moment for small businesses to establish their brand and grow. Each nation's development in the twenty-first century is correlated with the brands that export their impact abroad. Investment in national brands has a beneficial long-term impact on a country's economic growth, according to a study that looked at the relationship between the top 500 brand values and the growth rates of 38 nations between 2008 and 2017 (Okten, Okan, Arslan, & Gungor, 2019).

**Coping Mechanisms for SMEs to Deal with Economic Uncertainties**

For SMEs, diversification is vitally important. By growing their product or service, breaking into new markets, or creating new complementary items within their sector, small and medium-sized businesses can diversify. Based on the best complimentary sources obtained through the credit multiplier channel, SMEs can strategically choose to use a variety of financing sources (Chit & Rizov, 2024). For small businesses, cash flow management has been seen as essential to both their immediate and long-term survival. According to Uwonda and Okello (2015), poor cash flow management has been connected to the failure of numerous SMEs, jeopardizing their sustainability by depriving them of the cash flow required for expansion.

In order to stay competitive and secure the long-term viability of their firm, SMEs need to concentrate on meticulous cost control and management. Using a methodical approach to cost accounting and control procedures to optimise the value obtained from each resource is more important for effective cost management than just reducing expenses (Biadacz, 2022). Scenario planning is used by big, well-established companies to mitigate risks and create backup plans. It's a common misconception that SMEs can't implement and use the method. The attitudes of its managers, the financial limitations of SMEs, the managerial time orientation, and the complexity of the business are some of the obstacles preventing SMEs from implementing scenario planning (Nyuur, 2015).

**Government Policies and Economic Support for SMEs**

Governments must unquestionably assist their country's small businesses. Government financial aid is important for regional SMEs, and in today's network economy, it is important to establish strong social relationships, according to a 2014 study done in South Korea to examine the impact of government financial assistance on SMEs (Doh, 2014). In order to strengthen the ability of important institutions to assess, create, and carry out policies that promote private sector investments, small firm involvement in public procurement, and the general business environment, governments also undertake capacity building for SMEs (Harvie, 2004).

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**Objective of the Study**

To analyze the effect of economic fluctuation on performance of SMEs

**Literature Review**

Several studies have examined how economic fluctuation impacts small and medium enterprises (SMEs) performance. A study by Lagat and Auma in 2025 about the effect of external economic factors on the performance of SMEs in Nairobi County found that inflation rates, interest rates, and exchange rate volatility significantly affect SME growth and financial stability. High inflation increases operational costs, fluctuating interest rates limit access to affordable credit, and exchange rate volatility impacts import costs and profit margins.

Another study done by Sharma in 2022 about inflation and SMEs highlights how inflation has forced SME owners to reconsider pricing strategies, inventory management and operational costs. Rising costs due to global factors like the COVID-19 pandemic and geopolitical conflicts have made it harder for SMEs to remain profitable.

The World Economic Forum Report in 2022 found that **67% of SMEs globally** are struggling for survival due to recession fears, low profit margins, and difficulties in scaling their businesses. The report suggests that digital transformation and sustainability strategies can help SMEs improve resilience

**Methodology**

The study used a qualitative design to gain a deep understanding of the impact of economic fluctuations on performance of SMEs with a focus on the experiences of six SMEs managers from different business. The study employed a purposive sampling technique to select the six managers who had managed different business. Data collection was conducted through in-depth interviews, which provided participants with the opportunity to express their narratives authentically and in detail in secure and comfortable settings. The study’s ethical considerations were strictly adhered to, with all participants providing informed consent and understanding the study’s purpose and their rights, including privacy protection using unique code numbers to identify each participant. The transcribed interview data underwent rigorous analysis using thematic analysis, which involved several stages, including data familiarization, initial code generation, theme definition, and reporting.

**Results**

This study investigated the adverse effects of economic fluctuations on performance of SMEs settings. The research involved six managers from various businesses, providing a diverse perspective. The primary objective was to systematically identify and analyze the specific ways in which economic fluctuations influences performance of SMEs. The findings of the study have been carefully structured to align with and address the stated objective, offering a comprehensive understanding of the challenges and implications associated with economic fluctuations integration with performance of SMEs. Verbatim quotes from the participants were labeled as *‘Participant 1’, ‘Participant 2’, ‘Participant 3’*… and so on.

**Economic Fluctuations on Performance of SMEs**

Economic fluctuations profoundly affect the business operations of SMEs by introducing uncertainty and instability across multiple facets of their activities. When exchange rate are volatile, SMEs specially those engage in international trade, face significant negative impact on their revenue due to such volatility. As reflected from a quote from participant one:

*“The change in foreign exchange rates has greatly affected us. Some products, such as the packaging used for fish and refrigerators, are imported from abroad, so when the dollar rises, the purchase price increases, which reduces the profit……” participant 1.*

The quote highlights how fluctuations in foreign exchange rate, specially the rise of US dollars, directly impact the cost structure and profitability of a business that relies on imported materials. Since essential products like packaging for fish and refrigerators are sourced from abroad, an increase in dollar’s value means the local currency must be changed for more dollars to pay the same amount. This caused the purchase price of this imported inputs to rise, increasing overall production costs. Because these higher costs reduce profit margins, the business either has to absorb the extra expense, which lowers profitability or pass the costs on to customers, which may affect demand. In essence, the quote illustrates the vulnerability of business dependent on import to foreign exchange rate fluctuations and how such changes can squeeze profit by making imported goods more expensive.

Economic instability often leads to significant reduction in customer demand, which directly affects business operations, especially for SMEs. During periods of economic downturn or recession, consumers typically face job insecurity, stagnant or declining wages, and reduced disposable income, prompting them to cut back on spending, particularly on non-essential or discretionary goods and services. This drop in consumer confidence and purchasing power results in fewer customers in business, causing sales to slump and revenues to decline. As reflected from a quote from participant two:

*“Yes, many customers who used to regularly purchase software and hardware maintenance services have now started to avoid them because they are prioritizing basic necessities …..” participant two*

The quote illustrates how economic pressures influence consumers spending priorities, leading to a decline in demand for certain business services. Specially, customers who previously purchased software and hardware maintenance services regularly are now cutting back on these expenditures. Instead, they are focusing on their limited financial resources on essential needs such as food, housing and healthcare. This shift reflects common response during times of economic hardship and instability, where non-essential expenses are postponed or eliminated to preserve cash or basic necessities.

Adjusting a pricing strategy to economic fluctuations or any other economic situation is not just advisable, but it is often essential for business survival and growth. Economic conditions such as inflations, supply chain disruptions, changes in consumer demand and regulatory shifts can dramatically affect both company’s costs and its customer’s willingness to pay. As reflected a quote from participant three:

*“Yes, I have lowered the prices of some services, such as sewing light clothing, and I offer discounts during busy periods. I have also categorized the services into levels: "regular sewing" and "high-quality sewing ….” participant three.*

The statement from the participant demonstrates that a thoughtful and strategic pricing strategy tailored to market conditions and customer needs. By lowering the prices of certain services like sewing light clothing, you make your offerings more accessible and competitive, which can attract price sensitive customers and increase your overall customer base. Offering discounts during busy periods is also smart move, it helps to manage the demand, fill your schedule efficiently, and reward your loyal clients, all while maintaining a steady flow of income.

Reduction of customer demand and economic fluctuations are closely related because economic conditions directly influence consumers’ purchasing power, confidence, and spending behavior. When the economy experiences fluctuations such as rising inflation, higher interest rates, or increased unemployment, consumers typically face reduced disposable income and greater uncertainty about their financial future. This leads to consumer confidence and decline in discretionary spending causing demand for many goods and services, especially non-essential or luxury items to decrease. As reflected a quote from participant four:

*“Yes, when the value of the shilling decreases, the prices of goods change accordingly. This also affects the economy, which in turn impacts the customers, causing a decrease in the number of customers and a decline in the business's profit…….” Participant four*

This statement explains the chain reaction that occurs when the value of the shilling, the local currency, decreases - commonly known as currency depreciation. When the shilling loses value, imported goods and raw materials become more expensive because it takes more shillings to buy the same amount of foreign currency. As a result, businesses face higher costs, which often leads them to increase the prices of their goods and services to maintain profitability. These prices increase affect the overall economy by reducing consumer’s purchasing power, meaning customers can afford to buy less than before.

Having a plan for future economic uncertainties is highly beneficial and often critical for business resilience and long-term success. Economic fluctuations such as recessions, inflation spikes, supply chain disruptions or geopolitical tensions can unpredictability impact revenues, costs and customer demand. By proactively developing contingency plans, businesses can establish clear, actionable responses to various scenarios before crisis occur. This includes defining specific triggers for an action such as thresholds for rising input costs or falling sales, and assigning decision-making authority to ensure swift, coordinated responses. Such preparedness reduces delays overreactions when disruptions happen helping to maintain operational stability. As reflected the quote from participant five:

*“I am planning to start sourcing my products such as clothes, thread, and local fabric from the domestic market. I am also working on marketing tailored clothes online to reach customers outside the city, which can reduce the impact of economic fluctuations…” participant five*

The statement demonstrates plan to source products like clothes, thread and local fabric from the domestic market, combined with marketing tailored clothes online to customer outside the city, reflects a strategic approach to building more resilient and adaptable business model. By purchasing materials locally, you reduce your dependence on imports, which can be vulnerable to currency fluctuations, international supply chain disruptions and increased costs due to tariffs or shipping delays. This local sourcing can stabilize your input costs and improve supply reliability, making your business less sensitive to global economic uncertainties.

**Discussion**

**Impact of Economic Fluctuations on SMEs and Strategic Responses**

The statements and participant quotes provided offer comprehensive insights into how economic fluctuations profoundly affect the operations, costs, demand and profitability of SMEs. They also highlight practical strategies businesses adopt to navigate these challenges, emphasizing the critical need for adaptability and resilience in uncertain economic environments.

**Impact of Foreign Exchange Volatility on Costs and Profitability**

Participant one’s quote vividly illustrates the direct impact of foreign exchange rate fluctuations on SMEs that rely on imported inputs. When the US dollar appreciates against the local currency, the cost of imported goods such as packaging materials and refrigerators rises sharply. This increase in input costs squeezes profit margins unless businesses can pass the higher costs onto customer. However, rising prices risks reducing demand, placing SMEs in difficult position. This scenario underscores the vulnerability of import dependent businesses to currency volatility and highlights the importance of managing foreign exchange risks, possibly through hedging or sourcing alternative.

**Economic Instability and Reduction in Customer Demand**

Participant two’s observation about customers cutting back on non-essential services like software and hardware maintenance during economic downturns reflects common consumer behavior pattern during recession or periods of financial uncertainty. Job insecurity, stagnant wages and reduced disposable income lead customers to prioritize essential goods over discretionary spending. This shift causes decline in demand for many SME services and products, resulting in lower sales and revenue. The quote emphasizes the ripple effect of economic instability on consumer behavior and consequently on business performance.

**Importance of Adaptive Pricing Strategies**

Participant three’s approach to adjusting pricing by lowering prices for certain services and offering discounts during busy periods demonstrates a proactive response to changing market conditions. Categorizing services into different quality levels (“regular” and “high quality”) allows the business to cater to diverse customer segments and price sensitivities. This tiered pricing strategy not only attracts broader customer base but also helps manage demand and maintain steady cash flow. It exemplifies how SMEs can use pricing flexibility as a tool to remain competitive and profitable amid economic fluctuations.

**Currency Depreciation and Its Broader Economic Effect**

Participant four’s statement about the depreciation of the shilling highlights the broader economic consequences of currency devaluation, as the local currency weakens, imported goods become more expensive, leading to higher prices across the market. This prices increase reduces consumer’s purchasing power, causing a decline in customer numbers and business profit. This chain reaction illustrates the interconnectedness of currency value, inflation, consumer behavior, and business viability. It also stresses the importance of SMEs to monitor currency trends and consider strategies to mitigate their impact.

Strategic Planning for Economic Uncertainties

The insight from participant five about sourcing locally and expanding online marketing efforts reflects forward thinking-strategy to build business resilience. By sourcing materials domestically, SMEs can reduce exposure to foreign exchange risks, import delays, and tariff-related costs increases. Local sourcing stabilizes input costs and enhances supply chain reliability. Additionally, marketing tailored clothes online to customer outside the city diversifies the customer base and reduces on local economic conditions. This geographic expansion can help smooth revenue fluctuation caused by regional economic downturns. The participant’s plan exemplifies how SMEs can adopt their supply chain and marketing channels to mitigate the adverse effects of economic instability.

**Overall Implication**

Together, these statements paint a clear picture that economic fluctuations introduce multifaceted challenges for SMEs, affecting costs, demand, pricing strategies and overall profitability. The quotes reveal that SMEs are not passive victims of economic forces but actively employ various strategies such as pricing adjustments, local sourcing, market diversification and contingency plan to navigate uncertainty.

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