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Potential of Joint Stock Companies for SME Financing: Assessing Awareness, Constraints, and Policy Implications in Pakistan

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Abstract: *Investment is crucial for smooth execution of operations within the organization and the scarcity of the mentioned resource not only suspends the operations but also result in shutdown of companies, if the problem persists. This clearly demonstrates the severity of its importance. Availability of finance has always been a greater issue for third world countries because of low per capita income and consequently fewer saving. High inflationary rates decrease monetary worth and in turns greater money requirement for the establishment of organizations. With the globalization, no single firm can operate domestically without being in competition with multinational giants. The difference in investments makes the domestic organizations more vulnerable and the global companies a real threat to them. Share stock is an important mode of financing that facilitates establishment of large-scale manufacturing organization as well as provide common men the opportunity to invest. Joint Stock Companies may play a significant role in resolving the issue, however, the lack of awareness about stock market mechanism and negligence in less developed countries towards establishment and promotion of JSCs is a major impediment in reaping the benefits of mentioned mode of financing. The research aims to highlight the potential of share as a mode of financing i.e. development of joint stock companies in Islamic or the third world countries and also the impediments that restrict their growth as well. The research aims to help in devising policies expected to accelerate stock market operations thus benefiting investors, entrepreneurs, financial institutions and consequently the whole economy.*

Introduction

Economic instability is one of the major challenges for less developed, third world countries that leads to many other uncontrollable social and societal problems. Population growth without economic growth not only triggers unemployment, inflation and economic instability but the prevailing poverty also gives rise to chaos, crime and lawlessness (Hussain & Ahmad, 2021). Peace, harmony and economic stability remains a question for third world country due to the same reasons. The economic growth of a country depends on the growth of its corporate sector. To achieve the economic prosperity, the government makes policies for the industrial development. Hence the establishment of a stable corporate sector is a major concern of every government (Khan & Anwar, 2019). Though most of the countries find it difficult to accomplish the objective due to multiple macroeconomic factors that is also evident by their stagnant or restricted growth rate (Hussain & Ahmad, 2021). Based on economic prosperity, the whole world is divided into three categories that is the world developed nations, the developing ones and the underdeveloped. The developed countries are those whose companies have not only conquered their domestic market but have also captured the market globally. Developing ones are striving to align with the developed ones. However, the underdeveloped are way behind the developed or the developing ones in terms of economic prosperity, that not only affects their consumption/ spending but also their saving and investment capacities (World Bank, 2015). High per capital income contributes to high savings that consequently motivates people to invest (Khawaja, 2020).

Developing countries are struggling hard for the development of SME based economy as they are easy to establish and provide employment. However, their small size and limited capital make them vulnerable to the growing competition especially with giant MNCs all over the world. Unavailability of finance stimulates many other problems for SMEs including liquidity issues, inability to achieve economies, lack of R&D and access to latest technology (World Bank, 2015). All these factors negatively influence the growth of SMEs and result in decline of the local industry. World Bank (2015) also declared lack of access to investment as one of the major obstacles to the growth of SMEs all over the world. The problem is magnified in less developed countries despite their entrepreneurial potential, as these financial constraints ultimately restrict the ability of Intrapreneurs and Business graduates to pursue their dream of becoming an entrepreneur (Khawaja, 2020).

The establishment of a prosperous corporate sector will help third world countries to manage finances and resolve their investment issues without dependence on foreign aid or assistance. Availability of investment is among major obstacle for SMEs regardless of entrepreneurial potential (Hussain & Ahmad, 2021). This ultimately makes them more dependent on foreign assistance or aid. Share stock is an important mode of financing that facilitates establishment of large-scale manufacturing organization as well as provide common men the opportunity to invest. Joint Stock Companies may play a significant role in resolving the issue, however, the unawareness about stock market mechanism and negligence in less developed countries towards establishment and promotion of joint stock companies is a major impediment in reaping the benefits of mentioned mode of financing (Khan & Anwar, 2019). In developing economies like Pakistan, entrepreneurial potential remains underutilized due to limited access to finance, lack of supportive policy frameworks, and weak institutional linkages (Masroor & Tabassum, 2022; Hussain & Ahmad, 2021). Encouraging investment through the formation of joint stock companies could therefore contribute to broader economic stability (Masroor & Tabassum, 2022).

Statement of the Problem

Investment is crucial for smooth execution of operations within the organization and the scarcity of the mentioned resource not only suspends the operations but also result in the shutdown of companies, if the problem persists. This clearly demonstrates the severity of its importance. Availability of finance has always been a greater issue for third world countries because of low per capita income and consequently fewer saving. High inflationary rates decrease monetary worth and in turns greater money requirement for the establishment of organizations. With the globalization, no single firm can operate domestically without being in competition with multinational giants. The difference in investments makes the domestic organizations more vulnerable and the global companies a real threat to them.

Despite several sources of financing options such as loans, microfinance schemes, shares etc., the availability of investment is a challenge for most of small companies especially in third world countries.

Availability of investment is among major obstacle for SMEs regardless of entrepreneurial potential. This ultimately makes them more dependent on foreign assistance or aid. Share stock is an important mode of financing that facilitates establishment of large-scale manufacturing organization as well as provide common men the opportunity to invest without being dependent on foreign aid and jeopardizing national sovereignty. Joint Stock Companies may play a significant role in resolving the issue of availability of investment, however, the lack of awareness about stock market mechanism, legal policies and negligence in less developed countries towards establishment and promotion of JSCs is a major impediment in reaping the benefits of mentioned mode of financing.

Objectives of the Study

The objectives of the study are as follows:

- To highlight financial issues for SMEs in less developed countries
- To understand and highlight the social and economic benefits of Joint Stock Company as feasible mode of investment for less developed countries.
- To understand the barriers restricting establishment and growth of joint stock companies in less developed countries.

Scope & Significance of the Study

Lack of availability of investment is the major obstacle behind stifled growth of companies especially in less developed countries. The research highlights the scope of Joint stock companies in managing finance for capital intensive organizations in Islamic as well as third world countries without being dependent on foreign assistance. The research will assist in designing policies expected to stimulate stock market operations thus benefiting investors, entrepreneurs, financial institutions and ultimately the whole economy. The research aims to highlight the potential of share as a mode of financing i.e. development of joint stock companies even as SMEs in Islamic or the third world countries and also the impediments that restrict their growth as well. The research will be helpful in devising policies expected to accelerate stock market operations thus benefiting investors, entrepreneurs, financial institutions and consequently the whole economy.

Literature Review

Joint Stock Company is a type of organization that provides the benefit of gathering finances from the market in form of easily transferable securities i.e. Shares & debentures. Several distinctive features differentiate Joint Stock Company from the other forms of organizations i.e. sole proprietorship or partnership (Hussain & Ahmad, 2021). Some common benefits of joint stock companies include limited liability, double taxation contributing government revenues, variety of goods to the customers in the market at competitive cost because of mass production and advance technology and provision of employment on vast scale as compared to other forms of business organizations (Khan & Anwar, 2019).

Availability of investment has always been a major hurdle behind stifled growth of business entities in less developed countries that stems from limited income and lack of savings (World Bank, 2015). The total capital in a joint stock company comprises of shares whose value can be defined based on the affordability of the investors. The mechanism facilitates gathering of investment from the market that is capital formation easier for the establishment of entities (Masroor & Asim, 2023). Moreover, certain manufacturing organizations cannot be established as sole proprietorship or in partnership due to its huge amount of investments that are beyond capacity of people. A joint stock company provides you ease in the development of capital intensive organizations by facilitating accumulation of investment required by the company and authorized by the government. Even small & medium entreprises (SMEs) while in competition with giant multinational corporations needs to be financially self-sufficient to remain competitive in the market (Rehman & Naeem, 2020).

Not every individual has the business acumen neither everyone is a risk taker. People opt to being employed rather being an entrepreneur due to their lack of managerial skill or limited professional knowledge. The limited professional ability leads to risk avoidance and shift towards ordinary and traditional means of investment with low risk including investment in gold, land, or currency with higher and stable value like dollar etc (Kefela, 2011). Joint stock companies serve as a secure and halaal mode of investment for such people. Although banks also provide an opportunity to invest but in Islamic countries, the investment in banks remain a controversial and debatable issue due to interest being 'haram' (formidable) in Islam whereas shares are permissible (halal) due to the association of profits as well as losses in them (Ahmad, Rauf, & Rashid, 2011). Therefore, investment in shares can be considered as convenient and affordable form of investment for those who have savings but unable or unwilling to establish their own business including illiterate people, employed people, household women or students (Masroor & Asim, 2023).

Economic inequality is another most common worldwide social problem. Many countries are striving hard to maintain equality and reduce power distance in the society (Hofstede, 1980) and have made the objective the part of their MDG's (Millennium Development Goals). A Joint Stock Company helps maintain equality by providing distributed profits and losses among the number of people (shareholders) as the investment in Joint Stock Company is gathered from the masses in a market, therefore, the benefit in the form of dividend or the loss is also distributed among all of them promoting financial inclusiveness and equality (Khan & Anwar, 2019; World Bank, 2015).

Furthermore, the establishment of a single company accelerates the economy through multiplier effect. The employment creation by establishment of a single company leads to increased purchasing power of the people thus paving way for stimulated demand. Moreover, the establishment of a company also results in increased demand of raw material, distribution channels etc., therefore, the Joint Stock Company, due to its bigger size and vast production, generates spillover benefits on vast scale for associated companies like suppliers, distribution channels etc. thereby boosting economic growth on a wider continuum (Masroor & Asim, 2023; Hussain & Ahmad, 2021).

Figure 1: Benefits of Joint Stock Company to the Society

Based on the earlier discussion the fact is already established that joint stock company has several benefits not only as a form of organization but also as a mode of investment (Hussain & Ahmad, 2021). Specially, in the less developed and third world countries where scarcity of investment has always been a major cause behind the stifled growth of companies, share market can play a pivotal role in the resolution of the issue (Khan & Anwar, 2019). However, despite numerous benefits and its potential in providing investment that would consequently lead to economic growth, there are multiple hindrances as well behind the establishment of joint stock companies and their potential as a mode of investment for common men (World Bank, 2015).

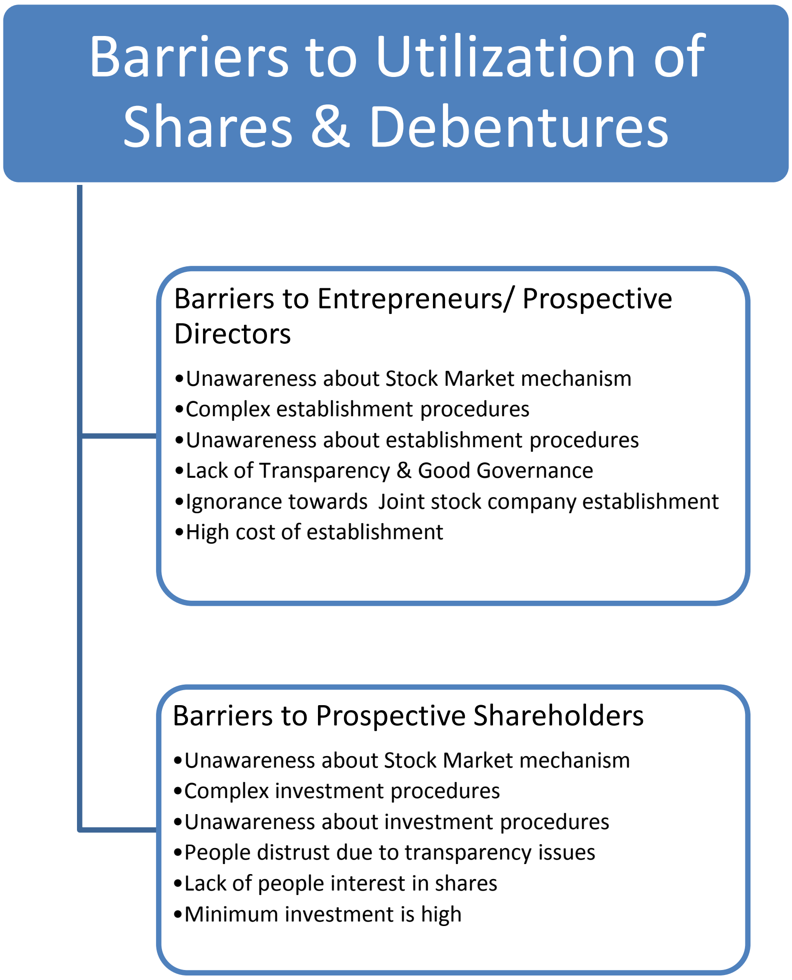

Figure 1: Barriers to Utilization of Shares as Mode of Investment

The characteristics of a joint stock company are distinct from those of sole proprietorship or partnership and are also the foundation of its several benefits (Hussain & Ahmad, 2021). However, the similar features can also become the obstacles if not managed properly such as transparency & governance issues, that plays a key role in investors' confidence and are particularly critical in emerging markets like Pakistan (Rehman & Naeem, 2020). The following discussion highlights factors impeding growth of joint stock companies in Pakistan.

The characteristics of a joint stock company are quite different as compared to other forms of organization including sole proprietorship or partnership. In a joint stock company, the people who manage the company are separate from those who owned that is shareholders (Berle & Means, 1932; Hussain & Ahmad, 2021). Although this characteristic facilitates the organization in gathering large capitals from the market to establish capital intensive organization, still the same separation of ownership from management also gives rise to many other critical issues including transparency and governance being the most crucial one (Jensen & Meckling, 1976).

Especially in third world countries and less developed nations, where compliance to law and order situations is already compromised, it is hard to earn investors' confidence and trust. The problem is further enhanced and restricts people from investing in the stock market. In developing and less developed nations, where compliance with legal and regulatory frameworks is often weak, maintaining investor confidence and trust becomes particularly challenging (Rehman & Naeem, 2020). Weak enforcement of governance standards and limited financial literacy further exacerbate these issues, restricting people's willingness to invest in stock markets (Khan & Anwar, 2019; World Bank, 2015). These challenges collectively hinder the broader development of capital markets and the growth of joint stock companies in such economies (Hussain & Ahmad, 2021).

Similarly, another issue that comes out of the characteristics of joint stock companies is the legal requirements it takes to establish one. As we have already discussed earlier, that in the joint stock company, the management is separate from the ownership. That gives rise to the need of proper registration procedures to be followed and the documentation to be done. Although the objective is to safeguard the rights of shareholders, however in the countries where the literacy rate is already below par, the cumbersome legal registration and investment procedures only proves to be a deterrent for the majority of the people. These policies not only include the registration procedures but also extend to minimum investment requirements, taxation policies etc. The outcome of such policies have their own repercussions as these complicated procedures, with low literacy rate in combination with lack of awareness about stock market mechanisms play a very crucial role in the downfall of companies by restricting people from establishing or investing in the organizations.

Another significant issue arising from the structural characteristics of joint stock companies relates to the legal and procedural requirements necessary for their establishment. As discussed earlier, in a joint stock company, management is separate from ownership, which necessitates compliance with formal registration and documentation procedures (Hussain & Ahmad, 2021). While these legal frameworks aim to safeguard shareholder rights and enhance corporate transparency, in countries with low literacy rates and weak institutional capacity, the cumbersome procedures often act as deterrents to potential investors ((Masroor & Tabassum, 2022 ; Khan & Anwar, 2019).

These regulatory barriers include lengthy registration processes, minimum capital requirements, and complex taxation policies, all of which discourage entrepreneurship and the establishment of new ventures ((Masroor & Tabassum, 2022; World Bank, 2015). The cumulative effect of these policies is evident in developing nations like Pakistan, where limited financial literacy, coupled with a lack of awareness about stock market mechanisms, restricts public participation in equity investments and, consequently, hinders the growth of corporate enterprises (Rehman & Naeem, 2020; (Masroor & Tabassum, 2022).

Methodology

The major obstacle against the development of an organization in under developed economies is their lack of access to finance and investment. This is a descriptive research identifying and highlighting the potential of Joint Stock Company and the reasons behind its backwardness in such countries. For the purpose, a research questionnaire based on the investment problems for SMEs along with establishment and execution issues for Joint Stock companies was administered to 150 entrepreneurs and directors in Pakistan. This is descriptive research conducted with the purpose of finding the potential of joint stock companies in third world countries along with the factors posing as a threat to their growth. Based on other studies of similar nature, a non-probability convenience sampling method was selected to gather data. A questionnaire was administered to 150 entrepreneurs in Pakistan to verify the problems faced by them and prevalent in the less developed countries restricting the establishment and growth of joint stock companies.

The major obstacle to organizational development in underdeveloped economies is the limited access to finance and investment opportunities (World Bank, 2015; Beck & Demirgüç-Kunt, 2006). This study is descriptive in nature, designed to identify and highlight the potential of joint stock companies as well as the reasons behind their underdevelopment in such economies (Hussain & Ahmad, 2021). For this purpose, a structured research questionnaire focusing on investment challenges faced by small and medium enterprises (SMEs), along with the establishment and operational issues of joint stock companies, was administered to 150 entrepreneurs and company directors in Pakistan. The study adopted a non-probability convenience sampling method, consistent with similar studies exploring entrepreneurial and SME financing issues in developing economies (Etikan et al., 2016; Khan & Anwar, 2019).

The data collection approach aimed to capture the perceptions of business owners and corporate professionals to better understand the investment barriers and structural constraints that limit the establishment and growth of joint stock companies in Pakistan and other less developed countries (Rehman & Naeem, 2020). The questionnaire was based on Likert scale measuring the level of issues from “Very Low” to “Very High”. The data is analyzed using multiple descriptive measures whereas non-parametric binomial testing was used to testify the significance of variables obstructing establishment and growth of Joint stock companies in Pakistan. All the factors that were identified as impediments to establishment and growth of Joint Stock Companies were made the part of questionnaire. The responses were meant to take the opinion of entrepreneurs about the level of impact of the factors i.e. to what extent do they pose risk to Joint Stock Companies from “very low” level to “very high” level risk.

Data Analysis & Discussion

Keeping the nature of the research in perspective, which focuses on identifying the prospects and barriers for joint stock companies in less developed countries, responses were gathered from 150 entrepreneurs and SME operators in Pakistan. Efforts were made to collect data from a diversified sample of SMEs, including both manufacturing and service organizations. Based on the responses, the gathered data was found highly consistent, as the value of Cronbach’s alpha was above 0.818, reflecting strong reliability and consistency of the applied tool and measured variables (Cooper & Schindler, 2014; Saunders, Lewis, & Thornhill, 2019).

As discussed earlier in the methodology section, the questionnaire was structured using a Likert scale designed to identify the perceived impact of various issues on a continuum ranging from “very low” to “very high.” The objective was to identify the impediments restricting the establishment and growth of joint stock companies, both as a form of business entity and as a mode of financing for capital-intensive organizations. The factors discussed in the literature review were analyzed using non-parametric binomial testing to assess their statistical significance and directional. The responses from “very low” to “low” were combined together in Group 1 whereas the responses from “moderate” to “very high” were tied as Group 2. The data was analyzed at 95% confidence interval to ensure greater significance.

According to the results in Table 1, all the factors were found highly significant at 95% confidence interval. As the factors were identified under two different perspectives; one as an entrepreneur and the other as an investor however, the responses were taken without categorizing the factors in categories as few of the factors were part of both. That included Unawareness about stock market mechanism, People distrust due to transparency issues and Lack of people interest in stock/ shares market. However, the others were distinguished on the basis of entrepreneurs versus investor's side as the role of both stakeholders is separate in Joint stock companies.

Among the factors that were considered major impediments for joint stock companies by the respondents were unawareness about establishment procedures in joint stock Company with a greater proportion of 88% whereas 12% considered it low risk. 91% respondents suggested complex establishment procedures of a joint stock company pose as moderate to high level risk for them. The results also indicated the fact that there exists greater unawareness about Stock market mechanism in the market. 87% people endorsed the fact that there exists greater unawareness by selecting it as a factor that has moderate to high level negative impact on Joint Stock Companies whereas the remaining 13% considered it a negligent factor with low level impact. The high level proportion of the mentioned factors also justify the high percentage of the other factor i.e. Lack of people interest in share/ stock market because if you don't have much awareness about the mechanism, how can you be interested in that.

Similarly, there were other factors that were identified on the investors'/ shareholders side as barriers to their access. Beside the unawareness about stock market mechanism, other factors included complicated procedures for investment in shares, unawareness about the investment procedures, trust and transparency issues, and nonetheless high requisition of minimum investment. The results indicated higher significance level for all factors. 85% people identified complicated procedures as a major issue for prospective shareholders restricting them from investment whereas 91% identified unawareness about investment procedure in share market as a barrier to shareholders' investment. The results revealed a greater need of increasing awareness to about people about stock market mechanism and also to bring ease in the investment procedures to encourage investment.

Table 1: Non-Parameteric Binomial Test

	Binomial Test: Issues for Joint Stock Companies/ Barriers to shares as Mode of Investment						
			Category	**N**	**Observed Prop.**	**Test Prop.**	**Exact Sig. (2-tailed)**
Shares	**Unawareness about establishment procedures of Joint Stock Company**	**Group 1**	**<= 2**	**18**	**.12**	**.50**	**.000**
		Group 2	**> 2**	**132**	**.88**		
		Total		**150**	**1.00**		
	Complex establishment procedures of a joint stock company	**Group 1**	**<= 2**	**13**	**.09**	**.50**	**.000**
		Group 2	**> 2**	**137**	**.91**		
		Total		**150**	**1.00**		
	Unawareness about stock market mechanism	**Group 1**	**<= 2**	**19**	**.13**	**.50**	**.000**
		Group 2	**> 2**	**131**	**.87**		
		Total		**150**	**1.00**		
	Lack of people interest in stock/ shares market	**Group 1**	**<= 2**	**20**	**.13**	**.50**	**.000**
		Group 2	**> 2**	**130**	**.87**		
		Total		**150**	**1.00**		
	Unawareness about investment procedure in share market	**Group 1**	**<= 2**	**13**	**.09**	**.50**	**.000**
		Group 2	**> 2**	**137**	**.91**		
		Total		**150**	**1.00**		

	People avoidance of buying shares/ non- trust on legal compliance/ transparency of share market	Group 1	<= 2	14	.09	.50	.000
		Group 2	> 2	136	.91		
		Total		150	1.00		
	Complicated Procedures for investment in shares	Group 1	<= 2	23	.15	.50	.000
		Group 2	> 2	127	.85		
		Total		150	1.00		
	non encouraging Investment procedures in share market for common people	Group 1	<= 2	27	.18	.50	.000
		Group 2	> 2	123	.82		
		Total		150	1.00		
	Minimum investment requirement in share market is beyond capacity of majority of people in Pakistan	Group 1	<= 2	24	.16	.50	.000
		Group 2	> 2	126	.84		
		Total		150	1.00		

Similarly, 91% people identified lack of trust on transparent operations of stock market mechanism as a higher risk problem indicating the need to ensure legal compliance and resolve transparency issues by following good governance practices. In Pakistan, lack of trust is one of the main reasons behind people lack of interest in shares despite its potential. Family ownership is comparatively more successful due to the same. Meanwhile, another problem that posed as a big problem for the common people was the minimum investment requirement for them. 85% respondents considered the factor as a major problem for the people restricting them from being investor. For all nine factors, Group 2 responses exceed 80%, confirming that respondents overwhelmingly consider these issues moderate to highly impactful on the underdevelopment of JSCs. These results empirically support previous literature highlighting that legal complexities, limited awareness, lack of transparency, and financial inaccessibility are key deterrents to corporate sector expansion in Pakistan (Hussain & Ahmad, 2021; World Bank, 2015).

Conclusion

Joint Stock Company is an important form of organization that has several benefits including the ability to develop capital intensive organizations being the most important and many others discussed earlier. Based on the aforementioned discussion, we can conclude that availability of finances through personal sources is mostly scarce in the less developed nation whereas the borrowed financing has its own repercussions due to overall economic depression and uncertainty in such countries limiting the leverage benefit and increasing the chances of bankruptcy for the organizations. The inability of the mentioned sources of investment restricts the entrepreneurs from playing the fields therefore emphasizing the need and potential of joint stock companies enabling the entrepreneurs the accumulation of capital investment by means of introducing shares in the market. It not only provides potential investment opportunity to entrepreneurs but also provide common men the opportunity to invest excess funds promoting equality and economic growth in the society. However, the stock market operations were found to have their own obstacles including unawareness and complicated procedures being the most dominating ones.

Policies are always designed to bring ease to the stakeholders. Similarly, the objective of the policies in operations in Joint Stock Companies should be to bring ease to the entrepreneurs or investors whether in the establishment or the investment procedures. However, the reality is contrary to the desired objectives. The results clearly indicated the need of improvements in the curriculum to increase awareness and motivation in Pakistan. The notion should be kept under consideration that the awareness about joint stock companies is not limited to management and business studies rather a basic understanding of the mechanism is a must for every individual to ensure their personal growth and to promote investment in companies. Financial literacy is the right of every individual as it ensures economic growth and prosperity. In Pakistan, the unawareness about the financial institutions reflect a huge gap that needs to be overcome. Banks as a financial institution and investment opportunity are not widely accepted in Islamic country like Pakistan due to debate about interest being 'Haram' that ultimately limits investment opportunities for common men and consequently lead to inflation on a widespread level.

Another factor was also recognized by the results that besides unawareness about share market procedures and stock exchange mechanisms, complicated rules & regulations also play a substantial role behind limited potential of Joint Stock Companies in Pakistan. The impact is further intensified due to low level of literacy in the society. Education has always been a critical issue in less developed countries. People are not mostly aware of consumer, employees or even basic human rights. It is, therefore, understandable, that a lot of people are not able to comprehend the rules and regulations and if these complicated procedures are restricting people from using Joint Stock Companies or shares as a tool for financial gain. Bringing ease in the policy and procedures will not only bring ease to potential investors but is also likely to encourage investment in the economy.

Transparency and good governance are also among major drivers that boost up people confidence. However, it is also among the main obstacles in less developed countries due to lack of legal compliance. In countries with weak legal environment, mostly the family owned companies are able to prosper because of having limited transparency issues. For the development of strong corporate sector, transparency and disclosure must be ensured to maintain investors' confidence. The removal of barriers to the growth and stability of joint stock companies will boost economic growth and prosperity, pave way for capital intensive manufacturing organizations, reduce dependency on foreign aid for high investment projects and nonetheless provide employment on vast scale.

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