UNIVERSITY OF KWAZULU-NATAL

INYUVESI YAKWAZULU-NATALI

THE ROLE OF THE DFIs IN FINANCING SMALL BUSINESSES IN SOUTH AFRICA

by

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DECLARATION

I, Lisebo Agnes Ntiso, declare that:

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LA Ntiso

30 June 2017

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DEDICATION

To my late parents and loving memories of Shabi.

ABSTRACT

This study explored the role of the development finance institutions (DFIs) in financing small businesses as a strategic tool for growth and development of the small business sector in South Africa. Although much research has been done and many debates have been argued around the problem of access to finance for small businesses, much of the documentation focuses on commercial lending and little attention has been devoted to development financing. Therefore, this study focused on the role of the DFIs in financing small business, in addition to studying the extent to which development financing narrows the financing gap and impacts on the growth of small businesses. Along with an extensive literature study, this thesis adopted a sequential exploratory mixed-methods approach consisting of two phases. Phase 1, a qualitative approach, through in-depth face-to-face interviews with the DFIs at both national and provincial level, was carried out to explore the existing programmes at the DFIs and to determine the extent to which the DFIs impact on the growth of small businesses. Phase 2, a quantitative approach, was based on a survey to investigate the perceptions of the entrepreneurs in Tshwane regarding the extent to which the financing by the DFIs, as identified from Phase 1, impacts on the growth of their businesses against business growth strategies; how it bridges the financing gap; and how the concept of development finance is constructed from the entrepreneurs' perspective.

The results from the literature study show that as an important strategic growth tool, development financing should be aligned to the growth plans of small businesses. Small businesses should therefore understand their position in the industry life cycle, which along with strategic growth and financing options available for the particular position, will allow them to make informed decisions on business financial needs. The findings of Phase 1 of the empirical research illustrate that the DFIs have both financial (in the form of asset finance, grants, loans and procurement finance) and non-financial programmes aimed at the development of small businesses. The results further show that the DFIs consider the number of employment opportunities created; skills development and business survival as measures of growth and development. Through the use of businesses support services, the DFIs help small businesses to establish banking relationships with financial markets, which can later benefit small businesses for relationship lending. The results from the Phase 2 investigation indicate that small businesses perceive financing by the DFIs as an alternative financing option. However, loans provided by the DFIs are perceived, like commercial loans, as too expensive and negatively affect cash flow. The results further show that stokvels, although informal, are used as a development financing platform by SMMEs. Entrepreneurs would prefer the establishment of a small business development bank that will work exclusively with the SMME sector and that understands the needs thereof – as per the stokvel model. The results further show that there is a perception among entrepreneurs that development finance from the DFIs is not easily accessible to the entrepreneurs. The findings of both Phase 1 and 2 show that both the DFIs and the entrepreneurs do not share a common understanding of business growth strategies and the financing options suitable for the growth stages of the business life cycle.

Key words: small businesses, DFI, development finance, business growth, business life cycle

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CHAPTER 1: INTRODUCTION AND OVERVIEW OF THE STUDY

1.1 INTRODUCTION

The importance of access to finance as a driver of growth for small businesses has attracted the attention of academicians, practitioners as well as policy makers, and it has gained prominence in the twenty-first century. In the 2011 State of the Nation Address, the president of South Africa, Mr Zuma, mentioned that small businesses are a component of job creation (www.economic.gov.za). Researchers agree that small businesses are catalysts for employment creation, poverty alleviation, as well as contribution towards economic growth and economic activity in the country (Ayyagari, Beck & Demirguc-Kunt, 2007). In order to achieve this role, small businesses need to have sustainable growth. The growth and survival of small businesses depend, among other things, on adequate finance. The availability of finance enables businesses to exploit opportunities, as well as to overcome and survive the challenges presented by both the internal and external environments. Finance is regarded as an important business function that funds the operations of all other business functions, for example, human resources; production; marketing as well as research and development. Finance is, therefore, is a developmental instrument for small businesses.

Development finance is viewed as a form of finance that is aimed at addressing development challenges. Sagastic, Bezanson and Prada (2005), state that development financing is a form of investment that is aimed at influencing self-sustaining growth and development through the provision of financial resources. As a growth tool, development finance is mostly available to emerging markets to affect development issues such as poverty reduction and employment.

1.2 BACKGROUND TO THE STUDY

Alongside the commitment towards achieving the UN Millennium Development Goals (MDGs), South Africa (SA) has developed a National Development Plan (NDP) which, among other things, is aimed at reducing unemployment by 6% by the year 2030. To achieve this goal, an additional 11 million new jobs need to be created and an economic growth of 5.4% per annum is required. Small businesses are expected to play a significant role in creating at least 90% of the jobs. The Economic Development Department (EDD) further reinforces the NDP through its medium-term tool: the New Growth Path (NGP). The NGP is considered to be a strategy for creating employment and inclusive growth by the year 2020. One of the key measures for the success of the strategy is to record the number of jobs created per 1% of the gross domestic product (GDP), or R1 billion invested (Patel, 2011). The President of SA articulates that development finance institutions should be instrumental drivers of job creation (Patel, 2011).

The prevalence of the high rate of unemployment (27.6%) in SA (StatsSA, 2016), is a major concern. High levels of unemployment lead to poverty, increased crime, and inequality, which pose great challenges for the country. Small businesses are more favoured for job creation than large business, mainly because the latter tend to be more capital intensive, while the former, due to limited resources, are labour intensive. Therefore, the SA government has identified small businesses as key aspects of economic development, poverty alleviation and an integral part of the job creation strategy; as such, the development and growth of small businesses has been firmly placed on the agenda for the government of SA, (EDD, 2011). The establishment of small businesses is deemed to be one of the best solutions to the problem (Abor & Biekpe, 2006; Beck, Demirguc-Kunt & Levine, 2005).

In the absence of newer information, the DTI (2008) reports that small businesses in SA make up about 96.7% of all businesses, and in 2007 they recorded a growth of about 27.2% up from 2004. Compared to large business which grew by 275.3% (4,596 in 2004 and 17251 in 2007), small business growth was extremely low. However, despite the low growth rates, small businesses play a significant role. The majority of small businesses (90%) are informal businesses and account for 15% employment against the 60% employment by formal small businesses (DTI, 2011). The Global Entrepreneurship Monitor Report further shows that about 94% of small businesses employ less than five people and only 6% of small businesses employ five or more people (Herrington, 2011). While appreciating that, small businesses contribute about 37% to the GDP, the Minister of Small Business Development, Zulu, in 2014 emphasised that small businesses are expected to increase their GDP contribution to range between 60% and 80% in the coming 15 to 20 years (www.economic.gov.za).

However, the minister was concerned about the growth and survival of small business and points out that any small business has about 37% and 9% chance of growing and surviving for four and ten years, respectively. The minister states that the short-term target contribution of the small business sector towards the GDP is 42% to 45% by 2019 (Ensor, 2017), focusing mostly on enterprises owned by black, female and young people.

Although many small businesses are continuously being established, many of these entities fail to survive beyond the infancy or introductory stage (that is, within one year) due to among other things, lack of access to finance (www.gov.za; Herrington, Kew & Mwanga, 2017). Research shows that although small businesses are engines for economic development, and may provide the solution to the high unemployment rate in SA, the problem of access to finance still exists (Ardic, Heimann & Mylenko, 2012) and needs to be addressed. In support of small businesses, governments intervene in the financing dilemma through the use of development finance. Development finance is viewed as one of the most prominent instruments in bridging the financing challenge facing the small business sector (Abedsamed & Wahab, 2014).

Research shows that unlike large businesses, small businesses do not have a track record, tangible assets, and established relationships with banks, all of which make them a risky market, and therefore not a market for commercial lending (Irwin & Scott, 2010; Federico, Rabetino & Kantis, 2010; Berger & Udell, 2006). Therefore, financing is a challenge for small businesses. In an attempt to address the financing gap, the government of SA has developed some policies that are meant to address the financing gap that small businesses face.

In 1995, the South African White Paper on small business development (Small business development strategy) was established to create an enabling environment in support of small businesses in alleviating poverty. The paper gave rise to the Act 102 of 1996, The National Small Business Act. This was enacted to support SMMEs in areas of access to finance access to the market and access to information. This was carried out by the Department of Trade and Industry through its Enterprise Development Unit (EDU) (DTI, 2005: 5; White Paper, 1995). Other spheres of government, such as provincial and local government also came on board in addressing the apartheid-based legacy of disempowerment of black businesses and women and to create jobs (Nieman & Nieuwenhuizen, 2009). More emphasis was put on the emerging and expanding SMMEs with more focus on the challenges facing previously disadvantaged groups, including black entrepreneurs. Increasing the supply of financial services is one of the pillars of SA's Integrated Small business Enterprise Development Strategy for 2005–2014. Various development finance institutions (DFIs) were therefore established both at national and provincial level to provide support to small businesses in the areas of access to finance (DTI, 2005; DTI, 2008; EDD, 2010). Zulu (2014), states that more funding, through the DFIs, is needed for the development of small business in order to not only address the challenges of unemployment, poverty and inequality, especially for historically excluded communities (www.gov.za); but to support decreasing innovativeness within the sector (Herrington *et al*., 2017).

1.3 THE RATIONALE OF THE STUDY

Despite the establishment of DFIs, access to finance and a lack of financial support remain at the top of the list of constraints that limit the growth of small businesses. Herrington *et al*. (2011) state that financial inaccessibility falls within the first three of the list of about ten main challenges facing small SA businesses, while Beck *et al.* (2008) also affirm that 62% of small businesses in sub-Saharan African face the problem of access to finance.

In SA, unemployment increased from 23% in 2012 to 26% in 2015 (StatsSA, 2015). The minister of the Department of Small Business Development (DSBD) posited that government investment in small businesses development is extremely important to address some of the challenges facing the country. The NDP also suggests that greater access to finance for small businesses is required in order to achieve the 2030 goals of creating 11 million jobs, of which 90% of the new jobs should be sourced from small businesses.

Thorough research has been done regarding the problem of access to finance as one of the main factors prohibiting the growth of small businesses. To prove that the issue of access to finance is a well-documented area, evidence can be drawn from as far back as the past two decades (Pettit & Stiger, 1985; Binks *et al.*, 1992; Berger & Udell, 1998), just to mention a few. Studies continue to be conducted and reports are made available that all suggest that funding is still a challenge facing small firms (Abor & Biekpe, 2006; Turner *et al*., 2008; Beck *et al*., 2010; Cowling 2010; Ardic, Malenko &

Saltane *et al*., 2012; Herrington & Kew, 2013). As Vanhanen (2007) states, more public funding is needed to boost and develop the small business sector. Vanhanen further discovered that overcoming the challenges of seed capital could help to create economies of scale and attract investors.

Research shows that banks are the main sources of external finance crucially needed for growth, however, due to the riskiness of the sector, small businesses are not a market for banks, (Beck & Demirguc-Kunt, 2006; Demyanyk, Ostrergaard & Sorensen, 2007; Carey & Nini, 2007, Ntiso, 2010). Therefore, governments have tried to address the finance dilemma faced by small businesses by introducing different forms of development finance. The intention of this support is to bridge the finance gap that is considered to be the main factor impeding the growth and development of small businesses. This study builds up on the researcher's dissertation at masters' level which recommended a broader study on DFIs' financing.

While the issues of access to finance for small business growth and development are well-documented areas in the fields of entrepreneurship, management, finance and development economics, the researcher has identified the following gaps (the full details available in chapter 4):

- Despite various efforts to avail finance for business, access to finance is still the prevailing problem within the small business sector;
- About 70% of start-up businesses fail during the first year of existence;
- There is limited published research on DFIs from the South African perspective;
- Small businesses make up to 96% of all businesses in South Africa, yet their contribution towards economic growth is recorded at about 37%, while about 94% of small businesses employ less than five people;
- South Africa is faced with the challenge of a high unemployment rate of 27.6% of which 65% are young people
- Sustainable developmental support of small businesses is deemed the key driver of economic growth, employment and poverty alleviation.
- The problem of access to finance always tops the list of prohibiting factor for small business growth in SA.

- The total early-stage entrepreneurial activity in SA at 6.9% which is a significantly low number (ranked number 52 out of 65 participating countries with less than an average of 18%, instead of 20% to match the unemployment rates.
- No existing research could be found on the role of the DFIs in financing small businesses in South Africa.

1.4 PROBLEM STATEMENT

Small businesses in South Africa are failing to grow (Fatoki, 2014), and in 2014, the minister of DSBD, Minister Zulu, stated that about 80% of small businesses fail in their first year of existence (www.economic.go.za). Research shows that lack of access to finance during the early stages (Agwa-Ejon & Mbohwa, 2015; Herrington & Kew, 2013) of the business life cycle, contributes to the high business failure rates and hinders the growth of small businesses (Mazanai & Fatoki, 2012). Research also identifies the introduction of development finance institutions (the DFIs) that have been established to help bridge the small business financing gap; recommends innovative approaches to provision of development finance for small businesses; and to improve micro-economic reforms to create business climate (Herrington, 2013, Ardic, Mylenko & Saltane, 2011). Despite the prescriptions of the Accelerated Growth Initiative of South Africa that small business must contribute towards achieving the 5% growth which is needed to address the social objectives, small businesses still fail to grow (Olawale & Garwe, 2010). This must be seen against the background that small businesses are expected to play a significant role in reducing the unemployment rate to at least 15% by the year 2020 (NGP 2011).

Research shows that finance is an important development instrument for the growth and success of small businesses (Abdulaziz & Worthington, 2013). However, previous research focused mostly on access to finance from the perspective of commercial banks (the main sources of finance) and devoted little attention to the role of the DFIs in financing small businesses, the gap which is central to this study. Hence, Beck, Klapper and Mendoza (2010) recommend that a need exists for further research to investigate if government intervention actually addresses the problem (a cost-benefit analysis). Most importantly, the studies do not document the extent to which financing of small businesses by the DFIs affects the growth and development of the small business sector, the area which the current study intends to explore. Small businesses are mostly ignored when solutions are sought to the problem of access to finance, apart from being used as instruments to measure the depth of the problem.

This leads to the key statement problem:

Participation of the DFIs in financing SMMEs (small, medium and micro enterprises) in South Africa can lead to the sustainable growth of small businesses in South Africa and reduce the problem of access to finance.

Key research question

How can participation by the DFIs in financing small businesses lead to growth and sustainable development for the SMME sector in South Africa?

1.5 RESEARCH AIM AND OBJECTIVES

In addressing this research problem, this study aims to explore the role of the DFIs in financing small businesses as an imperative instrument for the growth and development strategy of the SMME sector in South Africa (which bears the most significant reference to this study). This is done in order to establish an understanding of the role development finance plays in assisting small businesses to grow and competitively participate in the mainstream economy of South Africa. To achieve the research aim, the following secondary objectives needed to be achieved:

1.5.1 Research Objectives

- To explore the programmes that the DFIs have to finance small businesses in South Africa to ensure the growth and development of the sector.
- To explore the extent to which the DFIs bridge the financing gap that exists in the financial markets for small businesses.
- To examine the limiting factors for the DFIs in financing small businesses.
- To explore the perceptions of entrepreneurs on how financing by the DFIs impacts on the growth of their businesses across demographic variables.
- To investigate the propositions entrepreneurs have for small business development finance
- To determine the extent to which the availability of development finance aligns to the growth strategies for small businesses.

- To investigate the perceptions of entrepreneurs on the role of the DFIs' financing support to small business development in terms of bridging the financing gap.
- To recommend a development financing framework guiding the DFIs to assist small businesses to achieve sustainable growth.

1.6 RESEARCH QUESTIONS

The study articulates a perspective of development finance along the stages of the business life cycle as a business growth tool for the financing gap which exists in small businesses in the early and development phases of the business. While finance is one of the main growth instruments for small businesses, the financing gap which exists due to financial market failures must be addressed if small businesses are to grow.

With reference to DFIs, the objectives of the study led to the development of the research questions. Therefore in addressing the research objectives, the following questions were answered:

What is the role of the DFIs in providing finance to small businesses in South Africa?

1. What programmes do the DFIs have to provide financing to small business for the growth and development of the sector?
2. How do the DFIs bridge the financing gap in the financial markets for small businesses?
3. What challenges do the DFIs have in implementing programmes aimed for the growth of small businesses?
4. How does development finance align to the growth strategies for small businesses?
5. How do the entrepreneurs across demographic variables (gender, race, age and education) perceive the role of development finance towards growth of small businesses?
6. What are the propositions of Tshwane entrepreneurs for small business development finance?
7. How do the entrepreneurs perceive the role of the DFIs' financing support to small business development with regard to bridging the financing gap?

8. What can be recommended to the DFIs towards achieving a sustainable growth and development of the small business sector in South Africa?

1.7 WORKING ASSUMPTIONS

These working assumptions were developed after the conclusion of Phase 1 of the study.

Being an exploratory study, the researcher approached the study with no predetermined hypothesis on the grounds that the phenomenon of development finance is a fairly new concept in the field of entrepreneurship and management. However, during the Phase two, the working assumptions were developed based on the findings of Phase one in order to guide the establishment of a development financing framework for the sustainable development of small businesses in South Africa. Therefore, the second phase of the study was based on the following assumptions:

- There is a significant difference in perceptions of the respondents (the entrepreneurs) from the Tshwane Metropolitan Municipality regarding the impact of the DFIs' financing on small businesses growth (performance factor) across respective demographic variables (gender, race, age and education).
- There is a significant in the perceptions of the respondents on the role of the DFIs' financing support to small business development in terms of bridging the financing gap.
- There is a significant difference in the perceptions of the respondents regarding propositions for development finance for small businesses.

1.8 RESEARCH METHODOLOGY

In achieving the research aim and objectives, the study used an exploratory sequential mixed-methods approach, incorporating both qualitative and quantitative methods. While the literature study was used as the basis for relevant theoretical information, empirical information was gathered through both qualitative and quantitative research methods. Data was collected through the use of face-to-face interviews and a questionnaire survey; these were supplemented by a desktop study. Interviews (Phase 1) were conducted with 14 strategic/ programme managers of the DFIs of

South Africa and representatives from the small business development of the Department of Economic Development.

The results of Phase 1 were used for the design and implementation of the second phase (the quantitative phase) which was conducted through a questionnaire survey and in-depth interviews. The information was processed to obtain the final information regarding the development financing of small businesses in the Tshwane Metro Municipality by the DFIs. This second phase of the study does not only entail and involve the complementary information emanating from the conclusions of the first phase, but also comprehensively draws conclusions from the literature study as well. The survey questionnaire (Phase 2) was used to gather data from 301 small business owners/entrepreneurs of the Tshwane region of Gauteng Province. During Phase 2, in-depth interviews were conducted with 15 entrepreneurs who were purposively sampled from the 301 entrepreneurs who participated in the questionnaire survey. The in-depth interviews consisted of open-ended questions as part of the survey to ensure the trustworthiness of the responses.

Content analysis was used to analyse the qualitative data, while the quantitative data was translated into statistics and subjected to different and multiple computational runs and statistical analysis (descriptive and inferential statistics such as factor analysis, T-tests, ANOVA and Pearson's product correlation coefficient). The analyses were used to compare summaries of the findings and presented in tabular and graphic forms. A detailed account of the research methodology is found in Chapter 5 which discusses the research design, including the research methods, techniques and tools as applied in this study.

1.9 SIGNIFICANCE OF THE STUDY

The findings of this study are relevant to an academic audience interested in the fields of entrepreneurship, development economics, as well as strategy and management; business experts and entrepreneurs; as well as policy makers. The contribution of this study is important as it fills a research gap by building on the research interest in issues of access to finance (Beck, 2010). There is a critical need for policy makers to develop the small business sector which is believed to be able to assist in addressing some of the social challenges. The availability of adequate and appropriate finance needed for the growth of small businesses is a major concern of policy makers.

The current study also aims to contribute to the current debate in the fields of Entrepreneurship regarding entrepreneurial finance and development. Previous studies on entrepreneurial finance have looked at small business finance from the perspective of commercial lending which is mainly provided by banks. In contrast, the current study considers development finance as provided by the SA government through the DFIs in support of small businesses as development instruments that need to grow in order to affect employment, reduce poverty, inequality and to contribute towards economic growth. Therefore the study focuses on financing from the development perspective as opposed to commercial financing. The significance of the study therefore is to:

- Discuss access to finance as one of the main drivers for the growth of small businesses.
- Provide insight on the role of the government's investment in the development of small businesses with regard to development and growth, employment creation and poverty alleviation;
- Prove that growth, survival and sustainability of small businesses are closely related to development.
- Reveal the progress made regarding the development and growth of small businesses.
- Assist policy makers to identify the areas that need improvement and redefine where necessary;
- Provide much needed information to guide relevant policy development which may ultimately reduce unemployment, inequality and poverty through the development and growth of the small business sector; and
- Help to create a common understanding on the roles and responsibilities of all stakeholders regarding development financing.

The findings of the research are also aimed at contributing to the existing body of knowledge on entrepreneurship, strategy, small business management and development economics and public finance. The study has national strategy importance relating to NDP goals, SA policy and the UN MDG's factor of poverty eradication and women empowerment.

1.10 ETHICAL CONSIDERATION

The researcher made concerted efforts to abide by the Research Ethical Policy of the University of KwaZulu-Natal, and as such, the researcher secured research clearance from the university to conduct the study and sought permission to collect data from the selected data sources. Thereafter, the researcher asked for voluntary consent from the participants involved in the study, and where necessary, requested permission from the authorities (gate keepers) to conduct the study with the research participants.

1.11 LIMITATIONS TO THE STUDY

The current study is delimited in the fact that it only focuses on development finance agencies funded by the South African government. This implies that the findings of the study cannot be applied to all development finance institutions universally. Because this research is only confined to the Tshwane metropolitan area, the results may not necessarily be applied to all the provinces of the country, owing to the different levels of industrialisation of the various provinces.

It would be fair to conduct surveys throughout all nine provinces of South Africa, but due to time and financial costs, it was not possible. The researcher therefore decided to focus only on Tshwane entrepreneurs as representatives of the small business sector for the survey. It would be interesting to focus on a single industry; however, the current study did not distinguish between the different industries with regard to the phenomenon under study because development support for small businesses. The researcher therefore decided to only demarcate the study in terms of the region and the size of the business, and not according to the industry.

Various other limitations were identified during the study. Firstly, there has not been much documented research regarding the operations of the DFIs. This limited the study only to the information provided by the DFIs themselves which created the barrier for rich arguments. Secondly, some DFIs declined participation in the study which prevented the researcher from making holistic conclusions regarding DFIs in SA. It was an intention of the study to collect data through face-to-face interviews, but due logistical concerns and time constraints, telephonic interviews were used for follow-ups, however, the approach still earned the desired results.

1.12 DISSERTATION CHAPTER SYNOPSIS

This dissertation is divided into eight chapters in the following order:

Chapter 1 placed the current study in context. The background to the study was explained in such a way that the basis of the study could be understood. The motivation and rationale for the study followed to highlight the importance of the study. The research problem was mentioned, as well as how the current study aims to address the problem. This was followed by the objectives, research questions and hypothesis. A brief account of the methodology used in addressing these objectives was also covered in this chapter. The limitations, ethical considerations as well as definition of terms of the study preceded the last part of the chapter which provided the details of how the study was organised.

Chapter 2 is a literature review regarding small businesses, their importance and challenges facing the sector. Discussion of access to finance and financing models are covered in this chapter. As integral part in the study and a point of reference to identify financing gaps for small businesses, commercial financing is also covered in the last part of this chapter

Chapter 3 furnishes the theoretical framework within which this study is based. This entails different theories advocated by scientists and researchers within the field of study.

Chapter 4 focuses specifically on an evaluation of small businesses and the DFIs in South Africa. It also explores the relevant legislations and regulations as well as policies that relate to the financing of small businesses. The chapter also focuses on small businesses, including the practical challenges that affect the small business sector in South Africa.

Chapter 5 provides details of the methodology employed in the study. This includes a discussion of both the qualitative and quantitative approaches employed in addressing the objectives of this study. Specific techniques and tools used in addressing each of the research objectives as well as the justification from the literature point of view, and their relevance in this research are presented.

Chapter 6 is based on data presentation of the results as well as data analysis of Phase 1 of the study.

Chapter 7 consists of data presentation and analysis of Phase 2 of the study.

Chapter 8 comprises a discussion of the results based on the objectives of the study. This final chapter also consists of the summary of the main findings of the study; the conclusions as well as the recommendations.

1.13 CONCLUSION

The main emphasis of this study is to understand the role played by the DFIs in advancing finance to small businesses in South Africa, as an imperative instrument of the small business development strategy. This chapter demonstrated an overview of the study, detailing the motivation for the study and identifying the research problem. The chapter further points out the aim and objectives, research questions and hypothesis, limitations and delimitations, as well as the structure of the thesis.

The next chapter provides a conceptual framework of the study. It particularly furnishes an overview of three issues: small businesses, access to finance and development finance institutions.

CHAPTER 2: REVIEW OF FINANCE AND SMALL BUSINESSES IN LITERATURE

2.1 INTRODUCTION

Nowadays, more than ever, economies depend on businesses for job creation and employment and ultimately for economic growth. Businesses generally start as small businesses, and as such, small businesses can be seen as the centres or engines for economic growth. The purpose of this literature review chapter is to discuss the main concepts as used in this research, and to establish an understanding of the concepts as applied in this study. Therefore, the first part of the chapter deals with the definitions of the concepts. The second part of the chapter is focused on commercial financing, both for the understanding of the financing gap faced by small businesses, and as a comparison reference for development finance, which is at the core of this study.

2.2 DEFINING CONCEPTS

As stated above, this section will provide definitions of the concepts as applied in this study.

2.2.1 Development finance Institutions (DFIs)

Diamond (1957) defined development finance institutions (DFIs) as post-World War II and post-colonial development institutions that were designed to offer financial support that was focused on both national and regional development, as well as focused on enhancing economic growth. DFIs were established to address the inefficiencies of financial markets. This became necessary because financial markets are reluctant to provide financing for or to bear the risk of financing creditworthy clients, and thus the DFIs are meant to fill that financial gap. The DFIs provide support with a motive of cost recovery, therefore, projects that lack sufficient income-generating capability are not included in the DFI loan portfolio, These types of projects, instead qualify for a special fiscal, grant is concessionary funding mainly to help meet developmental agendas such as human needs and social services (poverty-related factors) (Masusike *et al.*, 2004).

2.2.2 Entrepreneur

As researchers do not agree on a single definition of an entrepreneur, a number of definitions therefore exist. An entrepreneur is a person involved in opportunity recognition, idea generation and commercialisation (Shaw, 2011) with the will-power to commit money to start a new business in anticipation of losing or gaining rewards upon the success of the business. The entrepreneur can also make a financial commitment by buying the business with the intention of growing (rewards) or risking making a loss (Scheier, 1934). The entrepreneur gains rewards which Livesay (1979) argues are the results of exploiting the opportunity that the entrepreneur sees and develops in order to create wealth. However, Carland, Hoy, Boulton and Carland (1984) hold that the entrepreneur is distinguished in terms of the innovativeness and strategic management attributes possessed by the entrepreneur. In addition to opportunity recognition and innovativeness, Watson (2001) attaches the ability to grow the business as one of the traits of the entrepreneur. The term 'innovativeness' has been further defined by Schumpeter (1939) who argued that it means not only a new idea but also a new function for the existing product.

An entrepreneur can therefore be defined as a sole owner of an independently run business and not an innovative corporate entity.

2.2.3 Small businesses

Just like the term 'entrepreneur', there is no standard definition for small businesses or small, medium enterprises (SMEs) as they are commonly known. However, the International Finance Corporation (IFC) includes micro enterprises and uses the acronym (MSMEs) to signify SMEs. Accordingly, the IFC defines small businesses as per Table 2.1 below

Table 2.1: Categorical definition of small businesses

Category	Employees	Total assets (TA) in US$	Annual turnover (TO)in US$
Micro	< 10	< 100 000	<100 000
Small	< 50	100 000 < TA < 3m	<100 000 TO<3m
Medium	50<employees<300	3m<TA<15m	3m<TO<15m

Source: Author's own compilation

Similarly, the National Small Business Amendment Act, No. 26 of 2003, (The Act) defines small businesses as the separate and distinct entities including co-operative enterprises managed by one or more owners in any sector or subsector of the economy. The small business employs between 1 – 200 people. The Act categorises small businesses in terms of the number of employees, total gross assets and total annual turnover per individual entity. It is due to this categorisation that small businesses are referred to as micro, small and medium enterprises (SMMEs). For the purposes of the current study, only the total number of full-time paid employees will be used in the definition of small businesses. The Act distinguishes between different industries and categories, and specifies different amounts for the total gross assets and total turnover applicable to these various industries and categories; therefore they are excluded from the definition of small business as in this study. The following definitions apply to this study:

- Micro enterprises are business entities with five full-time paid employees.
- Very small enterprises are business entities with more than five- up to twenty full-time paid employees
- Small enterprises are businesses with twenty to fifty (20-50) employees
- Medium enterprises imply businesses that employ fifty up to two hundred (50 - 200) people.

Together, all these categories mentioned above are referred to as small businesses. As Bezuidenhout and Nenungwi (2012) assert, small businesses are entities that are managed by the owners (entrepreneurs). The current study therefore, adopts the definition provided for by the Act; categorising small businesses as micro, very small,

small and medium enterprises managed by the entrepreneur, employing at least one up to two hundred (1 – 200) people with a turnover of R0 – R1 000 000.

2.2.4 Access to finance

The term 'accessing finance' is regarded by a number of studies as the availability of financial services to consumers (Irwin & Scott, 2010; Federico, Rabetino & Kantis, 2010; Berger & Frame, 2006; Beck, 2005 and Berger & Udell, 2002). Nonetheless, access need not be viewed only from the disposal of financial services at reasonable costs (Claessens, 2006), which reflect all pecuniary as well as non-pecuniary costs. Access therefore, must include the intersection between demand and supply in terms of access and use with relevance to the three types of consumers as shown in the following table.

Table 2.2: Difference between access and use

Type A: Current consumers	**Type B: Voluntary exclusions**	**Type C: Involuntary exclusions**		
	No need	- Rejected: high risk - Bad credit: no access	- Rejected - Discriminated - Lack of awareness	- Excluded due to price, product, income or respondent features

Source: Adapted from Claessens (2006)

With the exception of Type A consumers, who are financially included in the financial markets (financial inclusion), the rest of the consumers do not have access to financial services. On the one hand, Type B consumers voluntarily exclude themselves. On the other hand, Type C consumers are systematically or involuntarily excluded from financial services. In the context of Table 2.2 classifications, small businesses typically fall within the category of involuntarily excluded customers (Narain, 2010) and therefore, fall under Type C consumers.

Narain (2010) suggests that when measuring access to finance, financial facilities should take cognisance of a range of other elements, such as payments or transactions, savings, credit, insurance and pensions (Chidzero, Ellis & Kumar, 2006). Some researchers (Demirguc-Kunt, Klapper, Singer & Van Oudheusden, 2015) are of the opinion that access to finance is a difficult aspect to define, and hence, there is no standard definition. Demirguc-Kunt (2008) however, argues that if the former is explained in terms of usage, it (access to finance) may be easy to measure as exclusion versus involuntary exclusion. There is, however, a contractual or informational framework (Demirguc-Kunt, 2008) which adds to the reasons for involuntary exclusion. For the purposes of this study, Type C consumers are referred to as the financial exclusion or finance gap.

2.2.5 Development finance

Development finance is defined as a set of financial flows for the purpose of investment in development projects or ventures that generate income, as well as the activities that operate on the basis of commercial profit and full-cost recovery (Hoffmann, 1998). The United Nations (UN) argues though that the concept of development finance has no standard definition. The lack of a set definition has instigated various narrations regarding the concept which revolve around non-conventional forms of finance. However, this form of finance is closely related to the notions of funding, allocation and spending which cannot be separated (UN, 2012). By aligning this non-conventional form of financing to the definition of the term 'development' which relates to the reduction of poverty, unemployment and inequality as important indicators, 'development finance' would therefore mean financing aimed at reducing poverty, unemployment and inequality, which is a narrative of inclusion of social dimensions (Seers, 1969).

2.2.6 Business growth (performance) and development

Mao (2009) defines business growth as not just a process of developing a business from small to big, but also developing it from a weak to a strong entity as well. While growth implies a positive progression from one stage to the next, development involves the regeneration of individual stages of the business life cycle coupled with a periodic progression to the next stage. The growth of a business is a developmental process of adjusting from a state of unbalance, and developing from a lower to a higher balance, both internally and externally, in order to attain a balanced and stable growth of total performance. The latter includes: output, sales volumes, profit and an asset gross that needs a continuous high level of quality enhancement (Sun, 2009).

Mao (2009) highlights that in defining business growth, the three properties of growth: time; dynamics; and quantity and quality, need to be recognised. Business growth therefore, suggests:

(i) the value-added ability of the business to continually survive in an intense market through the optimal, efficient and speedy change between the factors of production and output, relative to the industry in which the business operates, and which is the factor that earns the business a competitive advantage; and
(ii) following the generation period and survival, a competitive advantage provides the business with the sustainable development ability to outperform in all aspects.

Sharing the same sentiments, Bulut and Can (2013) define business performance to express the degree to which management goals are fulfilled in the practices of the business, and their realised output by the end of a certain period. In the context of the current study therefore, the development and growth of a business is defined as the renaissance of the individual stages of the business life cycle, combined with a periodic progression to the stage of balance and total performance through a competitive advantage.

2.2.7 Credit rationing

Credit or loan rationing is defined as a deliberate decision by lenders to limit the issue of credit to borrowers, even in the situation where the borrowers are willing to pay higher loan prices or interest rates (Waller & Lewarne, 1994). Unlike financial exclusion where high loan prices are a reason for borrowers to decide not to borrow due to affordability reasons, in the case of credit rationing, the borrowers are willing to take up the funds despite the high interest rates (De Meza & Webb, 1992), but the lenders are not willing to issue funds. That is, there is mismatch between the borrowers and lenders.

2.2.8 Debt finance

According to Greater Capital (2016), debt finance is the main form financing by an external party with the anticipation of being repaid with interest, either in a lump sum or in instalments. The lender or the creditor requires that the borrower or debtor must have the ability to repay the debt in full. Repayments can be made over either a short-term or long-term period. Small business borrowers require debt finance for different financial business needs such as:

- Start-up capital
- Working capital
- Expansion finance
- Bridging finance

Bridging finance is a form of finance that is provided to the business and that is secured by contract held by the business for rendering a service. The business is given advance financial support by the financing institution based on the promise that upon completion of the project, the (latter) funder will recover the costs and the remaining amount belongs to the (former) business. Bridging finance is defined as a short-term loan against a confirmed or guaranteed cash inflow expected in the near future (www.nhfinance.co.za).

2.2.9 Stokvels

Lukhele (1990) defines stokvels as clubs or groups of people in South Africa which serve as rotating credit unions or saving schemes where members contribute fixed sums of money to a central fund on a weekly, fortnightly or monthly basis. The terms of reference for stokvels are tabulated in individual stokvel constitutions, including liberation on the size of the contribution as well as the roles and responsibilities of the members. Members are allowed to borrow money from the fund (access to finance) at agreed rates, and defaults on contributions and repayments are rare.

2.2.10 Retail financial intermediaries

According to Siklos (2001), retail financial intermediaries (RFIs) are defined as institutions or individuals that operate as the middleman between parties involved in a financial transaction. RFIs channel funds from the lenders through to the borrowers. The lenders give funds to an intermediary institution (O'Sullivan & Sheffrin, 2003); and the intermediary in turn gives the funds to the borrowers (Batiz-Lazo, Maixe-Altes & Thomes, 2010).

2.2.11 Trade credit

Trade credit is defined as a facility or a tool that is used for financing business growth where the business is allowed to purchase stock on credit for immediate use with the promise to pay later. This facility is not easily available for start-up businesses, but when made available, the costs are high and become more relaxed as trust is established between the creditor and the debtor. If the repayment is made before the due date, the creditor often relaxes the costs for the debtor (Encyclopedia, 2010).

2.2.12 Credit guarantee scheme

A credit guarantee scheme is a facility designed to operate within the formal financial system (Hannig & Joubert, 2003) where the guarantee is given to a financial institution as a security by a signatory (usually the government) that should the borrower default on payments, the lender will be reimbursed. According to Miller (2013), this facility holds attractive features for all the stakeholders involved: financial institutions; policy makers and borrowers. The facility helps cushion against the lending risks for financial institutions in addressing the changing needs in areas of portfolio concentration risks and capital requirements (of Basel II and III).

2.3 THE CONTRIBUTION OF SMALL BUSINESSES IN THE ECONOMY

Even though the importance of small businesses has already been highlighted in Chapter 1, their contribution towards economic growth is worth detailing from different dimensions. This is in order to validate the role of debt financing as one of the developmental strategies for small businesses. The role of small businesses towards the development of the economy is observed from the following angles: employment, economic growth, social responsibility and lastly, innovation.

2.3.1 Employment

Small businesses are considered to be the backbone of virtually all economies in the world, especially in developing countries. The reason for this is that in comparison with larger businesses, smaller businesses are more labour intensive than is the case with larger businesses, which are more capital intensive thus making the former agents of job creation (Christian, 2003; Newberry, 2006). For example, in the Association of

South Asian Nations, small businesses are accountable for the employment of from 70% to 90% of the domestic workforce. In Africa, a similar contribution by small businesses regarding employment is reported. For example, small businesses account for 85% of the employment in the manufacturing sector in Ghana, while in South Africa, approximately 70% of the private-sector employment is attributed to SMME employment (GEM, 2008; Abor & Biekpe, 2005).

Following upon the report that the unemployment rate for the last quarter of 2008 was at 21.9% (StatsSA, 2009), the Minister in the Presidency National Planning Commission announced that the government was committed to its goal of halving unemployment and poverty by 2014 (SAPA, 2009). This was consistent with earlier statements that the SA government intended to reduce the unemployment rate by 14% by 2014 through the commitment of about R44,5 million to a four-year development programme aimed at small businesses (Good News SA, 2008). However, due to the 2008/9 global recession, the unemployment rate instead rose to 24.5% in the third quarter of 2009, up from 23.6% in the second quarter of 2009 (StatsSA, 2009).

The line, however, needs to be drawn on how far the contribution of small businesses towards economic development can be observed. Beck *et al.* (2005) argue that the proportion of employment by small businesses is only greater in countries with higher education levels and a more developed financial sector and is not observable in countries with more exchange rate distortions. In South Africa, for example, small businesses that are operated in the rural areas are limited in their ability to create jobs because their establishment is more necessity driven development (for survival) than for economic growth/development.

However, the Global Agenda Council suggests that employment needs to be considered not only as a result of economic growth, but as another factor that drives economic recovery, as high levels of unemployment came about during the global meltdown. Therefore, Gul *et al.* (2010) suggest that a valuable tool would be for countries to make provisions to finance high-growth small businesses to reinforce employment.

2.3.2 Economic growth and national income

Research shows that a significant contribution is made by small businesses to their respective economies. Oketa (2009), for example, highlights that the percentage that small businesses contribute towards the total value-added GDP ranges from 60% in China, 57% in Germany, 55.3% in Japan and 50% in Korea. Oketa (2009) further shows that about 95% of the firms in Australia fall under the small business sector, and furthermore, Oketa state that in SA, 91% of the formal entities are small businesses that contribute about 57% to the GDP. Abor (2010) affirms that small businesses in Ghana represent about 92% of all businesses with contribution of about 70% toward Ghana’s GDP, mostly from manufacturing.

Small businesses have a positive impact on tax, both directly (company tax) and indirectly (value-added tax). According to SEDA (2014), SMMEs from the trading and manufacturing industries in South Africa have contributed more towards company tax than any other industries between 2008 and 2015. In 2010 combined, the two industries contributed 60.8% of R6 907million and 48% of R10 908 million in 2015.

The small business sector has proven to be a growth sector in many different countries. In Taiwan, for example, small businesses have a growth rate of about 2.41% compared to large enterprises which only have 0.60% (Taiwan Economic Affairs, 2006). Similarly in South Africa, small businesses are considered to be high growth businesses, which are likely to experience even more growth where equity investors promise capital investment, since investment growth is heavily based on return (Business Partners in Hannig & Joubert, 2003).

2.3.3 Social responsibility

Because small businesses are considered less mobile than large businesses, they relate more to their communities in order to protect their reputation with their customers (Scozzi *et al*., 2005). Newberry (2006), for instance, mentions a European study conducted on small businesses, where about 67.5% of the small businesses reported being involved in some external social responsibility projects, like supporting a local charity on a regular basis. The main reason for this is reported as an effort to increase customer loyalty and to build better relationships with the community.

Some researchers believe that small businesses practise the social responsibility principle, but most of them are not aware of it (Lepoutre & Heene, 2006; Murillo & Lozano, 2006). Perhaps this migrates from the common usage of the term “corporate social responsibility” which is language associated mostly with large firms (Murillo & Lozano, 2006) Therefore by creating jobs, small businesses help reduce unemployment, and also contribute to economic growth, all of which amounts to their responsiveness towards social responsibility.

2.3.4 Innovation and efficiency

Another factor that helps underscore the importance of SMMEs is innovation. Newberry (2006), for example, advocates that inherent flexibility and risk-taking abilities are the key drivers of innovation for a true entrepreneur. This is why small businesses are operated by entrepreneurs who nurture a business opportunity into a potentially high-growth venture in a complex and unstable environment. These entrepreneurs at the same time, conceptualise, organise and launch those businesses (Rwigema & Venter, 2004). Cornwall (2009) further emphasises that when faced with challenges in the competitive market, small businesses refine and redefine how to work and what they produce. This is the SMMEs' strength as innovators in comparison to their counterparts in large business which, due to extra costs to incur, cannot innovate. Instead of innovating, large businesses would try to create something bigger and better. In achieving this comparative strength, small businesses use six enablers:

- Personal passion;
- Customer connection;
- Agility and adaptation;
- Experimentation and improvisation;
- Resource limitation; and
- Information sharing and collaboration.

Research shows that small businesses are natural innovators who use more market radical changing innovation in their businesses. Moreover, these findings show that small businesses innovation is used broadly across the small business sector and is not only limited to technology and high-growth firms (Small Business Labs, 2009). However, Christensen (1989) points out that innovation within the manufacturing industry of small businesses is often unstructured and not well defined.

2.3.5 Market competitiveness and efficiency

The small business sector is characterised by easy entry and exit; this characteristic makes the economies more flexible and more competitive. The existence of a large number of small businesses creates competitive pressure, whereas small businesses with high turnover and adaptability play a big role in removing imbalances in the economy. Fan (2003), acknowledges the role that small businesses play as subcontractors in the downsizing, privatisation and restructuring of large companies.

2.4 CONSTRAINTS FACING SMALL BUSINESSES

Despite the crucial role small businesses play in the development of the country, their contribution may be short-lived given the impact of the constraints they face. These challenges hinder the growth of small businesses, which would otherwise have had a significant impact on economic growth. These challenges include the regulatory environment, capital and corruption. However, Beck *et al*. (2005) argue that the financial constraints have a larger impact than the constraints emanating from legal and corruption factors. Although large businesses also face high financial constraints, legal and corruption constraints are closer to zero than is the case for small businesses. When compared with large businesses, as shown in Figure 2.1, (later in this section) small businesses face almost double the negative impacts of financial constraints.

Fatoki (2014) asserts some of the barriers to growth of small businesses include lack of access to business finance, poor marketing and labour shortages. There are many factors that hinder the growth of small businesses, such as limited access to the market; limited information; business illiteracy; legal issues and demographical factors. The section below will discuss some of the constraints that have a negative impact on small businesses.

2.4.1 Impact of regulatory and disabling environment

Abor (2010) argues that regulation poses threats to small businesses, citing high start-up costs such as licencing and registration requirements, and the settling of legal claims, including delays in court proceedings. For example, the World Bank (2006) reports that in Ghana, a licence takes about 127 days to issue and it goes through 16 procedures; likewise, in SA, licencing takes about 176 days and goes through 18 procedures.

Some of the challenges that hinder the performance of SMMEs have to do with regulations and bureaucratic practices around larger businesses in different countries.

Large businesses make it difficult for small businesses to penetrate their market by imposing barriers to entry. These factors effectively force entrepreneurs to operate illegally outside government's regulatory reach, which in turn compromises their access to human and financial resources. In countries where the environment is enabling, there is a lower occurrence of illegal business when compared to environments with more regulatory constraints being placed on small businesses. The World Bank Group (2006), for example, reports that New Zealand has informal small businesses that account for only 12.7% of the gross national product (GNP), because the environment is enabling for small businesses.

Smith (1994) defines the shadow economy as the production of goods and services (regardless of whether legal or illegal) in the market by people wanting to avoid government regulations and taxes, as well as observation in the GDP estimates. However, Schneider, Beuhn and Montenegro (2010) argue that although the concept is difficult to define, the common working definition for most authors is that the shadow economy includes all unregistered economic activities that contribute to the calculation of GNP.

Developing economies experience the negative impact of the disabling regulatory environment more than is the case in developed countries. For example, Schneider and Enste (2011) who are called the philosophers of the shadow economy, report that in Africa the informal economy accounts for more labour force than is the case in the formal economy. The scholars highlight that Zambia is the leading African country with the informal economy accounting for 80% of the labour force; this is followed by Guinea, Benin and Rwanda with 79%, 76.9% and 75%, respectively. The productivity of this part of the economy was found to be 41.2% for Zambia, followed by 36.9% in Guinea while Rwanda recorded 38.7%. Comparatively, South Africa has the lowest informal economy labour force absorption. While the formal small business sector absorbs about 60% of the labour force, the informal economy absorbs about 15% thereof. Nonetheless the DTI reported that the small business sector contributed almost 50% of the GDP in 2004 (DTI, 2004). However, the 2011 report stated that the sector contributed 34% of the GDP while the contribution towards employment remained unchanged at 60% (DTI, 2011).

Nonetheless, the shadow economy is not a complete enemy of the economy. Small businesses that operate in the informal or shadow economy benefit the economy in a number of ways, such as reducing unemployment; because the income generated from the shadow economy indirectly contributes to the national income through the payment of taxes.

2.4.2 Lack of access to information and market

Large businesses have the advantage of having access to information and access to markets due to established networks and advanced infrastructure, while small businesses have few such benefits. For example, Okello-Obura, Minishi-Majanja, Cloete and Ikoja-Odongo (2007) state that small businesses in Uganda operate in a fragmented environment where information is both limited and incomplete. Due to lack of access to timely business information, as well as lack of finances, and technology, small businesses receive limited market awareness, and this contributes to small businesses in Uganda failing. Similarly, Gibb and Scott (1989) further confirm that entrepreneurs often have to cope with limited information and resources which are needed to review and plan in response to the competitive environment.

2.4.3 Limited access to finance

Although the small business sector has the potential to create jobs, a lack of access to finance is believed to be one of the main factors preventing job creation. According to (Bell, 2015), the World Bank expects 600 million jobs to be created within the next 15 years from 2015 onwards to accommodate the global workforce. Although small businesses contribute hugely to job creation, citing that SMMEs in emerging markets create four out of five new jobs created, a limiting factor is that about 50% of small businesses lack access to finance. Unless innovative solutions are found to improve access to finance for small businesses, the expected job creation cannot be achieved (www.worldbank.org).

The lack of access to finance for small businesses is thus considered a growth impediment facing the developing countries. For example, a study that was done in Ghana in 1994, showed that out of 133 enterprises, both large and medium, 53% of the enterprises identified access to finance as the most significant constraint (Aryeetey, 1998). Another example is that in Taiwan about 40% of small businesses reported that they were experiencing difficulties in securing funding (Taiwan White Paper, 2007).

Beck and Frame (2005) claim that because small businesses do not have a track record and/or collateral (World Bank, 2005; Asia Development Bank 2008), they are disadvantaged in trying to obtain external funding. As finance is the most important factor for growth of a business, without access to external finance, small businesses are bound to remain at the infancy stage of the business life cycle.

In addition, access to finance is the most dominant factor that hinders the growth of small businesses. Without enough working capital, the growth potential of small businesses becomes difficult to exploit. To achieve this potential, the entrepreneur needs to obtain extra finance from external sources. Failing to obtain external finance implies that the business is stuck in one stage of the business cycle forever, and ultimately there can be no growth.

Small businesses face challenges in trying to attract external financing, especially if they do not have equity, because they do not have a proven track record or collateral for the loan. In Burkina Faso, for example, a bank requires a large collateral before granting a loan (World Bank, 2005). Both supply-side (banks) and demand-side (entrepreneurs) blame each other for the financing gap. According to the Asia Development Bank (2008), small businesses are their own worst enemies in the area of accessing finance. The Asia Development Bank states that the problem lies with the small business's own weaknesses and lack of understanding of financial markets, including micro finance institutions and small banks. On the other hand, about 90% of the entrepreneurs that participated in a study in South Africa (Christianson, 2003) blame the banks for not reaching out to small businesses and doing nothing to improve the poor relations that small businesses have with banks (relationship banking). This study further showed that the major banks in South Africa cited the high transaction costs associated with small business lending which caused them to close down their small business units.

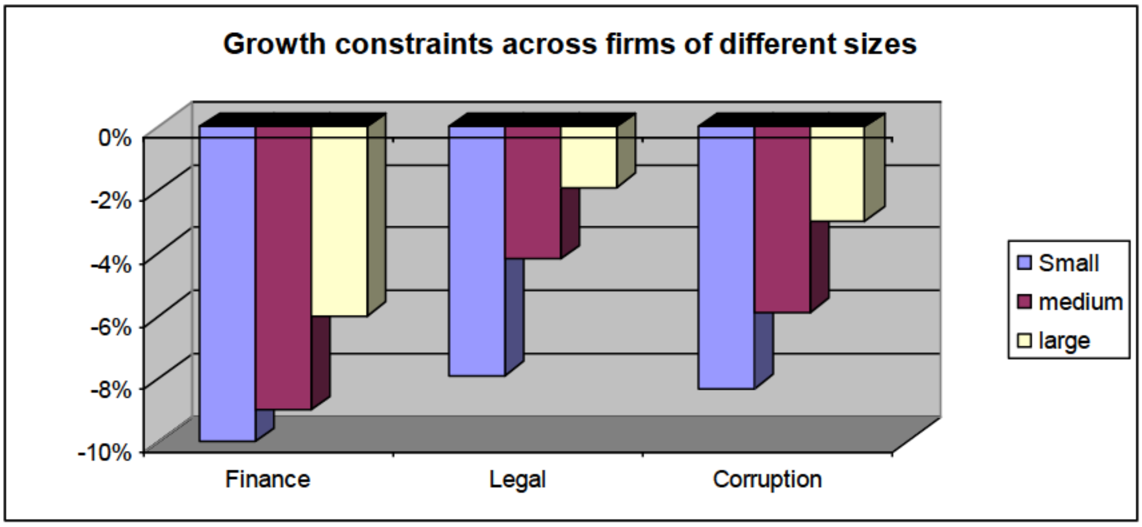


Figure 2.1: The effects of financing obstacles on different sizes of firms

Source: Beck *et al.*, 2005c

2.5 SOURCES OF FINANCE

Research shows that a number of sources of finance are available for small businesses from which to seek external funding:

- Financial markets (banks)
- Venture capitalists/ business angels
- Leasing/ renting companies
- Private investors
- Private financing companies/ trade credit
- Retail financial intermediaries
- Community clubs or stokvels
- Other (Own savings, family or friends).

2.6 LIMITATIONS OF COMMERCIAL LENDING FOR SMALL BUSINESSES

Financial markets (banks) are considered by many researchers (Demyanyk *et al.*, 2007, Carey & Nini, 2007; Beck & Demirguc-Kunt, 2006; Expert Group Report, 2006; Abor, 2010) as the main source of commercial lending. Therefore, this section will focus only on the limitations of commercial lending (**the financing gap**)

The financial gap, as identified in Section 2.2.1, depends on a number of distinctive factors that make access to finance difficult. These factors include: gender; race and age; educational or skills shortage; size of the bank; the industry; the location and the size of the business. Each of these limiting factors will be briefly discussed in the sections below.

2.6.1 Gender of the owner

Access to finance is often difficult for start-up SMMEs. Research, however, shows that it is even more difficult for female-owned businesses (FOBs) to access credit finance than their counterparts, male-owned businesses (MOBs) (Kon & Storey, 2003; and Kim, 2006). For example, Niethammer, Saeed, Mohamed and Charafi (2007) show that in Pakistan 91% of large loans were granted to men (19 000 rupees) compared to the 8 000 rupees loans, which are considered average-sized loans, that were issued to women. The authors, however, suggest that the reason behind this discrepancy can be attributed to the fact that the financial institutions have limited services to meet the needs of women entrepreneurs. Moreover, the evidence suggests that in Pakistan, as in most developing countries, women do not own land or business premises and often do not meet the minimum lending requirements. Land and business premises can be used by banks as security against loans.

The literature shows that there is no significant difference between the type of capital used during the start-up phase in businesses owned by either women or men, (Thirk, 2001) however, women are believed to commit a smaller amount of capital than men (Badulescu, 2011). Due to the high denial rates (Mijid, 2009), women tend to be credit averse and this shows in the low credit application rates. According to Coleman (2007), credit rationing is higher for women than men; and ultimately women often get higher loan interest rates. Credit discrimination against women is an indication of financial market imperfection (Coleman, 2007) but it can also be attributed to gender characteristics and attitudes in the firm’s capital structure (Mason & Harrison, 2011).

Female and male entrepreneurs generally differ in the way they finance their businesses (Verhuel & Thurik, 2001; Carter & Rosa, 1998). As reported in entrepreneurship literature, the issue of differences in financing sources is experienced more during the introductory (start-up) stage. For example, Verhuel and Thurik (2001) found that although men and women do not significantly differ with regard to the type of capital, women SME owners appear to have a smaller amount of start-up capital. In addition, women-owned SMEs begin in business with less than half of the capital amount used by men and face more credibility issues when dealing with bankers (Badulescu, 2011).

Similarly, Mijid (2009) found higher loan denial rates and lower loan application rates among female entrepreneurs. Coleman (2007) also provided evidence of credit discrimination against female entrepreneurs as they were more frequently charged higher interest rates (Carter & Rosa, 1998) and asked to pledge additional collateral before loans were granted. The literature gives various explanations for the differences between men and women entrepreneurs with respect to access to finance and these explanations can be categorised into discrimination, abilities and preferences, and competition (Harrison & Mason, 2007). Moreover, Verhuel and Thurik (2001) divided the impact of gender on SME capital into the direct and indirect effect. The former "direct effect" refers to the fact that while male and female entrepreneurs may share characteristics, they differ in the way in which they finance their firms. However, the latter "indirect effect" can be more attributed to differences related to business type, management and experience (Carter & Rosa, 1998).

Women entrepreneurs are faced with challenges in seeking start up finance, credit schemes and investment capital. The main criticism levelled against women's inability to access finance in Pakistan is, however, based on the social norm in the country where it is unacceptable for women to interact with male banking professionals. Research shows that women face discrimination from bankers. For this reason they are wary to approach banks because they lack collateral and viable business plans (Roomi, 2005). Unfortunately, women entrepreneurs in SA face the same type of discrimination from banks. Nieman and Nieuwenhuizen (2009), for example, cite Adhikary *et al.* (1999) in showing that women in SA lack finance for business start-up and that the financial institutions readily criticise their business plans without offering direction and guidance.

Proponents of this theory, such as Rau (2006) and Nwoye (2007), further agree that women have limited access to finance due to their high levels of illiteracy and their inability to develop viable business plans. In South Africa, Ntsika Enterprise Promotion Agency has, for the last decade, indicated in its workshops that women are faced with a lack of start-up finance. The basis for this can be found in the financial institutions' criticism against the business plans by women without then supplying any direction and guidance (Adhikary *et al.,* 1999). There is, however, evidence that women are still as successful entrepreneurs as men despite their challenges with regard to sources of finance and limited support systems (Nieman & Nieuwenhuizen, 2009).

Nevertheless, some researches show that there is no significant difference between the availability of finance from banks and the gender of the credit finance applicant. Watson (2001, for example, states that the mean score for loan approval by banks for male applicants is 3.84 and 3.83 for female loan applicants. The figures are generally the same, although the research sample for females was significantly smaller than for the male sample: n=13 (female) and n=52 (male). In support of this, research by Vos, Yeh, Carter and Tagg (2007) found no relationship between the gender of the firm's owner and the loan activity, both in the UK and USA.

2.6.2 Age and race of the entrepreneur

The literature on entrepreneurial finance agrees that the character of the entrepreneur plays a great role in the financing decision. For example, enterprises owned by young people and minority ethnic groups experience problems of access to start-up finance due to a perceived lack of credibility associated with them (Curran & Blackburn, 1993; Ram & Deakins, 1996; Irwin & Scott, 2010). This restriction means that anyone wishing to secure debt finance from the bank is disadvantaged if no guardian is willing to co-sign their surety. The implication is that young entrepreneurs have difficulty in accessing business finance directly from financial markets due to a lack of professional networks (Carter & Shaw, 2006).

2.6.3 Educational/ skills shortage factors

The level of education of the loan applicant plays a crucial role in the decision-making process. The level of education and business skill of the applicant determines their ability in business management and ultimately, business success, which is a challenge faced by many small businesses. (Abor, 2010) contends that small businesses in developing countries have the added challenge of a lack of management skills and training, and hence, the emerging entrepreneurs do not keep proper records of the business. Berger and Frame (2005) maintain that information deficiency is the result of audited financial statements being unavailable by small businesses. These scholars suggest that the audited financial statements yield credible financial information. Businesses that are owned by educated and experienced entrepreneurs have a greater likelihood of obtaining the needed finances (Smith-Hunter, 2006).

2.6.4 Size of the bank

The size of the bank has an impact on the availability of finance. Some academics, for example, believe that larger, more diversified banks, in particular banks that are found nationwide, have the advantage of risk-sharing that smaller and less diversified banks do not have, and this makes larger banks more accessible to small businesses (Jayaratne & Wolken, 1999; Demyanyk *et al.*, 2007). Similarly, the empirical study by Frame, Srinivasan and Woosley (2001) also found that large banks tend to charge small businesses lower rates and also less often than not, require collateral, the unfavourable situation for small business which barely have any collateral. In support of this strategy, the Asian Development Bank (2008) states that small banks are accountable for the lack of access that small businesses have to finance, although (Frame, et al., 2004) argue that issuing loans to small businesses can harm large banks that finance small businesses, as their overall costly relationship loan’s volume is reduced through price and quantity rationing.

Inversely, Godbillon-Camus and Godlewski, (2005) discovered that small businesses opt for small banks as their sources of external finance. This is in order to reduce credit rationing, given small banks’ super capacity around bank-borrower long-term relationships. In addition, while large banks are more accessible to small businesses in developed countries, it may not necessarily be the case in developing countries. In Nigeria, for instance, the opposite has proved to be true. From the study that was done on the static and dynamic effect of bank merger and acquisition on small business lending, the results showed that there was a negative relationship between merged banks and their lending to small business. The results show that for every 1% increase in the market share, the lending for small business fell by 6 694.76 naira (Nigerian currency). On the contrary, with the unmerged banks, an additional unit of naira in the bank gross total asset, increased the loans to small businesses by 47 000 naira indicating a positive effect for unmerged banks. In addition, for every one unit increase in the ratio of equity to gross total asset, small business lending increased by 300 457 naira (Emine & Okafor, 2008). The principle of behavioural finance holds that diversification minimises portfolio risk (Mpofu *et al.* 2008); the risk which in this study is associated with credit versus return. The larger the number of deposits, the more business lending increases, regardless of the actual size of the banks. Therefore, in bank credit, the more diverse the bank becomes in terms of deposits, the more accessible it becomes for small business financing.

2.6.5 Size and stage of the business

The size of the business also influences the accessibility to credit finance. Small businesses have a bigger struggle to obtain finance than large businesses have. According to Msimang (2005), there are some voids in the banks' business financing model because start-up small businesses are mostly unable to obtain financing. Berger and Frame (2006) argue that granting a loan to a micro enterprise carries enormous costs for the bank if compared to the actual size of the loan. Nonetheless, CDE appreciates that making loans to small businesses and medium enterprises can still be profitable if more caution is taken with those small businesses. The prudence that needs to be put in place here is with regard to an acceptable credit history, sufficient collateral and access to credit.

The problem of access to finance for small businesses is a well-documented area in the field of entrepreneurship, economics and management, and it can traced as far back as the 20th century (Berger & Udell, 1998; Binks *et al.,* 1992; Pettita & Stiger, 1985; Macmillan, 1930). Even today, in the 21st century, the debate on access to finance continues to be an agenda that is identified as the dominant obstacle facing the growth of the small business sector (Miettinen, 2014; Ayadi & Salim, G., 2013; Herrington, 2011; Beck, 2010; Berger, 2007; Claessens, 2006). Perhaps this trend will continue to prevail into the unforeseeable future. Ardic *et al.* (2012) show that even in countries that have high level of credit as a percentage of GDP, there are low levels of small business lending.

2.6.6 Industry

The industry in which the small business operates is another factor that influences the availability of finance for the business. Businesses that operate in manufacturing and construction are exposed to different financial needs and choices in comparison to businesses that operate in the services sector (Fatoki & Asah, 2011). According to

Mackay and Phillip (2005), the position of the business in the industry determines the financial structure. In concentrated industries, the actions of other businesses affect the business, whether it is an entrant, incumbent or existing business, as financial leverage tends to be higher and less dispersed.

Along with the position of the business in the industry, Michaelas *et al.* (1999) further argue that time and size determine the debt structure of small business. During an economic recession, small businesses are affected by short-term financial needs, while during an economic boom, long-term financial needs emerge. Similarly, small businesses operating in the agricultural sector in Ghana, as well as businesses operating in the medical industry, both have better financial options regarding long-term as well as short-term finances than their counterpart businesses operating in the manufacturing industry. Furthermore, the study shows that businesses operating in tourism, construction and mining rely more on long-term financing options and not short-term financing options (Abor, 2007).

Cowling (2010) asserts that small businesses in the start-up stage have bigger challenges regarding access to finance than in the later stages of the business because the start-up stage is characterised by high failure rates.

2.6.7 Location

According to Fatoki and Asah (2011), small businesses that are geographically closer to the banks have a better chance of relationship banking than businesses that are further away from the banks. This is consisten with the findings of Abor (2008) that businesses that operate outside the major cities of Ghana face major difficulties in attracting finance, while businesses that operate in the cities where financing institutions are located do not experience the same level of difficulty in finding financing. Okpara and Wynn (2007) cite the inaccessibility of the business to the customers and suppliers as one of the reasons for business failure in Nigeria.

In response to the challenge of inaccessibility, Reddy (2007) states that businesses choose to move to the cities although rental costs are relatively higher. Nonetheless, the high cost of rentals is less of a challenge for small businesses in Fiji than the challenges imposed by operating in the rural areas with its poor transportation and communication infrastructure that ultimately have a negative effect on the performance and growth of the businesses operating in such environments.

If small businesses are encouraged to grow they have the potential to make a significant contribution toward the economic growth and even lead to a reduction in unemployment. However, financing constraints need to be reduced (Rogerson, 2008) in order to help small businesses reach growth potential (Bohacek, 2006).

This concludes the first part of this chapter. The second part of the chapter dwells on aspects of commercial financing. The first section is focused on understanding the financing gap that exists in financial markets for small business.

2.7 THE REALITIES OF THE FINANCING GAP IN FINANCIAL MARKETS

According to Caselli (2009), the banking system is only suitable for fully developed businesses that have successfully navigated past the stages of development and start-up. This view implies therefore, that small businesses are not a market for commercial lending (Demirguc-Kunt, 2008). Caselli (2009) further states that banks are more willing to finance businesses that are in the rapid growth and mature phases than in any other phases.

The institutional regulation of the financial industry is responsible for the way the banks work. Christianson (2003) states that a large volume of research, including the National Treasury, agrees that the financial markets are over-regulated. The regulation which is based on guarding against risk and reckless lending by banks restricts the banks from comprehensively serving risky markets such as small businesses. These regulations have a greater impact on small businesses than large businesses. Beck, (2007) reports that access to finance is easier for large firms than for small firms. His study, carried out on 71 developing countries, shows that 30% of large businesses use bank finance and only 12% of small firms use bank credit.

Existing research shows that the imperfection of financial markets is biased against small businesses. A number of studies, (Dayal *et al.* 2008; Beck, 2007; Claessens, 2006; OECD, 2006; Mensah 2004; Hashi 2001) cite the following as some of the everlasting challenges that small businesses have to face from the financial markets:

- Lack of acceptable collateral;
- High risk sector in terms of lending (with a high failure rate);

- Poor creditworthiness;
- High costs of credit;
- High risk premiums;
- Small cash flow;
- High transactional costs for small loans;
- Short payment periods;
- Poor saving and credit management culture;
- Poor entrepreneurial and inadequate management skills;
- Information asymmetry and lack of track record;
- Lack of trust between entrepreneurs and investors (bank-borrower relationship);
- Limited margins for banks on small loan amounts; and
- Conservative nature of financial markets (factor of risk aversion).

The above-mentioned financing gaps are believed to negatively affect both financing institutions (supply side) and small businesses (demand side) at some point in the financing arena. While the negative effect on the latter is well documented, the negative effect on the former (supply side) is often overlooked. The financial institutions, as suppliers of finance, forego the opportunity to increase their client base. The conservative nature of the financial markets originates from the Basel II capital adequacy pillar three, which revolves around the aspect of credit risk management. Godbillon-Camus and Godlewski (2005) assert that credit risk management is the driving force behind the banks' way of doing business.

In order to be responsive to the capital adequacy framework, banks use methods that help them minimise risk. From these methods or systems, various factors result that limit access to finance for small businesses. Factors, such as the use of credit assessment systems, fail start-ups more than existing businesses as they may have limited or no credit history to prove them worthy, and hence small businesses are regarded as risky (Naim, 2008; O'Brien, 2008). Moreover, Godbillon-Camus and Godlewski (2005) show that small businesses are considered to be the most opaque, because of a lack of public information. Opaqueness is a character associated with small businesses because unlike their counterparts, large businesses, small businesses do not enter into contracts that are placed in the public domain. Neither is information available about small businesses' suppliers and customers; nor do small businesses issue trade securities that are market priced (Berger & Udell, 1998).

The other challenge that exists in financial markets is the financing terms that are presented to lenders, especially in the developing countries. The financing terms offered by financial institutions are not accommodative of small businesses. For example, Wanjohi (2010) argues that credit finance is a challenge to small businesses in Kenya because long-term finance is not available. Lack of long-term finance for small businesses forces them (small businesses) to rely on high-cost short-term financing from banks. The high costs include: the cost of credit, high bank charges and fees. Due to these high costs, small businesses cannot make enough profits and therefore cannot be competitive.

2.7.1 Understanding commercial lending

One of the functions of banks, as financial intermediaries, is to transfer resources from savers to borrowers. In transferring resources to borrowers, banks use savers' deposits to make loans to borrowers. Banks also offer other financial services for the development of financial markets (UN Report, 2001; Rungsomboon, 2005).

Commercial lending uses funds that are generated from members' savings and deposits to provide loans to borrowers. For this reason, financial markets price the loans in order to cover the costs of those funds, and hence, expect to receive returns from these investments. To achieve this, loan rates are charged based on the interest rate paid on the savings (Njuguna, 2008; Bledsoe, 2007; Beck, Siegel & Beares, 2001). This implies that the depositors are paid a specific interest rate, and that the interest rate charged on the loan will be higher. Beck *et al.* (2001) furthermore, indicate that the interest rate is the product of the principal (the amount of the loan excluding interest), rate and the time (the term money will be used) and frequency (number of payments), in this study referred to as loan price.

According to Repullo and Suarez (2004), the pricing of loans does differ according to the sources of and the relevance of customer relationships with the bank. Other researchers state that the prices of the loans depend on the models used for lending, such as the cost-based pricing model; risk-based pricing model; relationship-based pricing; competition-based pricing model, as well as the asset-based pricing model

(Njuguna, 2008; King, 2007; Diette, 2000; Basu & Rolfes, 1996). For example, if using a cost-based lending/pricing model, the bank costs for lending to both large and small businesses are high, and therefore, the price of the loan is high for either of the two types of businesses. Inversely, using a risk-based lending model, the risk profile of a large business is low (low possibility by default) (Abor & Biekpe, 2006) and as such, it attracts low loan prices, while the opposite is true for a small business which is considered to have a high risk profile (high possibility by default), and therefore, the loan prices become high as well. The same assessment and criteria are applied across all other lending models

These models are summarised in Table 2.3 (on the next page) to compare the pricing models effects on both large and small businesses, depending on how the business is evaluated against the lending model being used.

Table 2.3: Pricing models and the effects on large vs small businesses

Lending model	Large businesses/effect	Small businesses/effect
Cost-based	High/high interest rate	High/high interest rate or no lending
Risk-based	Low/low interest rate	High/high interest rate
Relationship-based	High/low interest rate	Low/high interest rate
Asset- based	High/low interest rate	Low/high interest rate
Competition-based	High/low interest rate	Low/high interest rate

Source: Researcher's own analysis and compilation

The high costs of bank loans discourage small businesses and prevent them from accessing debt finance, which ultimately impedes their growth (Beck, Demirguc-Kunt & Marksimovic (2005). Nonetheless, the table above illustrates the findings of Beck and Demirguc-Kunt (2008) that small businesses act as profit-making instruments for banks, not by increasing the bank's client base, but by increasing sales volumes through the high interest rates being charged (high loan prices). However, Kobayashi (2011) asserts that if lending to a small firm earns a negative return for the bank, the bank will not extend credit. As shown in Table 2.3 above, cost lending makes the loans very expensive for both small businesses and large businesses alike, but the cash flow of small businesses is more negatively affected than that of their counterparts, large businesses, as it can be assumed that the cash base of a small business is generally smaller. All pricing models have a negative effect on small businesses as the interest rates are always high for small businesses as opposed to larger businesses that are generally granted lower interest rates.

Financial Institutions (FIs), in particular banks, are among the most closely regulated of all the lending institutions. This means that the mix, quality and the yield of the loan portfolio of any bank are heavily influenced by the character and the depth of regulations in the industry (Peter & Hudgins, 2005).

Nonetheless, banks are discouraged by their regulator from granting high-risk loans (Wall, 2004). Conversely, banks become reluctant to grant small business loans because they are too costly. The transaction costs (in the USA) of a $5,000 commercial loan are, for example, similar to those of a $500 000 loan. The lending criteria, the client’s market assumptions and financial projects, all have to satisfy similar prudential standards (Beck, 2007; Evans, 1996); therefore, the costs of a small loan can exceed the value of the loan itself. However, Beck *et al.* (2008) discovered that banks admit that the small business segment is very profitable for them.

The National Credit Regulator (NCR) in South Africa oversees all credit activities in the financial market. The NCR was launched as the supervisory body under the National Credit Act No. 34 of 2005 (the Act) to regulate the SA credit industry. The Act necessitates that the regulator encourages the development of an enabling credit market which specifically addresses the needs of people from the historically disadvantaged groups, also from low income as well as rural or low density population communities. In addition, the regulator is commissioned to register credit providers, credit bureaux, debt councillors and to oversee that all parties conform to the regulations (NCR, 2009)

While banks are expected to be lenient in issuing credit, the banks’ priority is to guard against risk. The New Capital Accord (Basel II capital adequacy adopted by world’s banks with its three pillars: minimum capital requirements, a supervisory review process, and effective use of market discipline) requires improved banking system stability to ensure that all banks hold sufficient capital against credit risk (Butera & Faff, 2006). In addition, the Basel II regulatory framework requires banks to espouse new credit risk management procedures, which include credit-scoring models on analysing a client's creditworthiness. The three pillars of Basel II comprise of minimum capital requirement (credit, operational and market) risks, a supervisory review process and market discipline (Gama & Geraldes, 2012). The Basel II expects banks to report the risks and capital adequacy to their central banks. It further provides a standardised basis for monitoring risk and capital adequacy by the banking regulator and by banks’ counterparties, like depositors and funders. The purpose of this is to enable banks to function and also to protect their stakeholders against loss (Jacobson *et al.,* 2005).

The regulatory environment generally prescribed the way banks operate. The regulation which is based on guarding against risk and reckless lending by banks restricts banks from comprehensively serving risky markets such as the small business sector (Christianson, 2003). This challenging regulatory environment impacts more on small businesses than on large businesses, given that large firms access finance easier than small businesses, especially with regard to high interest rates, lack of collateral, information asymmetry, and others (Beck, 2007).

Even though banks are the main sources of finance, research shows that there will always be a mismatch between supply and demand for finance with regard to small businesses. There are three main factors identified from the supply side that contribute to the mismatch: risk, information asymmetry and bank regulation. Some scholars cite the riskiness of the small business sector as the driving force behind this mismatch, and hence, banks are reluctant to invest in them (Blumberg & Letterie, 2008; Beck, 2007; Berger, 2006).

Other researchers, however, cite the banking industry regulatory body which prescribes the way the banks operate, as accountable for the mismatch (Gama & Geraldes, 2012; Beck 2007; Peter & Hudgins, 2005; Wall, 2004; Evans 1994). The banks are in the unenviable position of being expected to guard against credit risk by the industry's regulatory body (Vanhanen, 2007). Previous research argues that the costs of lending to small businesses are high for banks due to the riskiness of the small business sector (Beck, 2007). Information asymmetry is another factor that has been identified, and this means that only the entrepreneur is well acquainted with the business and not the bank. This information gap (Denis, 2004) contributes to the perception that small businesses are not always reliable or credible. Berger and Udell (1998), however, argue that small businesses cannot be blamed for not publicly disclosing any information as they are not publicly traded.

Small businesses (demand-side), however, consider the fees and transaction costs charged by banks as too high (Okeahalam, 2001). In addition, small businesses themselves have limited information on how financial markets (banks) operate (Demyank *et al.,* 2007).

Although the majority of researchers blame the imperfection of the financial markets for the mismatch (Njuguna, 2008; Bledsoe, 2007; Beck *et al*., 2005; Beck *et al.,* 2001), banks' shareholders expect their businesses (banks) to generate income and increase their profits. All businesses are profit-driven, and as such, banks cannot afford to expose their funds to risk by issuing credit to a market perceived as risky.

2.7.2 Tools used in commercial lending

Banks use various tools and methods in their processing of loan applications. A credit assessment usually involves some basic methodology of evaluating the business and household cash flows (Jekwa, Whitfield & Kelly, 2007; Enterprise Toronto, 2008). In order to assess whether a potential borrower will default, the lenders use credit scoring. For the purposes of this study, credit scoring and loan pricing will be used as examples of the tools banks in processing business loans.

2.7.2.1 Credit scoring

Financial institutions use credit scoring as the main tool for evaluating loans. This is the process of assigning a single quantitative measure or score to a potential borrower. The credit score is used to determine the future performance of the loan and to reflect a relative chance of default (Wall, 2004; Frame *et al.,* 2004; Frame *et al.,* 2001; Feldman, 1997). According to Estes (2006), the use of credit scoring was developed by Bill Fair and Roger Isaac in 1958, and it was initially used to derive the mathematical probability of a borrower being able of paying back the debt on time. The two founded the company called Fair Isaac Corporation and developed this credit scoring model. This process is predicated on five factors:

- Borrower’s payment history;
- The level of outstanding debt;
- The length of credit history contained at the credit bureau;
- The number of credit inquiries on the report; and
- Types of credit at present.

In order to accommodate small businesses in the lending market, Fair Isaac developed the business credit scoring in 1995. Banks are still using the credit scoring model to make sound business lending decisions, where the higher the score the more favourable the decision will be for the business.

Frame *et al.* (2004) highlight that credit scoring is an important loan evaluating tool. Firstly, because it helps financial services to determine the credit risk associated with a borrower. Secondly, it ensures the maximum profit and security for their loan portfolios. Credit scoring, in addition to the above, helps the lender to underwrite and monitor loans without actually meeting borrowers. Institutions that use credit scoring have a competitive advantage over others in the small business lending arena. For example, Drechsel, in Harrison (2009), reflects that his company's ability to credit score the customers of his own clients on an individual basis, has made the company more competitive as the function is in high demand. Most importantly, Harrison (2009) found that the use of credit scoring helps banks to lower the underwriting costs and also to improve the accuracy of the credit evaluation. The law of supply stipulates that the lower credit costs lead to increased supply and hence, lower prices for credit. On the other hand, many authors have argued that banks using traditional underwriting methods may increase the costs that may lead to increased pressure on credit prices.

Similarly, Berger and Frame (2005) emphasise that the use of credit scoring in small business (SBCS) in the US reduces costs, which ultimately increase the availability of credit from banks. The results further reveal that the reduction of costs increases credit availability when banks use small business credit scoring, rather than the reduction in information opacity. Interestingly, the study shows that SBCS helps banks to maintain low-risk small business credits. This implies a low loan price for SMMEs, an element of risk-based loan pricing.

2.7.2.2 Pricing of commercial lending

Research shows that although loan pricing models set the precedence in determining loan prices, other factors such as: (i) administration costs; (ii) market risk; and (iii) credit risk affect loan prices. According to Repullo and Suarez (2004), the pricing of loans differ according to the sources of and the relevance of customer relationships with the bank. Whereas other researchers argue that the pricing of loans depends on which pricing models are being used, such as: the cost-based pricing model, risk-based pricing model, relationship-based pricing, competition-based pricing model, and the asset-based pricing model (Njuguna, 2008; King, 2007; Diette, 2000; Basu & Rolfes, 1996).

The following section observes the different factors that influence loan pricing. It is imperative to understand these factors in order to justify the rationale behind the prices of loans which are perceived by loan applicants as being high. Loan prices are based on costs, risk, product relationship and competition.

(a) Cost-based loan pricing model

Cost-based loan pricing is considered as the simplest model. According to Diette (2000) and Njuguna (2008), the model is based on the assumption that the interest rate of any loan is a function of four components, which are:

1. The funding cost incurred by the bank to raise funds from the depositors through the money market facility.
2. Operating costs of servicing the loan, including appropriate repayment processing, bank's wages, salaries and other expenses, such as monitoring, statements and collections.
3. Risk premium for compensation of the bank's degree of commitment inherent in the loan request.
4. Profit margin provided by each individual loan made by the bank from its capital.

Loans are priced based on all revenues, including the interest income and any fee-based income. All these revenues are spread over the life of the loan, with the consideration of the amortisation.

Njuguna (2008) further states that the bank's clients invest their money in order to get a return on their investment. This return is also calculated in the loan price.

(b) Risk-based pricing model

Risk-based pricing is the loan pricing strategy that is made in parallel to the expected loan risk. The riskiness of the loan is based on the credit risk of the borrower's ability to pay back, which predicts loan acceptance or rejection. The riskiness of the applicant determines the price of the loan should the application be accepted (King, 2007). Should the bank perceive that the SMME has a high probability to default; the loan issued gets priced at a higher rate than for the firm with a low probability to default. The risk adjusted rate is meant to compensate the lender for the possibility of default.

Banks use depositors' funds to offer loans (Caselli, 2009). Therefore upon issuing loans which are meant to generate profit for investors, depositors need to be protected against the loss of funds (default risk). According to Zoeb (1993), when determining the prices of the loans, banks deliberate on factors such as credit-risk premium, default risk, lending rate; loan type and risk return (Caselli, 2009).

(c) Relationship-based pricing model

The prolonged relationship between the client and the bank plays a role in the availability of funds. Banks are able to analyse the loan applicant based on the client's track record. This ability may give the client a comparative advantage over another client, and hence, minimises the risk factor of the loan applicant, implying a lower interest rate.

(d) Competition-based pricing model

Competition as a loan pricing function depends on the position of the bank in the market with regard to whether the bank is a price leader or price taker. Even though in the highly concentrated market, the price leader sets the price, because the business loan market is highly competitive, the lowest price competitor usually drives down loan prices in the market (Basu & Rolfes, 1996).

The Farm Credit Administration (2000) suggests that it is good business practice to continually observe the competitors' pricing of their loans, and it is helpful in any bank's loan-pricing system. The essence of this is that the extent to which the competitive financial market operates varies between various types of lenders. These lenders have different rates across different loan products that are updated throughout the year (www.fca.gov). This theory highlights that if the market is not appropriately and timely monitored, pricing below market may prevail. The below-market pricing may mean pricing deficiencies and unsafe and unsound practices for the bank.

(e) Asset-based pricing

Asset-based pricing is used to determine the price of the loan with the incorporation of the liquidity of the asset pledged. The more liquid the asset is, the less the price of the loan, because the asset can be easily converted into cash should the client default.

2.8 DEVELOPMENT FINANCE FOR SMALL BUSINESSES

The primary role of development finance institutions (DFIs) in the under-developed and developing economies is to address and bridge the gap in domestic fiscal and term-lending capabilities. The finance gap arises as a result of a number of factors including market, political or bureaucratic imperfections, and asymmetry associated with financial risk. The inefficiencies of the financial markets include their unwillingness and inability to bear the risk of providing capital to clients that are considered uncreditworthy (Masusike *et al.*, 2004).

ILO (2016) agrees that although financing is difficult for businesses in the development and start-up stages, the difficulty does not relate to the unavailability of funds (Kritzinger, 2002). Therefore, even in the midst of difficulty, financing still exists for the sector, and small businesses need to be on the lookout for such financiers.

According to the OECD (2015) bank lending is the most popular source of finance for many businesses, particularly SMMEs which rely heavily on debt for start-up finance, cash-flow and operation costs. However, due to the high risk profile associated with small businesses, bank financing is a challenge for entrepreneurs. Before making any financing decisions, entrepreneurs are advised to do proper planning in line with questions such as the following:

- How much finance is required?
- When and how long is the finance needed for?
- What security (if any) can be provided?
- Whether the entrepreneur is prepared to give up some control of the business in return for investment?
- In the planning process, these keys areas need to be addressed:
  - Set up costs;
  - Starting investment in capacity (fixed assets that the business needs before it can begin to trade; and
  - Working capital (stock needed).

2.8.1 Approaches to development financing

In order to address the inefficiencies of the financial markets (or the financing gap), the DFIs look out for different approaches through which to make finance available to the financially excluded clients. According to Masusike *et al.* (2004), the capitalisation of the DFIs consists of public sector equity and fiscal transfers supplemented by mostly loan or grant capital from private and donor sources. The capitalisation enables the DFIs to provide their prominent package services of development banking, such as extending loans finance on beneficial terms to revenue-generating ventures and projects; and to the people who cannot access finance directly. Some of the duties of the DFIs include:

- To reduce the cost of capital to borrowers through the partial transfer of a subsidy of the interest rate or maturity or grace periods;
- Asset and liability matching finance; and
- Stipulating less burdensome collateral requirements.

Moreover, co-funding with the DFIs benefits not only the borrowers (the poor and un-bankable clients) but the partnering institutions as well. The DFIs have the advantage of better understanding developmental risks and are therefore insensitive of higher risk which can be overridden by their strong risk rating (Masusike *et al.*, 2004). Some of the approaches which the DFIs use in assisting the financially excluded communities include: co-funding; grants, and equity finance, as explained below.

a) Co-funding

The DFIs are usually faced with budgetary constraints in reaching out to financially excluded enterprises that require capital. Research shows that the DFIs overcome these budgetary constraints by intermediating between other institutions such as financial markets and international funders (Masusike *et al.*, 2004).

b) The use of credit guarantee schemes as a form of development finance

Some researchers state that without collateral and a credible track record (information asymmetry) any financial support for business growth is not possible. Therefore, government introduced facilities such as the credit guarantee scheme to help bridge the gap (Beck *et al.*, 2010; Cowling, 2010; Abor & Biekpe, 2006).

In addressing the finance gap challenge that exists between commercial banks and small businesses that are considered not bankable, government had to intervene through good practices and policies and developed some partnerships with banks. For example, the Commission for European Communities (CEC) (2006) recommended a partnership with banks through the use of credit guarantee schemes. This is the model where governments provide surety that can be used to recover the bank losses which may occur as a result of payment default by the loan applicant (entrepreneur).

For policy makers the facility of credit guarantee scheme operates as a development finance instrument to accelerate lending for priority sectors, such as small businesses. For borrowers (small businesses), the facility improves access to finance and inclusion into the financial markets where the former can obtain finance for working capital (Rogerson, 2008), fixed and investment financing at favourable terms (loan prices) which would otherwise not have been funded. With appreciation that the growth of small businesses has the potential to make a significant contribution toward economic growth and the reduction of unemployment, financing constraints need to be reduced to help small businesses reach growth potential (Bohacek, 2006).

Credit guarantee schemes serve as an indemnity that is used to secure the bank loan for the small business with no collateral (Khula, 2007), and are important instruments that facilitate the achievement of national economic goals through enabling entrepreneurs access to finance for both venture creation and development (Samujh, Twiname & Reutemann, 2012). The credit guarantee scheme is believed by Oh *et al.,* (2009) to provide financial support to small businesses that lack sufficient investment from private financial institutions due to market failures and lack of collateral. Furthermore, the guarantee schemes help to increase the accessibility to private finance and enhance the competitiveness of small businesses. Therefore, credit guarantee helps reduce the risks of lending to small businesses.

Research shows that the main reason for the low supply of finance to small businesses by banks is associated with the risk factor of lending to the small business sector. Credit guarantee schemes therefore share the risk between the bank and the guarantee institution in an agreed ratio. In this way, the bank's risk and operation costs are lowered, while at the same time its returns are increased (Nigrini & Schoombee, 2002). In the process the banks are encouraged to participate more in small businesses lending than they would otherwise do. To minimise their risk, banks expect the borrower to provide collateral in the form of a fixed asset or machinery, which in most cases, small businesses in developing countries, including SA, do not possess. In South Africa the risk is shared (80:20) between the government, through its agency, SEFA and the bank. Meanwhile in Japan, the government covers 100% of the loan and the bank does not incur any risk (Wilcox & Yasund, 2008). Samujh, Twiname and Reutemann (2012) further show that risk sharing between government and the lender differs from country to country, for example, in the USA, (90:10); Malaysia, (70:90: 30:10); and Egypt, (70:30).

c) Microcredit

Microcredit is a form of development finance that is aimed at addressing the challenges of poverty. Research shows that microcredit is considered as a tool meant for poverty alleviation (Atapatti, 2005; Grameen Bank, 2012; Cooper, 2014), as well as a means to facilitate sustainable economic development (Khavu, 2010; Bernard, 2015). With the use of donor and public funds, governments, in an attempt to facilitate economic growth, established institutions that provide reduced-cost, risk-associated, as well as non-collateral seeking small loans to the poor (Khavu 2010).

2.8.2 Development financing and regulation

Development finance institutions, to date, are following the banking principles and regulations stipulated by the same regulator of commercial banks. For example, the Development bank of Southern Africa (DBSA) states that the institution is expected by the banking regulator to balance sustainable development impact and financial sustainability as proof that the institution complies with sound banking principles. The DBSA further alludes that the investment credit ratings underpin the borrowing strategies of the institution which help in placing the profile of the institution in international financial markets. However, the DBSA states that the role of development financing and development assistance (advising) are still being fulfilled by them (DBSA, 2004).

2.9 CONCLUSION

This chapter presented a review of the appropriate literature to provide a perspective on the main concepts as applicable to the current study. Issues pertaining importance, as well as the challenges facing the growth of small businesses were discussed in this literature review chapter. The issues of finance formed an integral part of the chapter to establish an understanding of why the access to finance is a dilemma for small businesses in the financial markets. Different factors influencing challenges of access to finance were displayed in the current chapter; including different pricing models as practiced in the financial markets. After illustrating the holistic overview of small businesses and commercial lending, the chapter then provided an overview of development financing as the backbone of the study and presented the approaches to financing available to the small business sector. Although not exclusive, different sources of development financing were discussed in the second part of the chapter. The final part of the chapter was based on the regulation of development finance institutions. The chapter also discussed the regulatory body of South Africa (NCR) in order to highlight how the country expands and subscribes to the Basel regulation. The next chapter focuses on the theories relevant to this study.

CHAPTER 3: THEORETICAL FRAMEWORK OF THE STUDY

3.1 INTRODUCTION

This chapter presents various theories that have been developed by researchers in the field of entrepreneurship and management. The aim of this chapter is to provide the current study with a solid foundation, and in so doing to connect the chapter to previous research in the field regarding theories that assume to be relevant to business growth. This chapter is based on business growth and relevant theories; highlighting the five theoretical viewpoints: entrepreneurial traits; competitive; strategic; resource-based; as well as environmental perspectives, with a specific emphasis on the theory of business development (business life cycle and structurist theories) which takes precedence over all the theories of business growth in this study. The theory of business development incorporates the theory of complexity, followed by growth strategies applicable to small businesses in order to understand the financial requirements needed for each stage of business development.

3.2 BUSINESS GROWTH AND RELEVANT THEORIES

Although the concept is extremely important in the field, researchers hold different views regarding the definition of business growth, which can be seen as a measure of performance (Baum, Locke & Smith, 2001). According to Wiklund, Patzelt and Shepherd (2009), growth implies a change in size from one period to the next. Some scholars in entrepreneurship believe that measures of business growth refer to increases in the number of variables: employment, sale volumes, value, and sales against competition. Kumar, Balboldh and Reddy (2012), agree that an increase in sales is an element of business growth, but argue that other elements of business growth include an increase in output, capital, and product capacity. Dilling-Hansen (2010) includes performance to the size and age elements of business growth, but similarly maintains that the size is measured by the number of employees.

Ridding, Madill and Haines, (2006) note that in understanding the theory of business growth, the main components need that need to factor in as assessment variables: the entrepreneur's profile or characteristics; the resources of the business; and the market. The Schumpeterian growth model highlights three key issues: an increase in market size, the exchange of information, and the reallocation of economic resources across sectors and R & D. The model indicates that an increase in these three factors results in long-term rates of innovation and growth (Schumpeter, 1934). Similarly, the integrative growth model of Wiklund *et al.* (2009) show that entrepreneurial orientation, environmental characteristics, firm resources, and the personal attitudes of the manager, all influence business growth, whether directly or indirectly.

3.2.1 Entrepreneurial traits

Wiklund *et al.* (2009) believe that business growth depends on the degree of entrepreneurial activity: the innovativeness, competitiveness, as well as risk-taking ability of the manager/ entrepreneur. The concept of strategic orientation maintains that entrepreneurial traits are equally important in the multidimensional model of Baum, Locker and Smith (2001). The model suggests that the individual, organisational and environmental domains are good predictors of small business growth. However, Rasmussen *et al.* (2014) argue that although competitive advantage and business performance are closely associated to the entrepreneurial competencies, those competencies that are needed to initiate and sustain performance are not clearly identified.

According to Hofstand (2007), on the anticipation that the owner does not possess enough assets to enhance growth, a possible solution to ensure the success or expansion of the business is through borrowing or hiring (the risk-taking ability). The success of this viewpoint rests solely on the strategic intelligence of the entrepreneur. A similar view is found in Hamilton (2001) who holds that some entrepreneurial traits, such as education, innovativeness, and planning have a positive influence on the successful performance of the business. These traits imply that the entrepreneur has adequate experience of the industry, which is a factor that enhances small business growth and development. The assertion of entrepreneurial traits theory is therefore: the performance and growth of the business is the result of the entrepreneur’s experience and management skills in business decision-making (Hamilton-Coplin, 2002).

3.2.2 Competitive strategy perspective

Competitive strategy perspective asserts that business growth depends on the strategic approach chosen for the business (Porter, 1980). Based on Porter's theory, the perspective of competitive strategy identifies low cost, differentiation and focus as the three broad business-level choices (Baum, Locke & Smith, 2001). Firstly, low cost strategy seeks to minimise costs as far as possible within all functions of the business through the construction of efficient scale facilities. The motive behind cost reduction is to target a large audience of customers who are usually price sensitive. Secondly, differentiation focuses mostly on the distinguishing attributes of the business products that demand premium prices, the direct opposite of the low-cost approach. The audience targeted by differentiation are on the look-out for quality and are willing to pay premium prices.

And lastly, focus strategy is aimed at serving specific needs to a distinguished and small market. Since the target market of the focus-based strategy are price insensitive, businesses following this approach have the tendency to demand higher prices. However, since businesses are motivated by market dominance and profit maximisation, a combination of both low-cost and differentiation is considered the best approach for business growth (Porter, 1980).

3.2.3 Resource-based perspective

The resource-based view is a theory which underpins that the fundamental basis for performance and competitive advantage for a business is the attribute of costly-to-copy (Barney, 1986). The ability of the business to capture and maintain a profitable market position (Conner, 1991) relies on underlying resources crucial to production and distribution. To distinguish from other performance theories, the resource-based perspective maintains that the performance of the business depends greatly on resources possessed by the business which include financial resources and personnel competencies. Gupta, Guha and Krishnaswami (2013) cite Penrose (1959) that both the internal and external resources of the firm assist in achieving the competitive advantage. Similar to entrepreneurial orientation, the resource-based view theory shows that the ability of the managerial personnel to successfully execute the plans with the available financial resources form the basis for business growth.

Rahaman (2011) argues that an increase in the number of employees and the sales volumes define business growth better, however further highlights that employment growth is also determined by the level of capital intensity employed in an individual firm. The debate implicitly shows that business growth involves an increase or a positive change in one or more of the business assets (capital, employees, product and capacity) over a period of time. The theory articulates that the competitiveness of the firm lies mostly in the effective use of the valuable resources, both tangible and intangible, that the firm possesses (Wernefelt, 1984). The latter has the potential to provide the firm with a competitive advantage on condition that the mentioned resources are heterogeneous (Peteraf, 1983); cannot be easily imitated and are not substitutable (Barney, 1991). Proponents of the resource-based perspective argue that because some resources are more important than others, the former tend to give the business a competitive advantage.

The resource-based view, which is skewed towards the theory of competitive advantage, argues that the success and maximum performance of a business depends on the possession of main resources that have value; are difficult to duplicate; and have appropriability as characteristics. According to Conner (1991), in order to be successful, a business requires either a distinct product which is differentiated, or a competitive cost advantage over its rivals. However, the special attribute feature of the product only factors in for the business if the customers recognise the feature as distinctive; and the role of marketing becomes a crucial aspect in achieving this awareness. As suggested by Siu and Kirby (1998), marketing is an important tool for the resource-based view.

In their model, Wiklund *et al.* argue that the most important resource for business growth is finance, as it facilitates the use of tangible assets, intangible assets, business capabilities, distinctive capabilities, and core competencies. The resources are deemed valuable if they meet the following: they add distinctive value to the business; they demonstrate an element of superiority; and scarce resources are always valuable to the business (such as distinctive skills, or financial resources which are usually a challenge for businesses). Resources that are not easily imitated add value to the business and valuable resources provide the business with the capability to exploit the opportunities.

As the resource-based view places more emphasis on resources for the growth of the business, the researcher believes that the theory is more applicable to established businesses. The latter seek growth through using the competitive advantage of the firm's distinctive resources, the attribute that is absent in emerging businesses. Therefore, the theory for being applicable to a selective group or category of small businesses and not being inclusive cannot, in the view of the researcher, be considered the best theory for holistic small business growth.

3.2.4 Integrated business growth model

The theory of integrated business growth model (Wiklund *et al.*, 2009) assumes that business growth is a function of a number of factors: entrepreneurial orientation, environmental characteristics, firm resources and the manager's orientation.

Mao (2009) qualifies the three connotations of business growth: (i) the time property of business growth; (ii) the dynamic property of business growth; and (iii) the unification of quality and quality of business growth. Time property relates to the long periods in which the business's process of development is observed in the long-term. The growth process of the business is not linear, rather the process transits from balanced to unbalanced, from stable to unstable, and hence, dynamic property. This aspect of the integrated growth model differs in perspective from life cycle models which assume that business growth is a linear process (Gupta *et al.*, 2013). In terms of the unification of quality and quality in the business, the former relates to innovation, and the ability to progress from immaturity to maturity of production technology, along with the optimal efficiency of both investment and output.

3.2.5 Theory of business development (Structuralist theory)

Development in respect of business is defined as a process or an act of growing a business over a period of time to become larger or more advanced; an evolvement with a gradual advance through evolutionary stages (www.merriam-webster.com). Incorporating the view of Adelman (1999), business development is a growth process that requires the reallocation of factors of production from low to high productivity. Greiner (1972) asserts that businesses undergo different stages of growth: creativity, direction, delegation, coordination and collaboration. This theory suggests that at each stage the business experiences a period of growth and reaches the peak which ends in a management crisis. The crises are addressed by introducing new structures (Mahalanobis, 1953) and programmes which allow for revitalisation and ultimately the evolution of the new stage (Bates & Khasawneh, 2005; Freel & de Jong, 2009). Thus, evolution and revolution are realities of business development theory, the theory that forms the basis for the business life cycle perspective. The structuralist view of development theory (Mahalanobis, 1953) stipulates that countries change their institutional structures which are not traditionally effective (financial markets) enough to provide financial and non-financial services to small businesses. This structural paradigm suggests that government has a role to in developing its people through expansion of new approaches that will eliminate the gap that exists for neglected sectors (small businesses) of the economy (Contreas, 2004: Portes, 1989)

In the next sub-section the relevant theories related to business development will be discussed in more detail.

3.2.5.1 Business life cycle or complexity view

Business life cycle theory assumes that business growth is a constant and predictable process similar to the human life cycle from birth to death. Timmons (1999) argues that conventional models, such as competitive strategy and psychological models, do not necessarily work on the analysis of developmental process of start-up. Timmons cites a number of reasons why these models are not compatible with the development of start-ups:

(i) Although the models seek to isolate the universal factors that enable the success of start-ups, the approach is not comprehensive for the whole development process;

(ii) Attempts by economics and management researchers left out or devoted little attention to the key issues of the development and performance of start-ups, therefore rendering the models inadequate; and

(iii) The models ignore the fact that the world in which start-ups evolve do not have determinacy, predictability, stability and constancy. The ever-changing environment causes the next stage of the life cycle to be unpredictable, and therefore it may yield completely different results of the linear process than those anticipated.

On the one hand, business life cycle theory views the process of start-up development holistically, assuming that businesses are stable, environments are predictable, and the only exception is change. On the other hand, the theory of complexity assumes an individual view of businesses which are fickle; with environments that are volatile and where change is inevitable. While the two theories differ in principle with regards to predictability and linearity of the start-up businesses, the two aspects are believed to be applicable for development financing strategic decision. On incorporating the theory of complexity into the perspective of business development, Tsai and Lan (2009) assert that unlike the life cycle view which assumes a progressive development for business, complexity views start-up development as both a nonlinear and chaotic process. Unlike the theory of the business life cycle which advocates for a linear process (Kat & Gartner, 1988), complexity theory (Slevin & Covin, 1998) factors in the impact of environmental change over the life of the business. Nonetheless, regardless of factors that each of the views incorporates in the development process of the business, both perspectives agree that business development occurs in different stages of the business life (the business life cycle).

Table 3.1 shows the theory of business development in comparison with the perspectives of the business life cycle (BLC) and complexity theories (CT).

Table 3.1: Business development view of BLC and CT

Theoretical View	Business Life Cycle view	Complexity Theory view
Basic assumptions	- Holistic viewpoint - Stability - Predictable environment, change is an exception	- Individual viewpoint - Instability - Unpredictable environment, change is inevitable
Main arguments	- Start-up development is a progress and predictable process - The process is unique for each stage requiring unique management skills including decision making attributes - Each stage has its own dilemma and survival is dependent on whether the entrepreneur can manage the crises - Entrepreneur can predict potential problems and develop responsive strategies on time	- Start-up development is a chaotic process - The process is a series of emerging orders, the business displays disjointed growth - New order can only be exhibited when transitional challenges arise for the business - Advance plans are not easy to formulate for unpredictable emergence of order. However, industry's learning curve can be utilised as a source of reference

Source: Adapted from Tsai & Lan (2009)

Research shows that the process of business growth is a complex phenomenon that imposes crises for the business at different stages as identified by the growth model. Churchill and Lewis (1983) maintain that every stage of the business life cycle is confronted by a different set of needs. Greiner (1972, 1998) holds that the two views of business development are interrelated since the growth process generates complexity during each phase of evolution. Both business life cycle and complexity views are not necessarily conflicting, however, both require that the business take the necessary managerial steps to alleviate problems brought on by the crises.

Timmons (1999) suggests that the business development is crucial during the first six years of start-up.

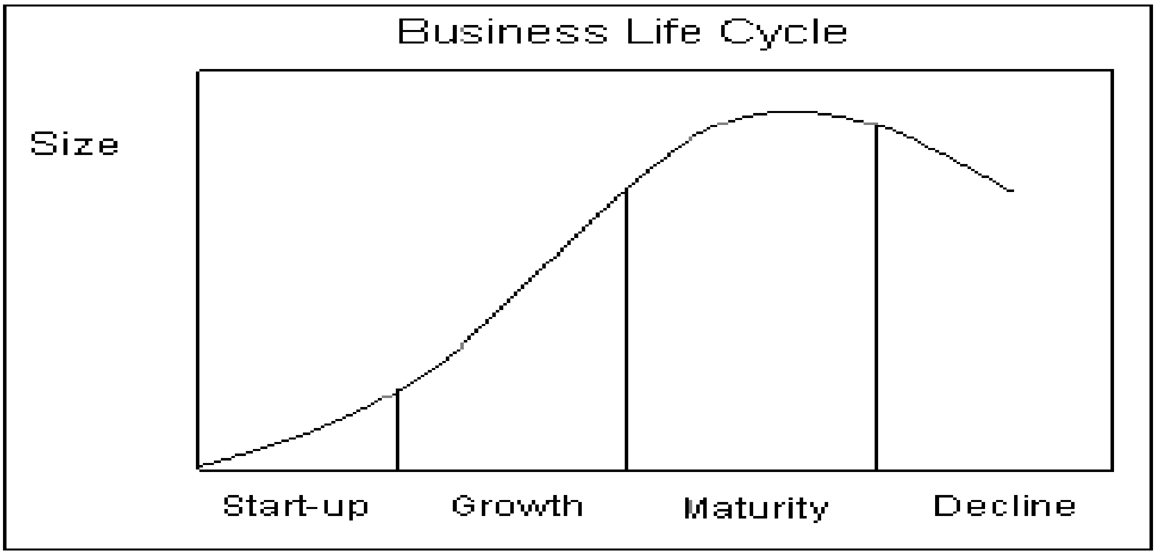


Figure 3.1: Business life cycle curve

Adapted from Payne (2007)

The curve in Figure 3.1 shows that businesses evolves from a start-up with the size of the business close to 0 as the business has almost nothing; the funds either borrowed from the owner's own savings or from elsewhere (Payne, 2007). Gradually the business begins to grow and moves to the second phase which is referred to as the growth stage where it faces lots of challenges, such as hostile competition, and to survive, the business needs to have enough financial resources to help attain its competitive edge.

Business experts and academics agree that business has four stages in its life: (i) introductory or infancy; (ii) growth; (iii) maturity; and (iv) decline stages. Nonetheless, there is an argument that for small businesses, the last stage does not always imply that the business will cease to exist, but it can also be revived or sustained as shown in Figure 3.2 on the next page. The figure provides an illustration of the different phases the business goes through from evolution to maturity where the entrepreneur has three options: to sustain the business in its current state, to revive the business and grow further into a bigger business; or to quit and leave the business.

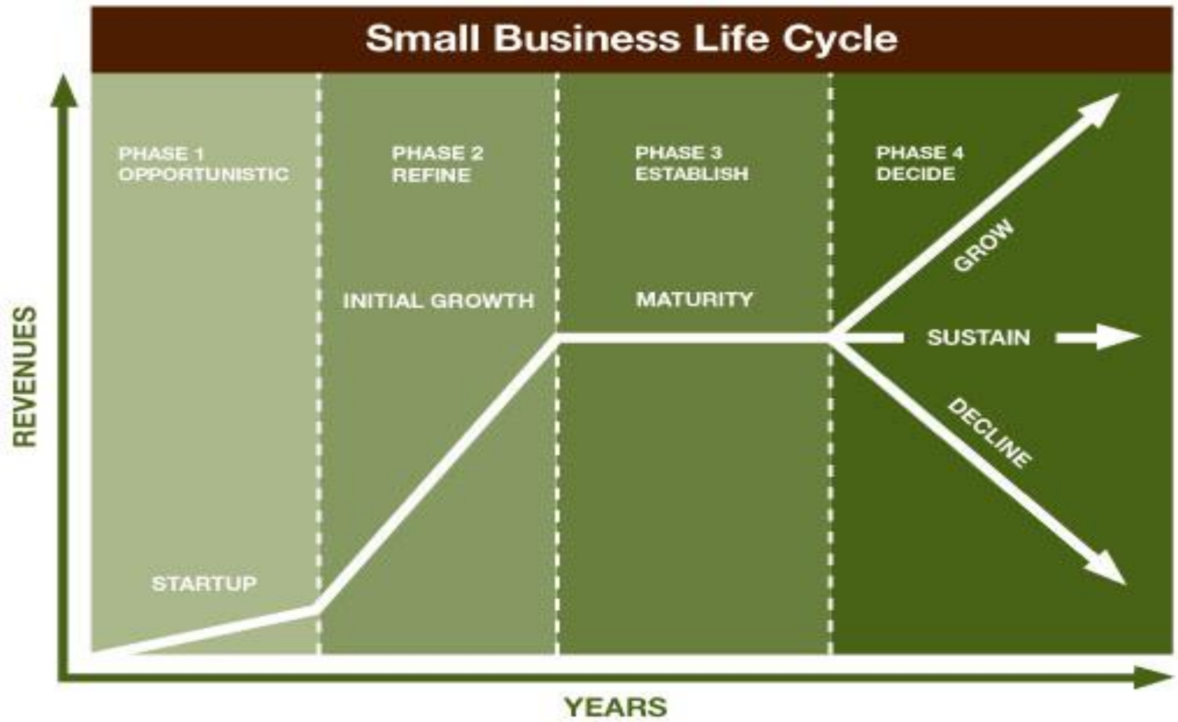


Figure 3.2: Small business life cycle

Adapted from North Hike LLC (2010)

Caselli (2009) states that during the first stage, the entrepreneur deals with the development of the business idea into operation. The functions of compulsory investment, profitability and cash flow are negative since sales do not exist during the first stage. Various activities are required for the development of an idea into operation, and these include issues such as: idea generation, legal and fiscal advisory costs, and engineering development. The revenue curve is therefore below zero point, implying a negative return to investment. Over a period of time after the business has been launched, sales begin to emerge, however, the revenue generated (cash flow) from sales is not enough to cover the operational costs. The business continues to operate at a loss until it reaches a break-even point, after which profits begin appear and where the revenue value becomes greater than zero, an early growth stage.

3.2.5.2 Business growth, strategy and competence

Some scholars emphasise competence (skill), strategy and business growth. Churchill and Lewis (1993) stress that a business lacking in managerial capabilities is at risk of failing because the owner-manager is considered an important growth factor, ahead of all the other factors (Greiner, 1972). According to Bhide (1996), during the initial stages of the business, the entrepreneurs focus on short term opportunities, however, after transitioning successfully from the survival to growth stage, the entrepreneurs are supposed to place more emphasis on long-term growth strategies. The entrepreneurs also have to integrate the business policies and visions with aspirations and personal interests and long-term strategies. For the intended purpose to be achieved, the strategy must be clearly defined and support the decision-making towards the growth of the business.

3.2.5.3 Growth strategies and business growth

Weinzimmer (2000) states that consideration of growth strategy is an important approach in determining business growth, because a business that has a solid growth strategy, as Bhide (1996) asserts, can withstand the problems of poor leadership. Otherwise, poor strategic growth plans render the business a failure even in the presence of strong organisational structures and control systems. Growth strategy is a method whereby a business aims to win a larger share of the market. The financial situation of the business is the most important factor this method depends on, alongside the competition and government regulations. In mastering growth strategy, the business needs to clearly incorporate the following three fundamental aspects:

- Target market;
- Product to be delivered to the target market; and
- Development channels to be adopted to find, acquire, and grow the target market.

Initially, the business needs to establish the potential target market in terms of the psychographic and demographics of customer segments. Along with the identification of the target market, the business must have a detailed set of activities to design, create and deliver the product to the target market. Ultimately, the business must have the development channels to create and deliver the product to every member of the target market. Development channels include the approach to reach the market, to understand and test the given product (McKaskill, 2010).

3.2.5.4 Steps in achieving sustainable growth strategies

Small businesses have low survival rates, with only 50% surviving more than five years, and just about a third of start-up businesses survive to ten years in any given time. Acknowledging this reality, Biederman (2015) contends that without growth strategies small businesses cannot show sustainable growth and are bound to fail. The following steps need to be adhered to for the business to achieve sustainable growth:

1. Establishment of a value proposition;
2. Identification of ideal customers;
3. Defining key competitors;
4. Verification of revenue streams;
5. Keeping track of the competition;
6. Focusing on own strengths; and
7. Investing in talent.

To ensure sustainable long-term growth for the business, an entrepreneur firstly needs to recognise the attributes that set the business apart from similar businesses. These are the distinguishing features that make the customers buy the specific product or service offered by the business. The entrepreneur needs to understand the feature that makes the business relevant, different and credible. The feature needs to be used to attract other customers that were otherwise not buying from the business. During the start-up stages of the business, entrepreneurs can focus on short-term plans but after transitioning successfully into the growth stage from survival, the focus needs to be on long-term strategies. The strategies must integrate the entrepreneur's aspirations and capabilities, together with business policies in pursuit of business growth (Bhide, 1996).

Secondly, an entrepreneur must identify the ideal customers. The business is set to address the needs of a specific market. To achieve the stated goal, the entrepreneur needs a clear vision of who the customers are, as well as their need for the product or service. A continued re-examination of customers' needs have to be done in order to make appropriate adjustments to stimulate growth.

Thirdly, the key indicators that affect business growth have to be defined. In the business world, change is inevitable. Change must be measured in order to ascertain effectiveness and to appropriate time and money. Comparing current business performance against previous performance is a valid test to measure change.

The fourth step in achieving sustainable growth strategies is a verification of revenue streams. The verification helps the entrepreneur to check if the current revenue streams are sufficient to make the business profitable, and to explore other potential revenue streams to make the business more profitable. The entrepreneur needs to be able to differentiate between offerings that have revenue stream and offering that do not possess the desired attribute. However, caution needs to be taken with offerings that do not necessarily provide a revenue stream but indirectly have a positive influence on other revenue streams.

The fifth step relates to competition; a closer look at the competition allows the entrepreneur to know if the competitor is excelling in areas which the business might be battling with. Learning how the competition exploits new ways that earn the best performance can help the entrepreneur with exclusive ways of creating informed growth strategies (Bhide, 1996). In order to best achieve this step, the entrepreneur must be willing to seek help to reap benefits from the available options, including repositioning the business.

To focus on own strength is the second last step in creating sustainable growth strategies. Exploiting the strengths of the business and not focusing on the weakness is a better alternative to establish growth strategies. This sixth step entails creating an own environment that matches the capabilities of the business and which can be built upon in order to grow the business.

Finally, the entrepreneur must invest in talent. The employees, as the first line for every small business, have direct contact with the customers; and as such, the business needs to employ motivated people who are inspired and have the value proposition of the business (Robert & Kimball, 2009). The best way to succeed in this step is to employ a few employees, pay them good salaries and buy cheap furniture. Rewarding the employees with the best salaries the business can afford is more valuable to the business than luxury furniture and holidays and parties.

Creating growth strategies is not a once-off exercise but a continuous process that needs to adapt and to change with an appreciation of the past. While the successes and failures of the past do not determine the future, reference to the past can be beneficial in developing informed growth strategies (Biederman, 2015).

3.2.5.5 Types of growth strategies

The characteristics and the environment of the business are the parameters within which the business can develop growth strategies. According to Ehlers and Lazenby

(2004) and Lazenby (2013) growth strategies are grouped into two: internal and external growth strategies. On the one hand, an internal growth strategy is a plan within which the business grows with the utilisation of internal resources. An external growth strategy is a plan within which the business grows through the exploitation of external resources.

Internal growth strategies

A business that plans to follow internal growth strategies has four options through which to expand: market development; product development; market penetration; and innovation (Fombrun & Wally 1989; Deed *et al.*, 2000).

Market penetration which is also referred to as a concentrated growth strategy is aimed at increasing the market share within the existing market segment and with the existing product. The effectiveness of the strategy depends on the following factors:

- The market for the product is not saturated;
- There is room to increase the product usage rate of the customers;
- The decline in total sales of the competitors;
- There is stability with regard to product availability, prices, quality or resources to produce the product; and
- The economics of scale overrides the cost.

Market development refers to the introduction of a business product or service in a new market. In order for this strategy to be effective, the business must have affordable and reliable distribution channels to the new market. The business must also be aware of the cultural barriers and buying behaviour of the new market entrants.

Product development is defined as a way of modifying and improving the business's product. This strategy is applicable to a successful product that is approaching maturity. The conditions for the success of this strategy include the following:

- The industry is faced with technological advancements and healthy competition that helps the business to offer better quality; and
- When the business has capital available for investment in research and development, advanced technology and the recruitment of competent human resource.

Businesses can grow through product development by adding new product-line extensions or new offerings (Lamb, 2007).

Innovation denotes technological competencies and capital reserves to the advantage of the business. Business that is growth-oriented keep innovating from time to time. For the strategy to be successful the following conditions must exist.

- Customers demand differentiation;
- The industry is faced with rapid changes and advanced technology;
- The business possesses research and development skills; and
- Is adaptable to innovative ideas.

External growth strategies

Strategies that are classified under external growth strategies are diversification and integration:

Diversification is a growth strategy that is aimed at providing the business with the opportunity to venture into a new line of business which is different from the existing offering. It has two approaches to growth strategy: related and unrelated diversification:

- **Related or concentric diversification** refers to the addition of a new related product to the business line of operation. The strategy is effective if:
  - The industry is going through a slow growth or no growth phase;
  - The current products are in the decline stage of the product life cycle;
  - There is a potential for economies of scale across all business units that can share the same strategic assets such as the distribution system; and
  - The potential exists to create a new strategic asset at a lower cost.
- **Unrelated or conglomerate diversification** is defined as adding a new unrelated product in order to penetrate the new market. This strategy succeeds if:
  - The industry is experiencing a sales or profit decline;
  - The existing market for the existing products is saturated; and
  - The business has the capacity to compete successfully in a new industry.

Integration is a growth strategy that involves both vertical and horizontal integration strategies.

- **Vertical integration** is a growth strategy which operates in two possible directions. The business can decide to enter the market as a supplier or take control of suppliers. This is the approach which is referred to as **backward vertical integration**. Alternatively, the business can opt to enter the market as a customer or overtake distributors, a strategic approach referred to as a **forward vertical integration**.
- **Horizontal integration** is a growth strategy through which the business acquires control of the supply chain through mergers, acquisitions and takeovers. This strategy becomes effective if the business operates in a growing industry and economies of scale can profit cost benefit or any form of competitive advantage. However, the challenge for this strategy is adapting to the differences in the culture, skills levels, management styles and values of merging businesses.

3.2.5.6 Finance, growth strategy and business life cycle

According to the Schumpeterian Philosophy (1954), small businesses are vulnerable to failure if they are not innovative enough to outclass the competition. Failure is usually the end result, particularly if older and newer small businesses are exposed to competition from new innovative small businesses. Existing literature documents an extensive analysis of the relationship between finance and growth. Previous research shows that small businesses are confronted with different sources of finance at different stages of growth, (Robin & Robinson, 2014; Berger & Udell, 1998). While start-up businesses depend mostly on own savings, or loans from family, friends and trade partners for funding, businesses at the growth stage depend mostly on financial intermediaries/ financial institutions. This stage is characterised by high failure rates due to a number of reasons, including but not limited to:

- Lack of business and management skills;
- Poor planning;
- Limited or no understanding of the industry.

Research indicates that businesses fail to survive the growth stage and beyond on account of lack of access to finance (CPLO, 2014; Mago & Toro, 2013)). Finance is an important resource to help the business take advantage of the opportunities available for growth, (Badulescu, 2011).

The financial needs of the business vary throughout the different phases of the business life cycle and require varying financing options. Berger and Udell (1998) propose a financial growth cycle model that indicates that at each stage of the business life cycle, the business is exposed with a different set of financial needs, and therefore needs a different financial strategic option. Unfortunately for the start-up stage, businesses are exposed to a limited source of finance, in most cases internal funding sources. High failure rates, information opacity, and lack of a trading record are some of the characteristics of the start-up stage of the business that limit access to finance (Berger & Udell, 1998; Cassar, 2004; Huyghebaert & Van de Gucht, 2007).

The table on the next page shows the different stages of business growth, along with specific strategic focus and investment requirements.

Table 3.2: Stages of business growth, strategic focus and investment requirements

Stage	Strategic Focus	Investment needs	Revenue trends	Profit trends
Start up	- Market entry - Revenue growth	- Launch start-up costs - Investment in working capital	- High growth	- Expect losses
Early success	- Customer acquisition - Customer retention	- Working capital	- High growth	- Profits emerge
Sustained success	- Customer retention - Business diversification - Return to shareholders	- Reduced business should be generating free cash flow	- Steady	- Strong
Maturity	- Ensuring customers expand beyond existing loyalty base - Exit strategy	- Business renewal areas - Acquisitions	- Stable	- Stable / decline
Decline	- Exit - Reversal of fortunes - Possibly rejuvenation - Succession	- Capital erosion - Capital needed for rejuvenation	- Decline	- Decline

The first three stages of the business cycle are part of the growth stage. The growth stage is a stage where the availability of enough capital is crucial for the business to manage growth; otherwise the high incidence of competition can affect the business's survival opportunities.

The Commission for European Communities (CEC) (2006) suggests that financing is necessary during the first two stages of the business life cycle: start-up (innovation) and growth stages. The commission does acknowledge that it is risky for banks to finance small businesses due to high transaction costs and the low rates of return at the early stages. However, it is unfortunately where risky financing is needed the most.

3.2.5.7 Business life cycle, growth and planning

Some researchers argue that a business that has no proper planning is as good as failed even before the business starts (Costa, 1994; Shonesy & Gulbro, 1998). In particular, Shonesy (1998) posits that not only "appropriate management", but also financial planning are predictable success measures. Business planning at every stage of the business life cycle plays an important role in the success and survival of the business. At each individual stage the business is confronted with a different set of challenges. According to Thompson (2003), a business plan is a roadmap of what the business does and how it (the business) has developed and how it (the business) intends to progress. The plan must also provide the strategy for the existing sales, as well as the processes to achieve the desired growth.

Researchers like Williams (1992), point out that business plans are crucial for business success, the business plans need not always be written down, as entrepreneurs are inclined to operate on mental planning for each stage of the business cycle. Citing successful entrepreneurs reported in reputable business magazines, the researcher indicates that some entrepreneurs admitted that no formal business plans were prepared with the founding of the businesses. The entrepreneurs, nonetheless, agree that the constant updating of goals; responding to change, as well as the budgeting part of the plan had always been constantly done and allowed for the success of the business. However, other successful entrepreneurs acquiesced that along with a clearly defined mission and objectives, an articulate business plan led to their business success.

Business planning ensures that the key targets are met and priorities are timely managed. The planning of the business must cover timeframes of the next twelve to thirty-six months and needs to at least highlight the following key items:

- the summary of the business;
- the marketing plan;
- operation information; and
- financial information.

Churchill and Lewis (1983) assert that businesses are faced with different needs in the various stages of business, and therefore each stage needs a different approach to planning. Each stage of the business is characterised by a different set of problems from other stages:

<u>Stage 1</u>: Start-up phase (existence)

In the first stage known as the start-up phase, the business is confronted with the need to acquire customers and to deliver the products or services. The entrepreneur is responsible for all the important tasks in the business, and therefore has to decide on three key questions:

(i) Can the business find/attract enough customers to deliver the product or service to so that there are enough satisfied customers to make the business viable?
(ii) Can the business expand from one key customer or pilot production process to a much broader sales base?
(iii) Does the business have enough cash to cover all the demands?

Due to the simplicity of the business organisation, the main planning must be to ensure that the business remains alive in order to graduate into the next stage, early success or survival. If the business fails to address the stated questions, the business is deemed to fail and will cease to exist.

<u>Stage 2</u>: Early success (survival)

Reaching the second stage is proof enough that the business has been established and has enough products or services to satisfy the customers that have been acquired. At this stage, the business is confronted with the challenge of matching revenues and expenses. To successfully address this challenge, the business must satisfy the following:

(i) It must generate enough cash to break even and to cover the repair or replacement of capital assets as they become worn out;
(ii) It must generate enough cash flow to remain in business and to finance sufficient growth so that the business is able to earn an economic return on assets and labour.

Since the business is still in the simplicity state with the entrepreneur still responsible for all the business tasks, there is minimal systems development and formal planning is on cash forecasting. The business that succeeds in addressing the stated challenge may grow in size and profitability and ultimately migrate to the third stage, sustained success.

<u>Stage 3</u>*: *Success (sustainability)

In the third stage of business growth, the entrepreneur has to decide whether to keep the business stable and profitable while providing a base for alternative activities, or to exploit the business's accomplishments and expand. These are the two sub-stages of stage three:

(i) A decision to keep the business stable, or
(ii) To revive the business and to establish a new grow path through the introduction of new products or by entering a new market (Churchill & Lewis, 1983).

3.2.5.8 Types of finance applicable to stages of the business cycle

Businesses have different financial needs at different levels of the business life cycle. Caselli (2009) identifies the first two stages of the business life cycle as the growth stages, namely,

(i) Stage 1: the start-up or early stage identified as the early growth stage, and
(ii) Stage 2: the early success or expansion stage as the rapid growth stage.

While all other stages of the business life cycle will need financing, in the first two stages financing is crucial to boost growth. The financing options available for the first two stages of the business life cycle (growth stages) are discussed in the following section. The other stages, the maturity and decline stages are excluded from this discussion as they are not growth stages and therefore not applicable to the development stages of small businesses.

<u>Stage 1</u>*: *Start-up finance

During the early stage of the business, financing is needed to start up the new venture which is moving from being an idea to coming into operation. This may include financing for equipment, inventory; and buildings. During this stage the business is considered very risky as the future development of the business is uncertain. Caselli (2009) suggests that the riskiness of the business can be managed through the provision of a strong support and understanding of business planning.

Research shows that at the start-up phase of the business, entrepreneurs use their own savings and loans from family and friends (ILO, 2016). Financing at the start-up stage range from microcredit to private equity, dependent on the industry the business venture is in. Unlike corporate financing which focuses mainly on debt for the whole company, entrepreneurial finance (small business finance) focuses on equity for the potential growth with a time horizon of up to five to seven years. On exit, the investors of private equity may utilise options such as initial public offering (IPO), buy back, trade credit or even a write off (Caselli, 2009).

(a) Microcredit

Microcredit financing includes various types of small loans offered to people mainly for the operation of a small business. It is perceived as a steering tool in the business development support for emerging entrepreneurs. Looking at it from the suppliers' side, it is also considered as banking at the doorstep for poor borrowers. Researchers such as Ahmed, (2005) and Dsani and Guo, (2003) agree that microfinance is an organised economic development strategy that offers several financial services aimed at assisting low income people to establish and grow their small and medium businesses.

According to World Review (2000), microcredit and rural finance programmes have been in existence since the early 1970s, for example, the Grameen Bank was founded in 1976 in Bangladesh and makes small loans to the impoverished without requiring collateral. Since then various microcredit activities and programmes have been established and developed. Two decades later, in the 1990s, developing countries were able to access microcredit. In Argentina, a credit programme aimed at small businesses was, for instance, implemented in 1993 (Paravisini, 2008).

(b) Bridging finance

Bridging finance refers to short-term loans that are designed to finance the working capital required for the daily running of the business. According to CPLO (2014), businesses need immediate cash flow to meet their current obligations.

Table 3.3 below portrays the stages of the business life cycle along with the financial or investment requirement for each stage.

Table 3.3: Financial or investment requirement for each stage of business life cycle

	Investment	Profitability	Cash flow	Sales growth
Development	Focused on the acquisition of productive factors	Negative	Negative	Not available
Start-up	Focused on the acquisition of productive factors	Strongly negative	Strongly negative	Starting
Early growth	Limited to inventory financing	Negative but reducing	Negative but reducing	Positive and increasing
Rapid growth	Limited to the inventory	Positive and increasing	Positive and increasing	Positive but decreasing
Mature age	Focused on the inventory or on the replacement	End of increasing	End of increasing	Getting to zero
Crisis or decline	Not possible to be identified	Falling down	Falling down	Negative

(c) Leasing or cessions

According to Naim (2008), commercial banks in partnership with development finance institutions have considered broadening their client base to serve small businesses, the market they have ignored for a long time. The services that banks are offering to small businesses mostly have to do with development skills such as banking skills; information systems; product standardisation; innovative marketing, low-cost delivery channels and quantitative risk-management. Nonetheless, Naim (2008) maintains that only medium businesses have the advantage over smaller businesses. Medium businesses have the benefit of access to term finance while smaller businesses only acquire fully-secured short term finance. Therefore, term finance can help medium businesses to invest in equipment (assets), and which will ultimately enhance their growth potential.

***Stage 2 – Growth stage*: Expansion finance**

Expansion finance is a form of capital that is meant to stimulate the growth of the business. The business that plans to expand through hiring additional stuff, to purchase additional equipment, or for any other costs that are associated with the expansion of the business, require flexible term finance to achieve this objective (BusinessFinanceNews, 2007). Financing required during the expansion phase of the businesses is driven by the need for investment, profitability, cash flow and sales growth variables. These four variables are therefore determinants and drivers for business growth. The four drivers are helpful in determining the financial needs across all the stages of the business life cycle.

3.2.5.9 Business development and environment

Shah *et al.*, (2013) argue that business development depends heavily on the careful selection of growth strategies that are appropriate for the competitive environment in which the business operates. The theory of a business-enabling environment is embedded in a neo-classic framework which assumes that businesses perform well where property rights and competition are protected. The theory advocates for minimal regulatory government intervention, along with a limited role for supporting economic participants. The proponents of the theory argue that potential growth exists for all small businesses, including informal enterprises, is unfair regulations are eliminated (Federal Ministry of ECD, 2008). Entry regulations have adverse consequences, not only on start-up businesses, but also erect barriers against entrepreneurship in established small businesses.

Some scholars believe that small business cannot afford to survive in the business world where they are competing with large established businesses (Grossruck & Kusel, 2008) which have already occupied the market (market saturation). Small business, however, can survive the challenge of market saturation through innovation. The proponents of this ideology suggest that, to survive, small businesses need the support of all the stakeholders within the economy. Nieman and Nieuwenhuizen (2009), for example, propose that different institutions within the economy need to play a role towards the support and development of small businesses.

Closely related to the resource-based view, the business environment assumes that business development relies on the environment in which the business operates (Penrose, 1959; Miller & Shamsie, 1996). In a situation where the environment is more enabling, there are higher chances for the business to succeed. An understanding of the business environment helps to reduce the barriers which can otherwise hinder the growth of small businesses. As some researchers agree, the business that is faced with the possibility of a decline (Pearce & Robinson, 1997), can through discretionary management, respond to internal and external threats and recover (Lawrence & Jones, 2001) and ultimately survive (Setton, 1999; Fortune & April, 1999). According to Indris and Primiana (2015), there is a significant relationship between the external and internal analysis of the performance of small businesses. An environmental analysis entails assessing the level of threat or opportunity factors that might be present in the business. Babatunde and Adebisi (2012) state that the business exists in a very competitive environment and for any business to survive, an environmental analysis is necessary.

Hamilton-Coplin (2002) advises entrepreneurs to constantly perform environmental scanning as a necessary and important aspect of achieving effective business growth plans. Constant environmental scanning helps the managers obtain a clear vision in order to proactively and innovatively plan for the successful performance of the business. Most importantly, this scholar further points out that the experience of the entrepreneur is key to identifying the opportunities (and threats) presented by the environment. These are the opportunities, which if intellectually identified, lead to the success of the business.

3.3 CONCLUSION

This chapter presented various theories that relate to business growth. Different growth strategies were discussed, along with the different forms of financing that are deemed applicable for each stage of the business life cycle. The theory resource-based view was found not applicable to this study given that the small businesses in their start-up and early growth stages possess no financial resources (the main core of this study) which can be exploited for competitive advantage. The theory of business life cycle alone was found to be inadequate as the theory ignores the chaoticness and unpredictability of start-up businesses and hence, this element of Complexity and structuralist theories were then incorporated into the BCL theory, providing a framework believed to be suitable for small business on the lookout for development finance as a growth instrument. Therefore, a new integrated BCL theory was discussed in more detail as this is the theory upon which this study is based. Close attention was given to business development theory that shows that during the first two stages of the business life cycle, small businesses are prone to failure due to a lack of access to finance, and hence, development financing is the possible solution for to ensure small business success.

The next chapter is focused on small businesses in South Africa, and includes an account of DFIs in South Africa as attempts to support small businesses through development finance.

CHAPTER 4: SMALL BUSINESSES AND DFIs IN SOUTH AFRICA

4.1 INTRODUCTION

The number of establishments in the South African small business sector has increased over the last two decades. The difficult economic times of the twenty-first century are seen as one of the driving forces behind the increased unemployment rates, and hence, the increased numbers of small businesses being established. As a developing country, South Africa is faced with the developmental challenges of inequality, unemployment, poverty, as well as low economic growth; all factors in which small businesses are expected to play a meaningful (Patel, 2011).

This chapter discusses the landscape of small businesses and DFIs in South Africa. The aim of the chapter is to firstly provide a holistic picture of small businesses in South Africa. Secondly, the chapter aims to observe the role played by the government of SA in providing developmental finance through the DFIs. Their distinctive operations are highlighted in order to understand their role in small business development and also to observe which gaps they aim to fill.

4.2 THE LANDSCAPE OF SMALL BUSINESSES IN SOUTH AFRICA

Small businesses in South Africa seem to be established as a response to the challenges of unemployment rather than for the purposes of competitiveness and growth. As stated in Chapter 1, South Africa has experienced an increase in the number of small business being established in the twenty-first century. Given the high rate of unemployment in South Africa (26%) (StatsSA, 2014), it has been deemed important to nurture the growth and development of the sector. However, a number of challenges hamper the growth of this crucial sector in South Africa. Some of the realities of the small business sector in South Africa will be discussed in this and the next section. These include among other things, the importance and success stories towards development of the sector.

There are about 2 251 821 small businesses in South Africa. Of these, only 667 433 are formal businesses and the rest operate as informal businesses (SEDA, 2014). Given the definition that small businesses include organisation that employ up to 200 people, it means that in South Africa about 45% of all employed people work in small businesses employing less than ten people, while over half of the private sector businesses employ fewer or no staff (SBP, 2009). This indicates that the majority of businesses in the country fall within the category of micro enterprises; the category which includes start-up businesses and businesses in the early stages of growth. As mentioned in Chapter 1, the minister of small business development highlighted that businesses in this category are unlikely to survive up to ten years, which implies that micro businesses need the most fostering, in efforts to address the problem of unemployment.

4.2.1 Entrepreneurship in South Africa

Although small businesses make up about 96% of all businesses in South Africa, reports show that entrepreneurial activity in the country is significantly low. When compared to other participating countries (65), the Global Entrepreneurship Monitor (GEM) 2016 reports that South Africa is ranked at 52 with a Total Early-stage Activity (TEA) of 6.9%. The South African ranking is even lower than the average (18%) of all efficiency-driven economies and also lower than the average (18.8%) of all middle-to-low income economies. The report further shows that when it is compared to its per capita ratings, SA would be expected to have a TEA of 20% (Herrington, et al., 2017). The 2013 GEM report shows that the challenges of small businesses have remained the same since 1996 although there has been a slight improvement in recent years (Herrington & Kew, 2013)

The government considers SMME development as a key aspect of the economic development, poverty alleviation and job creation strategy. According to StatsSA, (2016) although economic growth has increased in recent years, it increasing at a low rate (0.6%) and it remains insufficient to reduce unemployment which has been standing at 27% in the last quarter of 2016. Entrepreneurship is even more crucial to help address the socio-economic issues facing the country. Although the country has achieved elements of macro-economic stability and an increasingly open market, there are still concerns about South Africa's competitiveness. Low entrepreneurial activity and a shortage of skills are serious concerns hampering competitiveness in South Africa.

4.2.2 Characteristics of the small business sector in SA

According to StatsSA (2015), there are about 2 251 821 small businesses in SA. Only about 34% (667 433) of small business are formal businesses while the rest of the 66% (1 497 860) are informal businesses. The Gauteng province has the highest number (almost 22%) of small businesses in the country, followed by KwaZulu-Natal with about 17%. The Northern Cape Province has the lowest percentage of small businesses in the country, representing only 0.9% of all SMMEs as shown in Table 4.1 below.

Table 4.1: SMMEs across SA provinces

Province	Formal	Informal	Other	Total
Eastern Cape	50 670	141 739	4 957	**197 366**
Free State	26 224	60 816	9 806	**96 846**
Gauteng	306 231	465 100	13 989	**785 321**
KwaZulu-Natal	74 976	283 165	15 293	**373 434**
Limpopo	28 054	207 512	14 098	**249 663**
Mpumalanga	35 208	141 129	9 063	**185 399**
Northern Cape	8 534	9 058	3 019	**20 611**
North West	27 430	79 153	6 273	**112 856**
Western Cape	110 107	110 188	10 030	**230 324**
Total	**667 433**	**1 497 860**	**86 528**	**2 251 821**

Source: StatsSA, 2015

Table 4.1 shows that the number of formal businesses is almost proportionally equal to the number of informal businesses in the Western Cape. Gauteng has the highest number of formal business 306 231 (46%) and 465 100 (31%) of the informal businesses. Gauteng is followed by the Western Cape with 110 107 (16%) of the formal businesses, while KwaZulu-Natal follows the former in terms of the informal SMMEs (283 165 or 19%). The Northern Cape has the lowest share of SMMEs (20 611or 0.9%) in the country, followed by the Free State (96 846 or 4.3%) and North West (112 856 or 5%) respectively.

GEM 2016 states that the TEA index in SA stands at 6.9%, recorded at 13% below the average of 18.8%, positioning the country at 52 out of 65 participating countries (Herrington, et al., 2017). Although this figure is within the same range as other developing countries such as Korea (6.7%), the United Arab Emirates (5.7) and Qatar (5.7%), the country trails significantly behind its BRICS partners, Brazil, India and China with 19.6%; 10.6% and 10.3%, respectively. Worth mentioning, however, is that only about 2.5% of small businesses owned by the adult population in South Africa are established (have survived beyond three years), which places SA at 61 out of 65 participating countries. This is a low ranking for SA compared to other countries that are categorised in the same emerging market class, such as Brazil, China, Argentina and Columbia, all with established businesses at more than 6.5%, with the exception of China, similarly with 2.5% (Herrington *et al.*, 2017).

4.2.3 Profile of SMMEs in SA

According to SEDA (2016) the majority of small businesses in South Africa are informal micro businesses, the category which is characterised by survivalist self-employed people (Berry *et al.,* 2002). Small businesses ownership in South Africa is believed to be skewed more towards women, Black Africans, and young people. Some reports (DTI, 2008; GEM, 2014, Herrington *et al.*, 2017) cite a number of factors behind the small business sector being skewed toward this group of people (usually referred to as the designated or previously marginalised group) compared to other population groups., It is therefore, not strange that Black Africans make about three-quarters of entrepreneurial population, while the majority (62%) of entrepreneurs in SA operate in the retail trade, hotels and restaurant industry (Herrington & Kew, 2013, Herrington, et al., 2017).

SEDA (2016) shows that the small business sector in SA is classified mostly in terms of legal categories (formal and informal) as the categorisation bear a significant picture in the sector. The demographics mostly used in sector profiling are in terms of ownership, and the educational status of the owners. StatsSA (2015) shows that about 34% of the formal SMMEs are owned by black people. The formal businesses tend to be operated by educated, white people, with the majority being situated in the Gauteng and Western Cape provinces. With the exception of the Western Cape, all the provinces have more informal than formal SMMEs (Table 4.1). The report further indicates that most of these informal businesses are operated in the rural areas by less educated people.

Interestingly, Herrington *et al.* (2017) highlights that the male/female TEA ratio in SA is1: 0.74 which means that fewer women than men are involved in small businesses, which places the country at a ranking of 22 out of 65 countries. Even more interesting is the female/male opportunity driven rate which is at 0.94, indicating that an almost equal number of women to men take up a business opportunity in SA.

Table 4.2: Distribution of SMMEs per Industry

Industry	Formal	Informal	Other	Total
Agriculture	0	0	56 774	56 774
Mining	0	2 199	0	2 199
Manufacturing	62 657	138 801	0	201 459
Electricity, gas & water	6 656	801	0	7 456
Construction	77 098	222 143	0	299 242
Trade & Accommodation	186 798	757 669	0	944 467
Transport & Communication	56 620	76 514	0	133 134
Finance & Business services	172 423	99 289	0	271 712
Personal & community	105 181	200 444	0	305 624
Other	29 754	0	0	29 754
Total SMMEs	**667 433**	**1 497 860**	**86 528**	**2 252 821**

Source: StatsSA, 2015

Most informal businesses (51%) operate in the Trade and Accommodation industry while there are no businesses (0%) in the Agriculture sector. The Manufacturing, Personal and community industries, as well as the construction industry make up about 40% of the informal businesses. There are very few informal businesses in the mining and electricity, gas and water industries.

4.2.4 Capabilities and survival trends of SA small businesses

According to the Minister of Small Business Development, Lindiwe Zulu (2014), small businesses in SA have about 37% chance of surviving for at least four years. Most small businesses in SA (between 70% and 80%) fail within the first year of operation, while only about 10% to 15% of those that survive make it to five years. The most worrying issue is that most of these businesses that fail to survive to the next stage of the business cycle are owned by black females. About 80% of the SA population of 54 million is made up of black people of whom females make up about 51% (StatsSA, 2014). Both black people and females are part of the group that is believed to have been marginalised during the apartheid era, and which has left the country with the legacy of having to deal with the challenges of poverty, unemployment and inequality.

GEM, 2012 reported that more men than women in SA (45% versus 35%) have entrepreneurial capabilities; moreover, in spite of having more opportunities than other races, black people have the lowest capabilities (39%), (Turton & Herrington, 2012). Interestingly, although access to finance has always been at the top of the list of reasons cited for poor business performance, GEM, 2017 reports that profitability and personal reasons hold the top spots and finance is placed third (Herrington *et al.*, 2017).

Limited entrepreneurship capacity and a shortage of skills are two of the factors contributing to unemployment in the country. About 45% of SA entrepreneurs have a low technological orientation, although about 55% of early-stage entrepreneurs in SA use the latest or new technology, an improvement compared to the African region average of 45%, Herrington *et al*., (2017). The National Development Plan (NDP) recognises that small businesses, especially in the services sector, have a shortage of business and management skills (EDD, 2012). GEM 2016 reports that reasons linked to the entrepreneurs themselves are the second main reason after a lack of profitability for business continuity. According to the report, although unemployment is at the rise in SA, TEA is declining (at 6.9% in 2016 from 9.3% in 2010). To match the high levels on unemployment, Herrington *et al.* (2017) suggest that TEA in SA should be at least 20%.

4.2.5 Small businesses towards employment, poverty and inequality

The NDP entrusts small businesses to create about 11 million jobs towards unemployment alleviation by 2030. Small businesses in South Africa make up about 96% of all businesses. While the formal small businesses sector absorbs about 60% of the labour force in South Africa (FFI, 2017), the informal economy only absorbs about 15% thereof (DTI, 2008). In comparison with other developing countries (Schneider, 2011), the labour absorption of the informal sector in South Africa is the lowest.

Research shows that some people resort to establishing small businesses as a means to make ends meet and to end the prevalence of poverty. Many people see their own small business, in the absence of gainful employment, as a possible answer to meet their basic needs, which ultimately ensures people live beyond the poverty line. The poverty line in South Africa, as used by the government, stands at R1 077.00, and is reported to have risen by more than the inflation rate. The food poverty line (PFL) rose by 12.9% between 2016 and 2017, while the inflation rate is standing at 6.4% for the same period (StatsSA, 2016).

According to Ratshinga (2016) inequality is one of South Africa's main development challenges. With a Gini Coefficient of between 0.66 and 0.70, the country is considered by the World Bank as the dual economy with one of the highest inequality rates in the world. The reduction of inequality levels from 0.7 to 0.6 and the elimination of poverty, are some of the main strategic goals of the NDP for the year 2030, through among other things, the utilisation of small businesses.

4.2.6 Small businesses and economic growth

SMMEs in South Africa contribute about 42% of the GDP (StatsSA, 2015). Informal small businesses account for only 8.8% of the GNP. The low figure may be an indication that most of the businesses are formal due to enabling environments. In contrast, Burkina Faso's informal businesses measure 38.4% on the GNP (www.worldbank.org). The NDP aggressively promotes an economic growth strategy, and small businesses have been entrusted to meaningfully contribute towards job creation. The strategy that is aimed not only to reduce unemployment to 6% by 2030, but to create 11 million additional employment opportunities would ultimately require that the GDP grows at the rate of 5.4% per annum.

The NDP envisages that 90% of new jobs will be created by small businesses and expanding businesses. That strategy implicitly indicates how much small businesses are valued for economic growth in the country. The NDP emphasises that for the strategy to be achieved, not only greater access to finance and equity finance, but simpler regulations and better skills training are required.

4.2.7 Challenges for small businesses in South Africa

GEM (2014) cites access to finance and poor profitability as among the main reasons for the low survival rates for small businesses. Other than the challenges of access to finance and the legal environment, the GEM SA (2006) report shows that small businesses in South Africa are also faced with the challenges of gender, business skills and financial illiteracy. From the study conducted by a private sector research and development company, Small Business Partners (SBP) in 2014, about 71% of the 500 respondents were concerned that it was difficult to operate a business in SA, citing problems such as lack of skilled labour, burdensome regulations, economic conditions, lack of finance and cost of labour as barriers to success. These issues will be discussed in the section below.

4.2.7.1 Regulatory and enabling environment facing small businesses

According to the World Bank (2014), SA is ranked in 41st position of 189 countries in terms of an enabling environment for doing business. The country is also ranked in the 64th position in terms of the ease of starting a business. Government bureaucracy is identified as one of factors that pose a challenge to entrepreneurial and business activity in SA. For example, there are long delays in the time required to obtain permits and licences (GEM, 2014)

The challenge of a dis-enabling environment has a great effect on entrepreneurs, particularly at the start-up stages, and should be addressed if small businesses are to play a meaningful role in the mainstream economy. According to Sharp in Payne (2012), the high taxes force start-ups in South Africa to operate illegally. This implies that start-up businesses prefer to remain informal in order to avoid paying high taxes. Reports show that small businesses mostly (about 93%) operate as informal businesses. As such, most businesses in this category hardly survive to contribute significantly to the economic development of the country.

4.2.7.2 Access to finance and small businesses

Access to finance and credit in South Africa is ranked among the top three problems that hinder the growth of small businesses in the country (SEDA, 2016; Herrington *et al.*, 2017). The challenges posed by the availability of finances, as reviewed over a number of years from 2001, has been one of the most cited among the key challenges facing small businesses (Herrington, 2011). Small businesses in South Africa are no different from their counterpart SMMEs in other developing countries when it comes to lack of access to finance. Similar challenges that affect the rest of the world also face small businesses; however, given the legacy of apartheid in the country, the challenges are much worse for the previously marginalised communities than is the case for the previously economically included population (DSBD, 2010).

Given the strategy for the development of small business, in order to effect the proposed employment creation (11 million jobs) by 2030; the National Planning Commission for the NDP advocates for increased and strengthened financial services. It is foreseen that lower costs and improved access to financial services, along with better coordination of the relevant agencies (DFIs), and private investment through partnerships can help to achieve the objectives. GEM, 2014 reports that in SA, banks remain the main sources of business finance, however, small businesses can also seek finance from venture capitalists, business angels (i.e. private investors), informal investors, as well from the DFIs (Herrington *et al.*, 2014).

4.2.7.3 Access to information and markets

Small businesses in South Africa are faced with many challenges caused by access to information and competitive markets. The DSBD (2010) states that due to the limited access to competitive markets and information, small business owners do not possess the requisite managerial skills and their products do not meet the required quality standards, and therefore they cannot operate enterprises that grow.

4.3 GOVERNMENT INTERVENTION IN SUPPORT OF SMALL BUSINESSES

The World Bank has for quite some time (from as far back as the traceable 1980s, but the past two decades is used to dignify the argument here) been of the view that the public sector needs to play a significant role in ensuring that small businesses are supported in terms of the regulatory environment, access to finance and businesses development services. Fan (1993) highlights the following as public sector responsibilities.

- In providing support with regards to the regulatory environment, the public sector needs to:
    - Address market failures to open opportunities;

    - Improve transaction efficiency and reduce risk; and
    - Reduce fixed costs.
- Regarding the support for access to finance, the public sector needs to:
    - Increase competitive pressure in financial markets;
    - Reduce transaction costs; and
    - Strengthen financial institutions' capacity to serve small clients.
- In order to provide support for business development services, the public sector must:
    - Provide market support structures to help small business competitiveness;
    - Foster markets for services fit for and demanded by small businesses; and
    - Develop low-cost service product and delivery mechanisms needed by small businesses.

In addition to Fan's (1993) recommendations, Tewari, Skilling, Kumar and Wu (2013) further state that the much needed support for small businesses lies in the growth and sustainability of innovative enterprises. The early-stage failure rates and lack of competitiveness within the small business sector are cited as the reasons for the proposal to improve the small business development policy per the Word Bank agenda of dealing with the problem of unemployment.

The South African government appreciates the potential of small business to assist in addressing the development dilemmas of poverty; inequality; as well as unemployment, and most importantly, takes cognisance of the sector's contribution towards economic growth. The Minister of Small Business Development, Ms L Zulu, in 2014 stated that one of the main reasons the government was paying attention to the development of small businesses, was the confidence placed in the sector to defeat the challenges of poverty, unemployment as well as inequality, and ultimately underdevelopment. The government therefore intervenes to grow and help reduce the high failure rates faced by small businesses.

The White Paper policy on small business development was developed in 1995 to create an enabling environment in support of small businesses in alleviating poverty. Unemployment, inequality and poverty reduction are some of the key development challenges for the country post-1994. The paper gave rise to The National Small

Business Act, No.102 of 1996. The Act was meant to support small, micro, medium enterprises in the areas of access to finance, access to the market and access to information. The increasing challenge of unemployment is attributed, among other things, to a shortage of skills, and also limited entrepreneurial capacity among the SA population at large. In response to the challenge, the government identifies small businesses as a key aspect for economic development, job creation and poverty alleviation. As the DTI (2008) asserts, the SMME development policy of 1995 was extended to the ten-year (2005-2014) strategy. The 2005-2014 Integrated Small Business Development Strategy was based on:

- The increase in supply of financial and non-financial support;
- Creation of demand for SMME products and services; and
- Reduction of regulatory constraints.

The DTI was entrusted to carry out this mandate through its Enterprise Development Unit (EDU) (DTI, 2005 White Paper, 1995).The EDU coordinated various strategies to develop the small business sector. One of these strategies was the coordination of access to finance. Implementing this strategy influenced the establishment of new, and the development of various existing development institutions which are referred to as development finance institutions (DFIs), namely, the National Empowerment Fund (NEF), Land Bank, National Youth Development Fund, Provincial Development Corporations, Industrial Development Corporation (IDC), South African Micro Apex Fund (SAMAF) and Khula Enterprise Limited (Khula). In April 2012, Khula and SAMAF were merged with IDC to become the Small Enterprise Finance Agency (SEFA) (www.thedti.gov.za)

The strategy, which was made a policy document in 1995, has been reviewed annually since 1994. According to the DTI, the SA government realised its responsibility to create an environment conducive to the formation and growth of small business enterprises. The White Paper on small businesses strategy on the development of small businesses was to include, but not limited to, an enabling legal environment, reorganising regulatory conditions, accelerating access to: information, market, affordable infrastructure, enterprise skills and management and finance. In July 2009, the new ministry, Economic Development Department (EDD) was established within the headquarters of the DTI. Six agencies that were initially under the DTI were transferred to the new ministry: the three development finance institutions (DFIs): IDC, Khula Enterprise Ltd and the South African microfinance Apex Fund (SAMAF), along with the three regulatory bodies: the Competition Commission, Competition Tribunal and International Trade Administration Commission. These institutions were established to achieve the following key objectives:

- To facilitate development financing at concessionary rates for entrepreneurs and small businesses;
- To reduce anti-competitive practices in the economy and prosecute offenders in key sectors; and
- To ensure a sound trade administration regime.

The purpose of these objectives was mainly to combat the three social challenges of unemployment, poverty and inequality, (EDD, 2012). The SA government has identified the development of small businesses as a key aspect of the economic development, poverty alleviation and job creation strategy (the DTI, 2008). Likewise, The Accelerated Shared Growth Initiative of South Africa (ASGISA) (2009) stipulates that an average of 5% of economic growth is needed to address the development challenges, such as unemployment and poverty. The expectation is that small businesses which make up about 96% of all businesses, must contribute towards economic growth. As research suggests, innovative entrepreneurs create jobs and contribute to the economic development, therefore they need to be supported through an organised economic development strategy that offers several financial services aimed at assisting innovative entrepreneurs to establish and grow their small businesses (Ahmed, 2005 Dsani & Guo, 2003).

4.3.1 Issues of finance in South African small business development strategies

In 1992, the Minister of Trade and Industry of the Apartheid regime legalised micro finance by signing into law an exemption to the Usury Act that removed the price control on small loans. The act removed interest rate ceilings for loans under R6,000 with a repayment period of less than 36 months. This was followed by tremendous development in the commercial micro-lending in the country, although this lending served more for consumer spending than for the operation of small businesses (Porteous & Hazelhurst, 2004).

The issue of small business finance was further adopted in 1995 when the White Paper on the National Strategy for the Development and Promotion of Small business was introduced (Figure 4.1). The paper stated that black people in the past had made positive progress in the micro and small enterprise segments of the economy. The paper identified the constraints facing the small business sector, and highlighted access to finance as one of the main obstacles which the development strategy must cover (White Paper 1995).

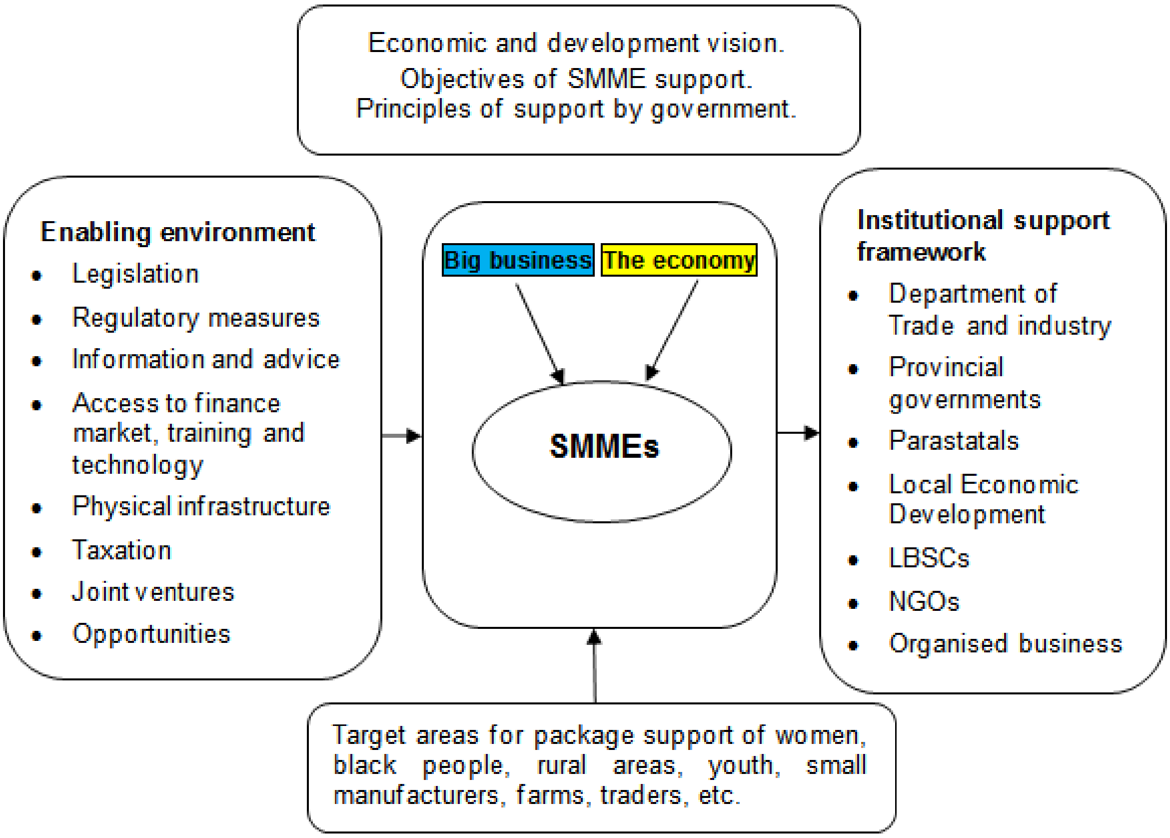


Figure 4.1: The South African national SMME development support strategy

Adapted from (Nieman & Nieuwenhuizen, 2009)

Figure 4.1 presents a support model to create an enabling environment and institutional support for small businesses in South Africa through interventions by various stakeholders which include the economy, big businesses, parastatals and multinationals. The figure implies that if the environment is enabling enough, small businesses have the potential to participate in the mainstream economy like their counterparts, big businesses and other international businesses. The enabling environment helps small businesses to transfer services to other institutions.

The rapid growth of the micro finance industry provided the impetus for a second Exemption to the Usury Act in 1999. Revisions regarding the amount of small loans led to the amount being increased from R6 000 to R10 000. To manage the sector, The Micro Finance Regulatory Council (MFRC) was established. This came along with new regulations for governing the way micro-loans would be administered and how repayments were calculated (National Credit regulator, 2007).

The SA government through its Integrated Small Business Development Strategy for 2005 – 2014 has identified the following three pillars (DTI, 2008):

- Increasing the supply of financial and non-financial support;
- Creating a demand for small business products and services; and
- Reducing regulatory constraints.

The need for increased financial support is one of the priorities towards the development of small businesses. Despite their remarkable importance to the economy, small businesses are marginalised in their access to credit finance by the imperfections of the financial markets. Research shows that due to a number of factors, small businesses are not covered by the commercial lending net. The citations range from lack of collateral, lack of skills, high failure rates and information asymmetry, just to mention a few (Marais *et al.*, 2007; Gem Report, 2006, Mutezo, 2005; Beck *et al.*, 2005). The cited scholars believe that in addressing these challenges, adequate support is required to help the small business sector grow and for countries to reap remarkable results from the sector.

In May 2014, the small business unit of the DTI was converted into an independent department, The Department of Small Business Development (DSBD) which was established by the President. This was a move to strengthen the government's commitment to placing small businesses at the centre of economic growth and job creation. The main development focus of the DSBD includes:

- Black business supplier development programme (BBSDP)
- Co-operative incentive scheme (CIS)
- Shared economic infrastructure facility (SEIF); and
- National informal business upliftment strategy (NIBUS).

The **BBSDP** was developed as a cost-sharing grant that is offered to black-owned small businesses in order to help them improve their competitiveness and sustainability; the support that is meant to help small businesses to participate in the mainstream economy and to create employment. **CIS** is a grant (100%) that is offered to registered co-operatives in order to improve the viability and competitiveness of co-operative businesses through lowering the cost of doing business through an incentive meant for Broad-Based Black Economic Empowerment. **SEIF** was developed in order to leverage public sector investment that provides appropriate infrastructure and creates an enabling environment for businesses to crowd-investment, particularly in townships. **NIBUS** was developed in order to address the development challenge faced by small businesses (www.DSBD.gov.za).

4.3.2 Gauteng SMME development policy (GSDP)

In implementing the national SMME development Strategy, the Gauteng Province has developed a policy that is aimed at developing small businesses in the province for the period 2009-2014. The Gauteng SMME Policy Framework was established to enhance growth and development upon the following fundamentals:

- The Gauteng Employment, Growth and Development Strategy 2009-2014 which sets a coordinated and integrated approach to provincial development informed by the Gauteng Medium Term Strategic Framework;
- The Draft Gauteng Industrial Policy Framework 2009 which focuses on labour-intensive development that seeks to promote localisation and reverse deindustrialisation;
- Gauteng Broad-Based Black Economic Empowerment Strategy which is complemented by the Gauteng Preferential Procurement Policy Framework adopts the national framework and describes specific provisions designed to transform the economy by increasing the number of black people that own and manage their own businesses;
- Gauteng Local Economic Development Policy
- Gauteng Co-operative Development Policy;
- The Draft Gauteng ICT, Employment, Growth and Development Strategy;

- Proposed strategy procurement initiatives in order to promote increased localisation of supply;
- Targeted Gauteng Township Economy Interventions which is complemented by the Priority Township Programme.

The Gauteng Provincial SMME development initiatives are extended to the participation of district metropolitan (such as Tshwane District Metropolitan Municipality) and local municipalities, many of which have introduced growth and development strategies, special plans, local development strategies and integrated development plans that are centred around small business development.

There is a clear indication that the main target for GSDP through its Gauteng Industrial Policy Framework (GIPF) is employment creation of permanent employment opportunities. The GIPF which is aligned to and in formed by the National Industry Policy Framework (NIPF) as well as the Industrial Policy Action Plan 2 (IPAP2), complements the SMME policy and is aimed at the expansion of decent work opportunities; strengthening of inter-sectoral linkages through supply chain development; the development and expansion of medium tech labour-intensive manufacturers. This aim is deemed possible because Gauteng has the largest concentration of manufacturing and services industries in the country. The Gauteng provincial government plans to achieve its agenda of SMME development through collaboration and support of other government agencies to ensure the policy, legal and regulatory framework is consistent and conducive to the growth and development of small businesses.

4.3.3 Development finance institutions in South Africa

This part of the chapter provides an account of individual government DFIs, and the scope of operation of individual DFIs as provided by their respective documents. While provincial DFIs specifically serve communities in their respective provinces, national DFIs serve the country as a whole.

4.3.3.1 National Youth Development Agency (NYDA)

The challenges facing young people, such as unemployment and underemployment are global problems. According to the World Youth Report (WYR) (2005) Western Asia, followed by North Africa and sub-Saharan Africa have the largest number of young people who live below the poverty line. The report notes that over 200 million youth live below one dollar per day, and about 515 million young people live below two dollars per day.

The report further indicates that due to the economic slow-down, the influx of youth into the employment markets has brought with it acute problems in some countries. This report is backed by the International Labour Organisation that states that more than 100 million new jobs will have to be created in the next twenty years. This job creation is to provide suitable employment for the growing numbers of youth, including girls, young women and people living with disabilities in the economically active populations of the developing countries. The United Nations Report (2005) also recommends that, apart from funds designated to promote youth employment, governments should designate resources for programmes supporting the efforts to provide employment for young women and youth with disabilities (UN Report, 2005).

In response to calls such as the above UN report, the SA government launched Umsobomvu Youth Fund (UYF). UYF was established in 2001 to address the needs of the SA youth (18-35 years old) and women who are seeking self-employment opportunities or business ownership. UYF changed its name to the National Youth Development Agency (NYDA) on 16 June 2009. NYDA came about through the combination of two existing youth bodies: Umsobomvu Youth Fund and the Youth Commission of SA.

The then premier of the North West provincial government stated that the province will continue to economically empower young people by providing opportunities for the youth (Ramatlabana, 2009). The premier added that the provincial government will continue to ensure that it supports youth-owned small businesses and it will make sure that youth benefit from government contracts by being represented in their procurement services.

NYDA has various programmes that are aimed at facilitating access to finance for the young people of South Africa. The financing programmes offered by UYF/NYDA are: Enterprise Finance (microloans), Masasizane Women Enterprise Fund and Youth Progressive Fund.

4.3.3.2 Industrial Development Corporation (IDC)

The IDC is a self-financing DFI which was established in 1940 as a state-owned development finance institution. The IDC is primarily aimed at contributing to sustainable economic growth in Africa. The institution also promotes the economic empowerment prosperity of all South Africans. In promoting economic prosperity, the IDC promotes entrepreneurs by the building of competitive industries and enterprises based on sound business principles (www.idc.co.za).

Nieman & Nieuwenhuizen (2009) highlight the following core strategies of the IDC:

- Maintaining financial independence;
- Providing risk capital to a wide range of industrial projects;
- Serving areas not yet addressed by the market;
- Empowering new entrants of the entrepreneurship market and medium-sized manufacturing businesses;
- Developing and investing in diverse human capital; and
- Promoting global involvement in partnerships rooted in and for the benefit of SA and the rest of Africa.

The IDC aligns itself with the goals of the “Shared and Accelerated Growth Initiative of South Africa” (ASGISA). The IDC provides financing that stimulates job creation, investment activities and economic growth and, for example, reports a remarkable job creation of 360 000 new jobs from an investment of R128 billion invested in businesses while saving about 43 000 existing jobs (IDC Report, 2014). This evidence shows that by investing in SMMEs, the IDC is more fruitful. Nonetheless, it may be argued that more jobs are created from investment in SMMEs, because the IDC claims that the small business sector constitutes the majority of the institution’s clients. In 2004, for example, 73% of the IDC’s approved loans were for SMMEs, implying therefore that only 27% of loans were invested elsewhere. Moreover, the IDC considers the SMME sector as a crucial element of a developing country, hence the justification for more investment in the sector.

Furthermore, the IDC (2008), states that because it fully supports government’s Black Economic Empowerment (BEE) in considering funding applications, the assessment for each project covers the project’s ability to meet the following BEE requirements:

- Job creation;
- Urban renewal;
- Rural development;
- The empowerment of women;
- Poverty alleviation;
- Skills development;
- Education; and
- Access to finance for wealth creation.

For its involvement with BEE, the IDC won four awards in 2007 at the Business Map Business Report BEE Awards.

The IDC's main programme as discussed below is a transformation and entrepreneurship scheme which provides various funding schemes.

Transformation and Entrepreneurship Scheme (TES)

The Transformation and entrepreneurship scheme is a financing scheme aimed at entrepreneurs from previously disadvantaged groups in SA, namely, women, people with disabilities, and worker and community groupings. This institution has been established to assist these people with access to finance to develop or grow their businesses. The IDC considers this scheme to be a catalyst for the development of business opportunities by providing capital for the start-up, expansion and acquisition of businesses. It is expected to run for a period of seven years from 2008 onwards (IDC, 2008). The scheme consists of the following five forms of funds:

- Women's entrepreneurial fund to the value of R400 million;
- Equity contribution valued at R150 million;
- People with disability fund of R50 million; and
- Development Fund for workers to the value of R250 million.

The above programmes are meant to address financing gaps affecting the designated group to help them kick-start businesses. Since the element of collateral can be high for the designated groups, the IDC has developed the above programmes tailored to reach out to the target groups.

4.3.3.3 Small Enterprise Finance Agency (SEFA)

The Small Enterprise Finance Agency (SEFA) is a subsidiary of the IDC which is mandated to focus on small business development. SEFA was established in 2012 through the merger of the two agencies: Khula and the South African Micro Apex fund (SAMAF). As a DFI, SEFA is mandated to foster the establishment, survival and growth of small businesses within the nine provinces of SA. In achieving its mandate, SEFA provides direct lending products, institutional support, and wholesale lending products which are channelled through other intermediaries.

4.3.3.4 SEFA loans through Retail Finance Intermediaries (RFIs)

Retail Finance Intermediaries' loans are used to provide business loans to RFIs for on-lending to SMMEs. RFI are non-bank independent institutions to which SEFA lends money on a wholesale basis. Their objectives are to provide:

- A funding to SMMEs that would otherwise not be able to access finance from commercial banks;
- SEFA with a vehicle of facilitating access to finance to previously non-bankable SMMEs operating in rural areas; and
- Financing solutions to SMMEs operating in niche markets where traditional financial services would otherwise not be available.

SEFA's loans are used to assist both less experienced RFIs and experienced RFIs. Loans for less experienced RFIs range from R1 million to R10 million. Similarly, loan amounts for experienced RFIs range from R5 million to R100 million.

In order to access these loans, both experienced and less experienced RFIs must meet SEFA's development and institutional criteria. SEFA expects less experienced RFIs to be able to demonstrate credible plans for operations, management and credit policies. Moreover, a less experienced RFI has to give a clear indication of operating sustainability within 60 months or five years. Similarly, for experienced RFIs, SEFA expects that RFIs must be able to self-fund the envisaged programme for at least the first two months of implementation. The RFIs must provide the three year projections that indicate operational sustainability. In addition, the projections must show at least five year financial sustainability (SEFA, 2014).

4.3.3.5 National Empowerment Fund

The National Empowerment Fund (NEF) is a government set-up agency that was established to provide capital for black economic empowerment transactions. It was established in 1998 by the National Empowerment Fund Act, No. 105 of 1998. As another agency of the DTI established to redress the post 1994 inequalities, it is mandated to:

- Promote a better universal understanding of equity ownership through promoting a competitive and efficient economy capable of generating employment opportunities;
- Provide historically disadvantaged individuals (HDIs) with opportunities to acquire shares in restructured state-owned assets and private enterprises;
- Encourage the culture of saving and investment among HDIs and foster entrepreneurship; and
- Achieve its goals of sustainable empowerment and transformation by developing business ventures pioneered and run by HDIs (DTI, 2005).

Because the NEF supports the BBEEE Strategy and related scorecards, it funds HDIs that want to start their own businesses, existing ones that aim to expand and HDIs wishing to acquire shares in existing white-owned enterprises (DTI, 2005). The NEF states that it does not function as a bank and cannot compete with other DFIs, so it stands up to:

- Ensuring consistency of application of various charter scorecards across industries;
- Facilitating transformation in targeted areas and sectors in the economy;
- Facilitating additional funding from others by leveraging HDIs' funding; and
- Offering rural and community development support programmes to assist communities to acquire shares in projects that generate income for social upliftment.

Products offered by the NEF in support of SMMEs include: Entrepreneurial Support and Rural and Community Support as shown in Figure 4.2.

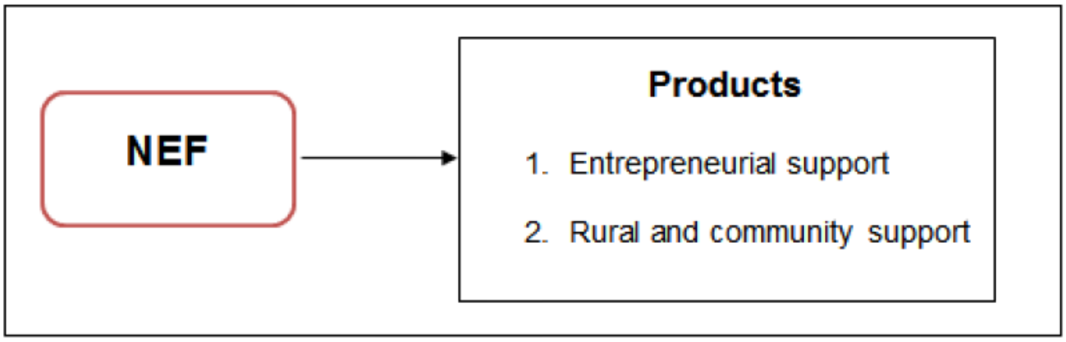


Figure 4.2: NEF funding model

Source: Author's compilation

1. Entrepreneurial Support

Entrepreneurial support offers three types of funding programmes for SMMEs depending on the amount the business requires and the stage of the business cycle the business is in. These programmes include generator, accelerator and transformer as illustrated in Table 4.3 below.

Table 4.3: Types of Entrepreneurial support loans

Product	Amount	Purpose
Generator	R250 000 – R1 million	For start-up and early stage business
Accelerator	R1 million to R3 million	For business expansion
Transformer	R3million to R10 million	For transforming businesses into BEE entities

Source: Author's compilation

2. Rural and community support

The rural and community development projects facilitate community involvement projects that promote social and economic upliftment. The programme supports the BBBEE Act, therefore it aims to increase the extent to which the workers, co-operatives and other collective enterprises own and manage businesses. This product enables communities to acquire shares in income generating projects in historically marginalised economic areas.

Priority is given to or will be given to legally operating enterprises. Moreover, in order for the fund to be effective, the NEF expects the HDI to be assumed to be at risk. The HDIs must, however, demonstrate a contribution to the enterprise, either financially or otherwise. A potential for survival, prosperity and sustainability earns more consideration by the NEF (DTI, 2005).

The NEF's objective is to assist black businesses that are excluded from the financial markets for being considered a risky segment. The NEF therefore intervenes to assist black business to participate in the mainstream economy in the areas of:

- Access to finance;
- Access to markets;
- Insufficient industry knowledge and, where necessary, management experience;
- Equity contribution and lower bargaining power between suppliers and customers;
- Undercapitalisation and low asset base; and
- Lack of reliable, accurate information, management and business planning skills.

The NEF differs from other DFIs in that it is the only DFI exclusively working on the development of B-BBEE.

4.3.3.6 Gauteng Enterprise Propeller (GEP)

The Gauteng Enterprise Propeller (GEP) is a provincial DFI that is mandated to provide financial and non-financial support to small businesses in Gauteng. The provincial government of Gauteng established the GEP in 2005 with the two key objectives of combating poverty and reducing unemployment; and supporting the growth of small businesses and Broad-Based Black Economic Empowerment (BBBEE) to participate in the main stream economy.

The establishment of the GEP has its basis in the Gauteng province's Growth and Development Strategy (GDS). The strategy identified small businesses development to be among key partners in addressing the challenges of unemployment, poverty and inequality. The objective is to assist small businesses to become active participants in the Gauteng mainstream economy, as well as to contribute to the growth and development of key priority sectors.

4.3.3.7 Free State Development Corporation (FDC)

The Free State Development Corporation is a statutory organisation established in terms of the Free State Development Corporation Amendment Act, No. 4 of 2006. It is mandated to establish and develop sustainable SMMEs in the Free State by providing both financial and non-financial services (FDC, 2007). The Act was further amended to also reflect the incorporation of the Foreign Investment and Promotion Agency (FIPA) and became effective from June 2010 (FDC, 2012) with among others the following objectives:

- The promotion and development of small businesses;
- To assist Free State-based small businesses with funding by advancing loans; and
- To initiate economic empowerment projects that would benefit the Free State.

The FDC aims to achieve provincial growth and to develop the strategic goal of promoting sustainable economic development. Although the FDC issues finance to only qualifying entrepreneurs, the institution does not, however, give distinction to “the qualifying”. Nonetheless, the FDC maintains that its activities for the period 2007/2008 targeted supporting SMMEs owned wholly or partially owned by women, youth and people with disabilities. The FDC in its 2007-2014 corporate plan aims to reduce the current unemployment in the Free State which is recorded to be at 38.5% to 20% by 2014 (FDC, 2007).

The FDC is determined to address finance gaps brought by gender and age factors by targeting to serve these markets. It also assists businesses that lack collateral by taking equity if there is an implication of potential for growth and profitability in the business. Furthermore, the FDC claims that it offers business subsidies for tailored services, such as rent rates for emerging entrepreneurs. The businesses that the FDC aims to assist include manufacturing, franchising, retail, mineral beneficiation, tourism and agro-processing. This institution provides three types of loans for start-up capital, expansion capital and bridging capital to small businesses in the Free State as illustrated in the following Figure 4.3.

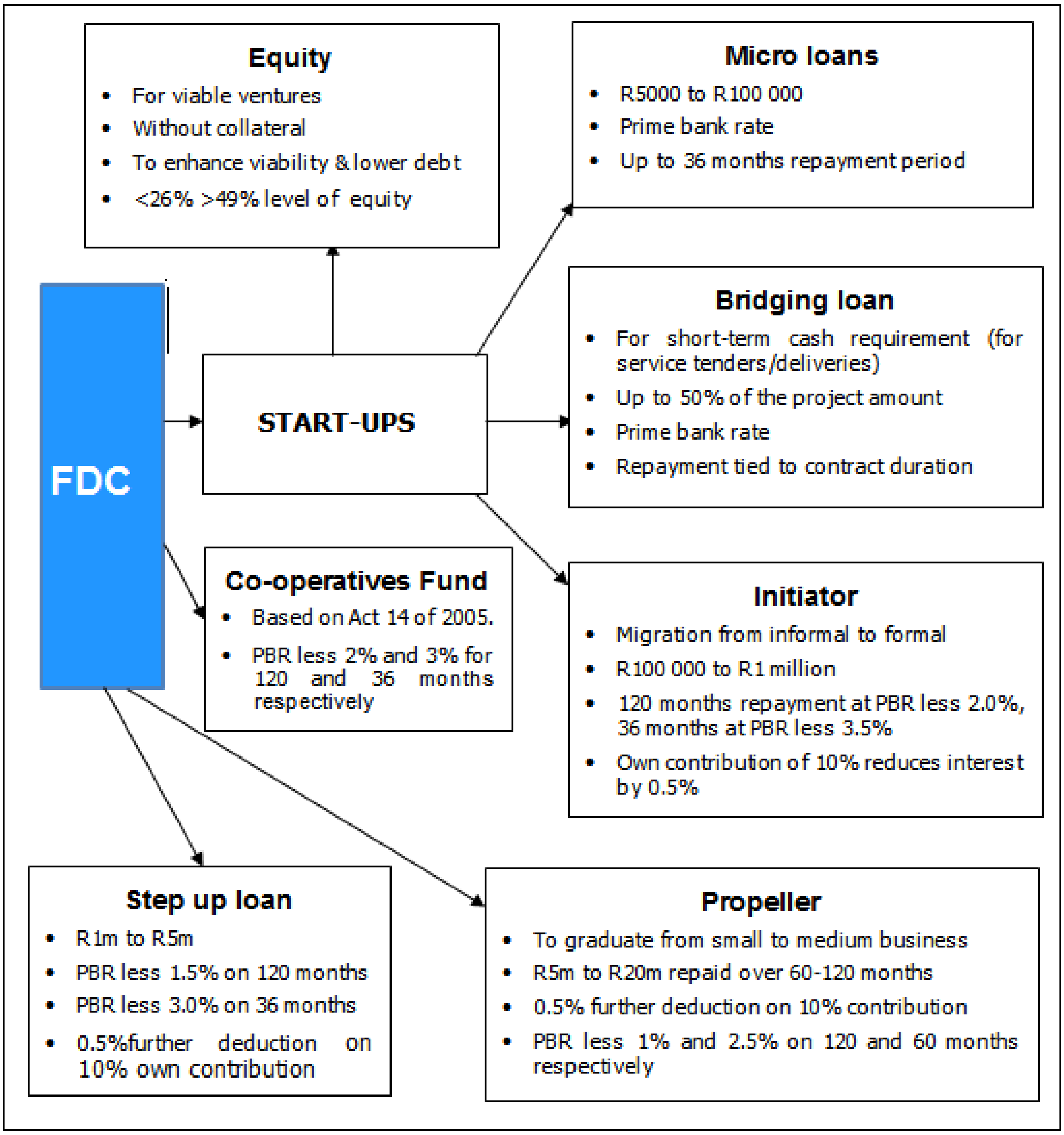


Figure 4.3: FDC financing plan

Source: Author's compilation

As shown in the figure above, micro-loans are issued with a minimum value of R5, 000 and a maximum of R20, 000. The interest rate on these loans is linked to the prime bank rate less 3.5%, with a repayment period of up to 36 months (FDC, 2007).

4.3.3.8 Northern Cape Economic Development Agency (NCEDA)

According to Warie (2011) the NCEDA was established in order to respond to the problems of transforming high-level investment and business opportunities into actual business operations in the Northern Cape. This was done to ensure that business operations could contribute to the economic growth and social equity of the Northern Cape community. As shown in Figure 4.4, NCEDA consists of two units: an economic development unit, and trade and promotion units. The aim of the agency is to promote enterprise development that contributes significantly to economic growth and development in the Northern Cape Province.

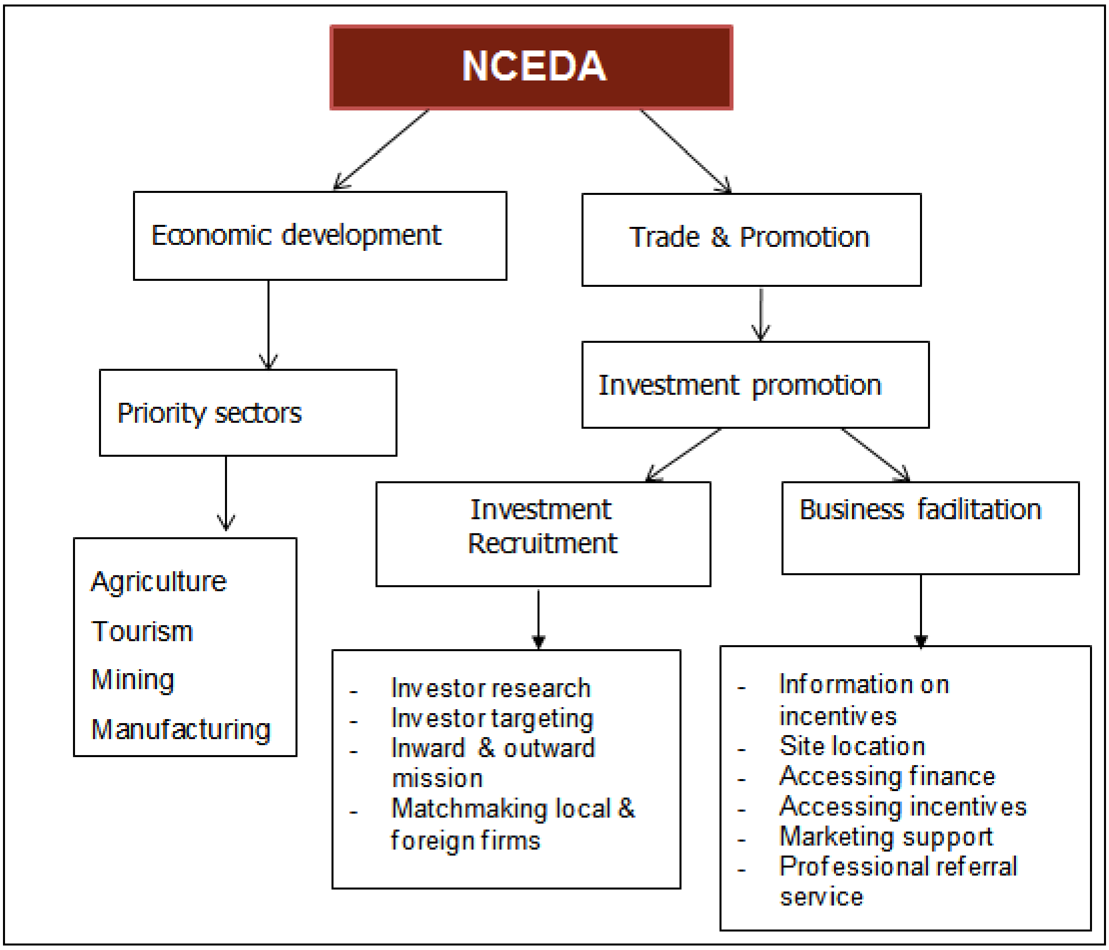


Figure 4.4: NCEDA's Operation Plan

Source: Author's compilation

NCEDA has a strategic focus on three sectors: under the economic development unit agriculture the focus is on tourism; mining and manufacturing, while for the trade and investment promotion unit, the strategic focus is on projects that are ready for investment in the primary sectors. The investment promotion offerings of NCEDA include investment recruitment and business recruitment. The purpose of the former is to proactively market the province and priority industries with the intention of attracting investments. Similarly, the purpose of the latter is minimise delays in the investment process (NCEDA, 2011).

4.3.3.9 Limpopo Economic Development Agency (LEDA)

LEDA was established in 2012 in order to champion the provision of development finance to SMMEs with the purpose of stimulating growth and development in the Limpopo Province. One of the core businesses of LEDA is to promote small business development with the objective of facilitating job creation, which will ultimately help to reduce unemployment and eliminate poverty in the Limpopo province. Figure 4.5 provides an illustration of LEDA's operation plan.

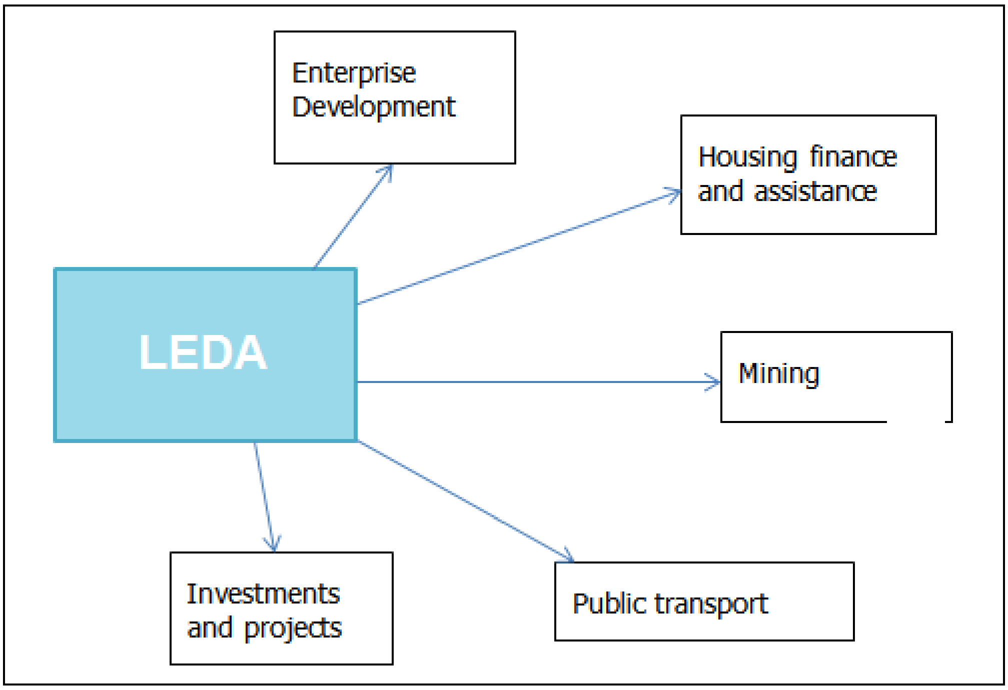


Figure 4.5: LEDA's operation plan

Source: Author's compilation

4.3.3.10 Casidra

Casidra is an acronym for "Cape Agency for Sustainable Integrated Development in Rural Areas". Casidra is a DFI serving in the Western Cape, focusing on rural and economic development. Casidra runs various development programmes in the province, as small business development fall within the programme of Local Economic Development. The main objectives of the programme are to:

- Provide assistance to growth-orientated businesses which lead to employment growth; and
- Provide a project management service to respond to economic development initiatives and programmes.

Through the discontinued Real Business Development (RED door programme), Casidra used to support entrepreneurs, however, the programme has since been taken over by the Small Business Centre that was established to take over the work that was done through the Red Door programme, especially in areas of tender processing and costing (Casidra, 2013).

4.3.3.11 Ithala Development Finance Corporation (IDFC)

The IDFC was established in terms of Section 3 of the KwaZulu-Natal Ithala Finance Corporation Act, No. 2 of 1999 to channel financial resources in order to provide both financial and supportive services to the people living in KwaZulu-Natal. Through proper planning and execution, the institution is mandated to finance and monitor the implementation of development projects and programmes. These projects and programmes are aimed at promoting, assisting and encouraging the development of human resources, social, economic, financial and physical infrastructure within the province. Furthermore, the institution is aimed at promoting, encouraging and facilitating private investment, as well as ensuring the participation of the private sector along with community organisations in development projects and programmes that contribute to economic growth and development.

The IDFC provides both financial and non-financial support to small businesses and co-operatives. In order to ensure the growth and success of businesses in KwaZulu-Natal, both established and star-up businesses are supported through the institution’s business finance that provides for short-, medium- and long-term financing products. The DFI also provides business support and mentoring services to emerging entrepreneurs in the province. The co-operative lending programme is meant to assist communities to form co-operatives and to have access to finance in order to reduce poverty and unemployment by contributing towards increasing disposable income amongst second economy participants (Ithala, 2012).

In its repositioning strategy after the poor performance prior to the 2013/2014 financial year, IDFC aligns its activities with the provincial growth and development strategy (www.pmg.org.za). To achieve this alignment, the institution has three business units as shown in Figure 4.6.

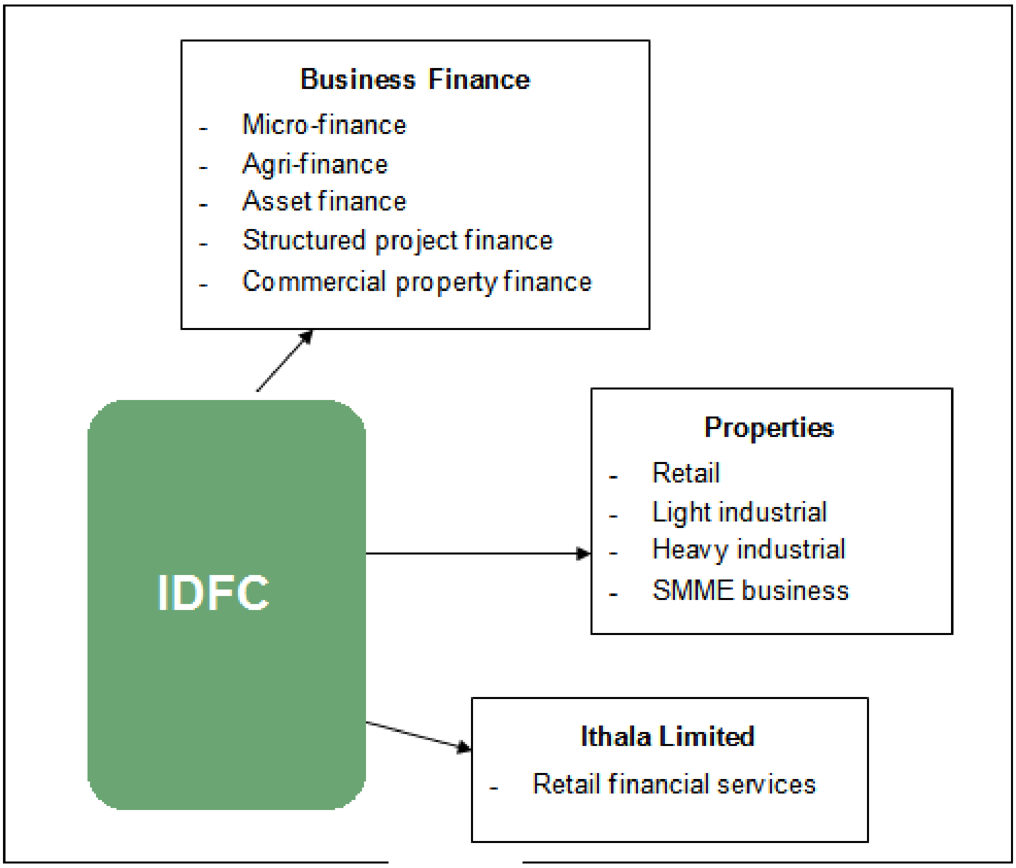


Figure 4.6: IDFC operating model

Source: Author's compilation

4.3.3.12 Mpumalanga Economic Growth Agency (MEGA)

The MEGA was established in terms of the Mpumalanga Economic Growth Agency Act, No.4 of 2005 to promote the development and growth of SMMEs and co-operatives in the province of Mpumalanga. The agency was established through the merger of the Mpumalanga Economic Empowerment Corporation and the Mpumalanga Investment Initiative. This DFI is aimed at leveraging trade and investment, providing finance to small businesses, and to provide housing finance to the Mpumalanga population. The MEGA offers business loans between R10 000 and R1 million, as well as bridging finance to businesses with existing contracts. The institution also assists in the development of co-operatives in the province.

As a DFI, MEGA works with the IDC, SEFA and NYDA as strategic partners. In order to qualify for the support of MEGA, the businesses must be owned by individuals over the age of eighteen years and older who are from designated groups; be registered and operate on a full-time basis in priority sectors of the Mpumalanga Province. In the case where the business is owned by more than one person, at least one of the owners must be fully involved in the business operation; and the business is expected to have at least 26+1% BEE shareholding (MEGA, 2012). Figure 4.7 provides an illustration of the MEGA operation model.

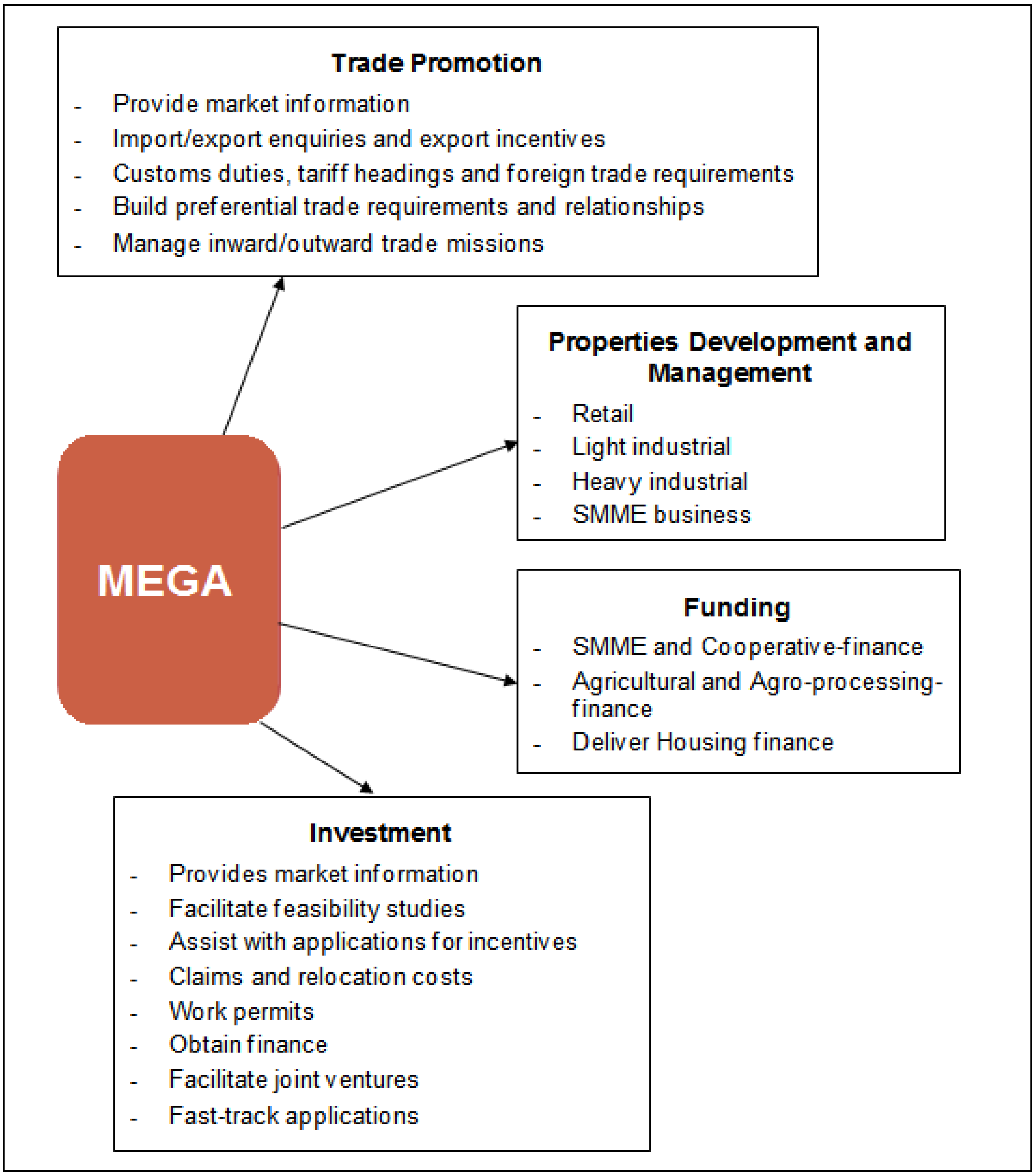


Figure 4.7: MEGA operating model

Source: Author's compilation

4.3.3.13 Eastern Cape Development Corporation (ECDC)

The ECDC is an economic development and investment agency established in 1996 to serve the community of the Eastern Cape Province. Among other things, the ECDC is mandated to facilitate economic development; stimulate exports; build existing businesses; and to facilitate start-up businesses. The ECDE understands the importance of small businesses towards growth and development in the country, especially for the Eastern Cape province, therefore the DFI is committed to provide the much needed support, resources, investment, and capital opportunities for the sector. As shown in Figure 4.8, the objectives of the ECDC include: to attract new investors and position the Eastern Cape as an investment target; to stimulate exports; to facilitate economic development; to build existing and to facilitate start-up businesses (ECDC, 2013).

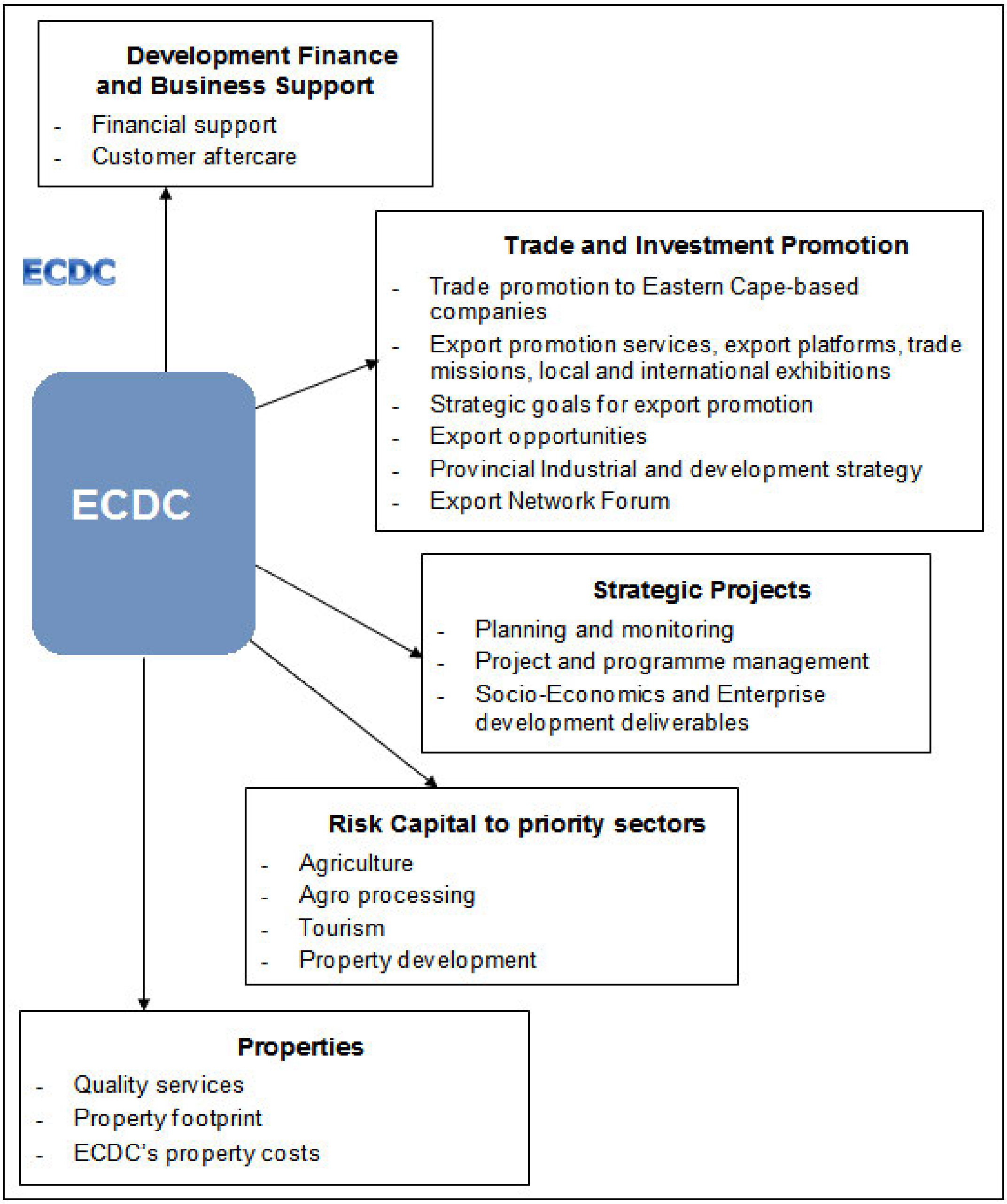


Figure 4.8: ECDC operating model

Source: Author's compilation

Figure 4.8 provides an operation model of the ECDC including the support of small businesses. Small businesses that intend or are involved in any of the identified business operations get support from the ECDC. The institution offers loans from R10 000 up to R20 million to small businesses that have head offices in the Eastern Cape with collateral not being prerequisite, but some form of contribution by the owner/s is required to indicate commitment. These loans can either be short or long term, depending on the need and assessment of individual business. The main objective of the support by the institution is to bring a meaningful development impact to the province (www.ecdc.co.za).

4.3.3.14 North West Development Corporation (NWDC)

The NWDC is a DFI established under North West Development Act No 6 of 1995 to serve the North West Province with a specific focus on industrial promotion, trade, customer protection and trade regulation. The aim of the DFI is to contribute to economic growth by focusing on the sustainability of sectors such as agriculture, culture and tourism in villages, townships and small settlements. As a public entity classified as Schedule 3D of the Public Finance Management Act, the institution operates within the legislation arm of the following Acts of the country:

- Constitution Act, No 108 of 1996
- Public Finance Management, Act No 1 of 1999
- National Credit Act, No 34 of 2005
- Rental Tribunal Housing Act of 1999
- Companies Act, No 71 of 2008
- Small business Act, No 102 of 1996
- Co-operatives Act, No 14 of 2005
- South African Revenue Services Act, No 34 of 1997

With its economic development agenda, the NWDC was mandated to focus on the facilitation and promotion of fixed direct investment; export promotion and the development of programmes in the priority sectors of mining, manufacturing, tourism and agriculture, and to assist in the trade development in the second economy in order to boost the capacity of various exports market.

4.4 CONCLUSION

This chapter discussed the small businesses and DFIs in South Africa. The first part of the chapter provided a holistic picture of small businesses in South Africa. The section portrayed the profile of small business sector along with detailing the growth challenges facing the sector. The role played by small businesses against developmental issues in South Africa were also dealt with in this section of the chapter. The crucial stance taken by the government through its Department of Small Business Development towards developing small businesses against the highlighted challenges was also displayed in this chapter. The second part of the chapter dwelled on the role played by the government of SA in providing developmental finance through its development finance institutions (DFIs). Their distinctive operations were discussed in order to display their individual roles in small business development.

The next chapter is based on the methodology employed in the study in answering the research question.

CHAPTER 5: RESEARCH METHODOLOGY AND DESIGN

5.1 INTRODUCTION

The previous chapter discussed the perspective of South African small businesses as well as the available DFIs. The purpose of this chapter is to provide the details of the methodology applied in carrying out this study. The methodology in this study was designed to incorporate the approaches that were deemed necessary to gather the information required to investigate the role of the DFIs in advancing finance to small businesses in South Africa. While the preceding chapters were based on the conceptual and theoretical background to the study, the current chapter is based on the objectives and research design; sampling description and techniques, the research instruments and data analysis techniques that were utilised in this study. Most importantly, this chapter highlights the purpose and objectives of the study, along with research questions and the methodology employed to achieve these objectives to reach a conclusion for the research statement, a thesis.

As recommended by Saunders, Lewis and Thornhill (2003), the study used the research process onion (Figure 5.1 further on), which offers both the comprehensive and structured approach of the research process. The research process onion provides a complete set of details of why a particular data collection method was chosen.

5.2 PURPOSE OF THE STUDY

The primary objective of this study is to understand the role of the DFIs in financing small businesses as an instrument of growth and development in South Africa for the period 1996 – 2012.

5.3 RESEARCH DESIGN

The researcher has the responsibility to clarify a method through which the answers to the scientific inquiry are to be obtained. According to Kerlinger (1986), research design is a preconceived plan and structure that is meant to provide the answers to the research question. The scientific inquiry that investigates a phenomenon needs to address the three questions: ontological, epistemological and methodological questions. Ontological and epistemological questions provide for two different ways of viewing the philosophy of inquiry or research. Ontological questions clarify the nature of reality, either objectively or subjectively (Hudson & Ozanne, 1988); while epistemological questions clarify the manner in which the researcher relates to reality (Carson *et al.*, 2001).

If we consider the epistemological question: "What is knowledge?"; the question unpacks: the ways in which data is truthfully and reliably obtained to address sociological research and theory, the best methods of analysis to use; and the information about what people know. Mouton (2008) claims that the epistemological question is embedded on what is distinctive about the world of science and how it is different from the world of everyday life; and hence the search for truthful knowledge.

Based on these ideologies, two epistemological aspects considered in this study are: (i) what knowledge is and what are the parameters within which an understanding of everyday life can be known? And (ii) how knowledge is acquired and how knowledge can be displayed? According to Henning *et al.* (2009) epistemology is the philosophy of knowledge, “how we come to know”. And this philosophy is closely related to the methodology which means that we come to know by inquiring in particular ways. The beliefs about the nature of reality and knowledge guide this study in relation to the questions asked. The underpinning assumption is that there are manifold realities, and individuals give meanings to those realities based on their experiences in order to understand what they are experiencing (Morgan & Smircich, 1980).

The ontology and epistemology have two ideologies: positivism and interpretivism. These paradigms display the position that the researcher decides to take in revealing knowledge.

5.3.1 Positivism paradigm

According to positivist ontology, the world is external and objective reality does not exist in any research phenomenon, irrespective of the researcher’s belief or perspective. That is, the purpose of science is independent of emotions and thoughts. In a positivist framework, according to Henning *et al.* (2009), science is seen as the way to get to the truth and to understand the world well enough so that it can be controlled by a process of prediction. The positivists believe that the world operates by the law of cause and effect that researchers can detect by means of scientific methods. Positivist research progresses through hypotheses and deductions, with concepts being operationalised so that they can be measured.

Statistical and mathematical techniques are central to consistently and logically discovering the truth. These techniques provide for independence between the researcher and the researched (research subjects). In other words, researchers remain detached from the participants in order to maintain emotional neutrality through the creation of distance (Carson *et al.*, 2001). Researchers following positivism prioritise on objectivity (Hudson & Ozanne, 1988). Knowledge is sourced from sensual experience and observation, while an assumed reality is systematically described, and not essentially measured. Researchers that follow the positivism paradigm use scientific methods of inquiry such as experiments and surveys to maintain objectivity.

5.3.2 Interpretivist paradigm

The ontological and epistemological view of interpretivists is that reality as we know it is constructed inter-subjectively through meanings and understandings developed socially and experimentally; and we cannot separate ourselves from what we know (Cohen & Crabtree, 2006). That is, the reality cannot be separated from our knowledge. The interpretivist perspective believes that reality is multiple and relative and hence, Lincon and Cuba (1985) further explain that these multiple realities rely on other systems for meanings. The view of this paradigm is that access to reality is only through social constructions such as language, consciousness, shared meanings and instruments. Interpretivists do not view the world in isolation, but view it through a series of individual eyes (Dudovskiy, 2016), and believe it to be constructed by human beings.

Unlike positivists that isolate the objects of natural science research from the researcher, interpretivists believe that social research subjects are dependent on, and are the creation of human beings and therefore more subjective than objective (Willis, 2007). An interpretivist or a constructivist researcher relies on the views of research subjects about the phenomenon (Creswell, 2003).

Researchers that follow the interpretivist paradigm, enter the field with some sort of prior insight of the phenomenon, but acknowledge that the prior information is not enough to develop a fixed research design on account of the complex, multiple and unpredictable nature of reality (Hudson & Ozanne, 1988). The findings or knowledge from constructivist research is created as the investigation progresses and emerges through dialogue (Cohen & Crabtree, 2006). Saunders *et al.* (2007) developed the research onion, as shown in Figure 5.1, to illustrate the different steps through which a researcher goes in order to successfully formulate a research methodology.

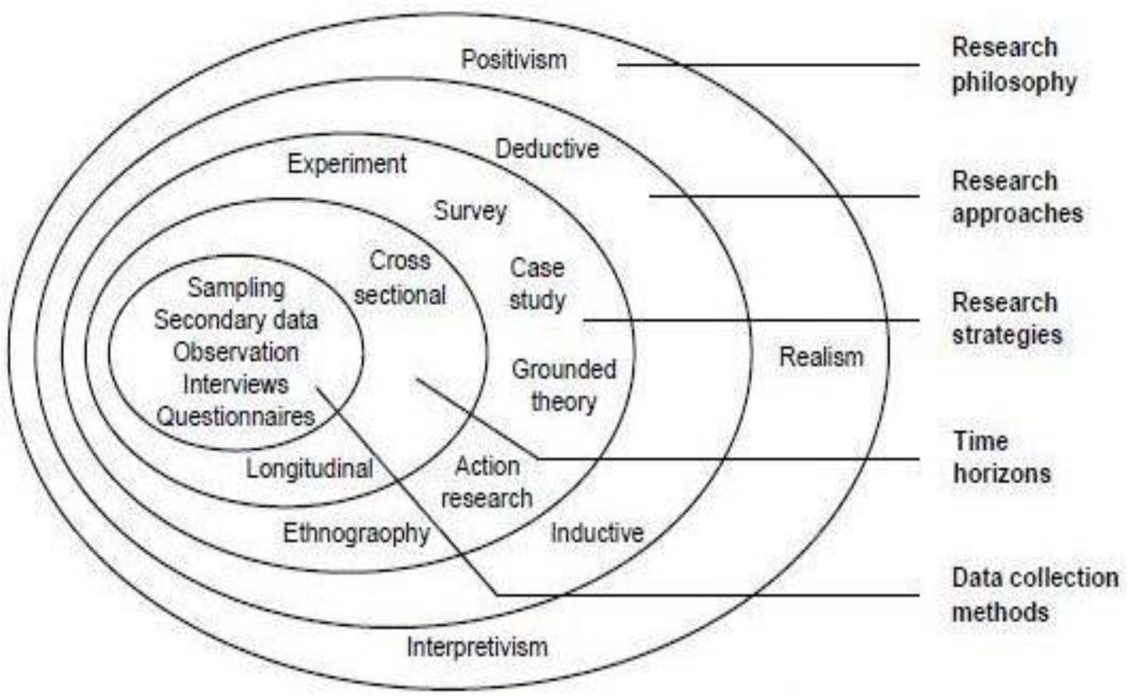


Figure 5.1: The research onion

Source: Saunders, Lewis & Thornhill, 2003

Firstly, the philosophy of research needs to be clearly defined. This will enable the establishment of the second step which is to appropriately design the research approach. Thereafter, the third step of adopting the research strategy follows. The fourth layer of the research onion is the identification of the time scope. And finally, the methodology of data collection is identified in the fifth step.

5.3.3 The researcher's philosophy

According to Creswell (2003) the interpretivist or constructive researcher most likely relies on qualitative data collection and analysis methods, or a combination of both qualitative and quantitative methods (mixed methods). Quantitative data may be utilised in a way which supports or expands upon qualitative data and effectively deepens the description. The researcher views the world with an interpretive lens. This philosophy as Henning *et al.* (2009) assert, understands that knowledge is not only constructed by observable phenomena, descriptions of people's intentions, beliefs, values and reasons, meaning making and self-understanding, but that it is also dispersed and distributed.

Given this background, the researcher was interested in unpacking and understanding the meaning that the heads of financing departments or sections within the DFIs had constructed about how they made sense of the financing world along with experiences they had in financing small businesses.

To achieve the research objectives, the study used both an applicable literature review, as well as empirical data. No single method was deemed adequate to achieve the objectives of the study; therefore, a mixed-methods approach was used. On the one hand, a literature review was used for both the theoretical and conceptual framework part of the study, which was made possible through the use of up-to-date relevant information retrieved from relevant scientific journals, books, reports, working papers, as well as relevant business and institutional websites.

On the other hand, empirical data was obtained from both qualitative and quantitative modes of inquiry, as these approaches were deemed necessary to provide the answers to the questions developed in achieving the research aim. Current studies on small business access to finance are predominantly quantitative in nature. The researcher realised that no single approach will be sufficient to provide the needed information for this study. In this study, therefore, the researcher, as an interpretivist, decided to use a combination of both quantitative and qualitative methods (Creswell, 2003). Obtaining information from both qualitative (supply side) and quantitative (demand side) approaches was deemed more comprehensive in providing the desired outcomes of this study. Although the study is predominantly qualitative, quantitative data was used to complement and expand the qualitative data.

The study therefore, had two phases of data collection: the qualitative phase and the quantitative phase. Phase 1 was aimed at exploring the programmes the DFIs have in small business that allow for growth and development, and to identify the extent to which DFIs bridge the financing gap facing small businesses in financial markets. Phase 2 sought the perceptions of the entrepreneurs regarding the impact of the Phase 1 outcomes on the growth of their businesses, as well as to measure the outcomes of Phase 1. The methodology adopted for this study is referred to as a sequential exploratory mixed-methods approach. Creswell (2014) states that although the sequential exploratory mixed-methods approach has two phases, the study is skewed towards qualitative techniques, unlike the sequential explanatory mixed-methods approach which is skewed towards quantitative techniques. In sequential exploratory mixed methods, qualitative data is gathered and analysed in the first phase. Thereafter, the information is used to develop quantitative research instruments in order to gather quantitative data.

The study could have used any form of mixed methods: triangulation, explanatory, concurrent or conversion methods, however, the phenomenon under study requires that the qualitative approach be carried out first in order to inform the quantitative approach as the second stage of the research. The current study is exploratory in that it focuses on exploring a contemporary topic (growth of small businesses) from a new perspective (development finance). This study concentrates on the development finance institutions that are state-owned and excludes all institutions that provide development finance to small businesses that are owned and funded by non-governmental entities. Many studies in this field use either a survey approach to gather information from the demand side of access to finance (entrepreneurs / small businesses) or the supply side (financing institutions). However, this study is vigorous as it analysed the data that is gathered from both supply and demand side, as shown in Table 5.1.

Table 5.1: Summary of research methods employed in the study

Objective	Source of data	Methodology and tools	Analysis
- To explore the programmes the DFIs have in financing small businesses for growth and development of the sector. - To investigate the extent to which the DFIs bridge the gap that exists in the financial markets for small businesses - To examine the limiting factors for the DFI to finance small businesses.	- 4 Programme heads/managers and 3 credit managers of the DFIs (NYDA, DSBD, SEFA & IDC) - 6 investments/ credit officers of provincial DFIs (LEDA,FDC,NCEDA CASIDRA & EDA) - Policy documents	- Interviews - Documents	- Content analysis (Atlas.ti 7) - Document analysis
- To determine the extent to which the availability of finance aligns to growth strategies for small business.	- Literature study	- Desktop study	- Researcher's analytic skills
- To explore the perceptions of the entrepreneurs on how the DFIs impact on the growth of their businesses across demographic lines. - To investigate the propositions that entrepreneur have for small business development finance - To investigate the perceptions of the respondents on DFIs financing with regards to bridging the financing gap	- 301 entrepreneurs in Tshwane Metropolitan Municipality	- Questionnaires - In-depth face-to-face interviews	- SPSS - EFA - T-test - ANOVA - Pearson Coefficient - Thematic and content analysis
- To recommend a framework guiding the DFIs to assist small businesses to achieve sustainable growth	- Both literature study and empirical research	- Synthesis	- Researcher's skills and experience

Source: Author's own compilation

5.3.4 Literature study

The main aim of the literature review was to explain the important concepts as applicable in this study. The study also covered aspects such as contribution of

SMMEs in the economy, and constraints that the SMME sector faces. Funding requirements have also been discovered from the review of literature. In particular, matters relating to small business, including the components thereof, were discussed as part of the literature review. The literature study provided valuable information on small businesses, including the SMME importance and challenges. Issues of finance were also discussed as an integral part of small business development. This part of the study provided an account of commercial financing in the context of SMME development in order to illustrate the financing gap faced by small business, a challenge for business growth. Commercial financing became an important point of reference for development financing, the core of this study.

The literature study also assisted with regard to the theoretical landscape of this study. With the help of the desktop study, the South African small business sector and development finance institutions were also portrayed. Various lending programmes by a range of DFIs have formed part of the literature review. The literature review was made possible through the use of up-to-date relevant information retrieved from relevant scientific journals, books, reports, specific websites of financing institutions, and working papers available for business finance, as well as the annual reports of the DFIs.

The purpose of a literature or theoretical study is to review and discuss the most relevant and appropriate theories, definitions and models of a phenomenon under inquiry. The literature review forms the theoretical framework for the empirical study (Mouton, 2008). Similarly, in the current study the aim is to explain the meaning of the concept of development financing within the context of the growth and sustainable development of small businesses.

According to Kumar (2005) the literature review has four most important functions; it helps to:

- Bring clarity and focus to the research problem;
- Improve the research methodology;
- Broaden the knowledge base of the research area; and
- Contextualise the findings.

Based on these, the literature review has firstly helped the researcher to understand the relationship between the research problem and the body of knowledge in the area of development financing. Secondly, it has helped to identify, from other researchers, the methods and procedures used in investigating similar research questions to the one being investigated in this study; to find those that have worked well and those where problems were encountered. Having knowledge of these pitfalls, the researcher was in a position to select the method that was capable of providing valid answers to the research question. In addition the researcher is confident in defending the use of the methodology used in this study **(validity)**.

Thirdly, the literature review has broadened the knowledge base of the researcher to be able to identify the gaps, and to clarify how the current findings will fit into the existing body of knowledge. Lastly, upon fitting into the existing knowledge, literature also helps in comparing the current answers with what others have found in order to identify how the study contributes to the existing knowledge. Continued referral to the literature review helped in distinguishing the current study from others without compromising the importance of placing the findings in the context of what is already known in the field.

5.3.5 Empirical study

This is part of the investigation where the researcher gathers empirical information through observation and experimentation. The empirical study consisted of both a qualitative (Phase 1) and quantitative (Phase 2) phase. The former was set as the basis of the study and the latter was used to support and expand on the former (constructivist perspective).

5.3.5.1 Phase 1: Qualitative phase

The qualitative phase was conducted first. During this phase, the qualitative paradigm was used to obtain rich information from people who are directly involved with the financing of small businesses in their natural setting (Creswell, 1998; Merriam, 2001). As Mouton (2008) suggests, the approach focuses on people’s own experiences; and studies people in terms of their own definition of the world, while being sensitive to the context in which people interact with each other. Bhatnagar (2012) shows that in qualitative research, questions probe with a smaller sample size but get much more information per respondent which requires an interviewer with special skills through the use of various data collection instruments. Analysis is allowed to be subjective and interpretative (Ntiso, 2010).

The qualitative approach is defined by Nieuwenhuis *et al.* (2007) as the methodology that is concerned with understanding the process, the social and cultural contexts which underline various behaviour patterns. The qualitative approach is mostly concerned with exploring the "why" questions of research. The qualitative approach seeks to explore and understand the experiences, actions and feelings of the respondents; the questions are designed to be broad and open-ended (Ivankova *et al.*, 2007). The methodology typically studies people or systems by interacting with, and observing the participants in their natural setting, focusing on their meaning and interpretation (Holloway & Wheeler, 1996). The approach tries to reconstruct the interpretation, describe or reconstruct the depth, richness, as well as the complexity of the phenomenon at hand, with the purpose of understanding and gaining insight into that phenomenon (Burns & Grove, 1997).

As Ntiso (2010) asserts, this method has been found to be relevant for this research as it intended to answer the question "What is the role of development finance in financing small businesses in South Africa?" The most appropriate information for this particular question was sourced from the managers or programme heads who are directly responsible for small business funding within the DFIs.

Information was gathered through use of face-to-face in-depth interviews and some telephonic interviews with the programme managers of small business development units of the DIFs. The information was supplemented by the review of literature and the desktop study.

5.3.5.2 Phase 2: Quantitative phase

The quantitative phase was conducted as the second phase of the study following the completion of the first phase. This approach was believed to be the most appropriate to address the objectives of the study that could not be achieved through qualitative research techniques. The second phase was used to both complement and supplement the first phase research.

Even though it is a common practice in quantitative research to have hypotheses, this is not the case in this study. Bryman and Cramer (2001) contend that although hypotheses have the advantage of forcing researchers to think systematically about the phenomenon, the former have a potential disadvantage, as they (hypotheses) may divert the researcher's attention too far from other facets of the data collected. Based on this assertion, the researcher believed that the study being an exploratory study, has the potential to reveal other facets and therefore hypotheses could not be used.

5.4 POPULATION AND SAMPLING TECHNIQUES

The population is defined as the total number of people or units of analysis. A sample is a sub-set of the population which has all characteristics of the whole population under enquiry. Sampling refers to the process that is used to select a representative of the population for study. As stated, this study used an exploratory sequential mixed-methods design consisting of two phases. The study used different sampling techniques for the two phases of the study: the qualitative stage and the quantitative stage as explained below.

5.4.1 Phase 1 sampling

Purposive sampling was used for the qualitative part of the study. Only heads or managers of small business funding programmes within the DFIs were chosen to participate in the study. This sampling method means that participants are selected because of some defining characteristics that make them the holders of the data needed for the study (Nieuwenhuis, 2007). Congruent to the objectives of the study, purposive sampling was used for the qualitative stage of the study because the subjects possess some specific attributes and have the expertise and specific insight regarding small business financing.

Purposive sampling is non-probability sampling which refers to the collection of information from persons that possess some distinct knowledge with regard to the study phenomenon. Sampling in the qualitative/ interpretive approach always uses purposeful sampling. This type of sampling increases transferability of the study and maximises the range of information that can be obtained about the object of the study (Babbie & Mouton, 2001: 400). This sampling was considered the best sampling method, because according to Patton (1990) it is about the selection of information-rich cases for the study. Therefore, the study subjects were chosen because they deal with the financing of small businesses and hence, are likely to be the most knowledgeable and also informative about the phenomenon that the researcher was investigating. The population for Phase 1 was 14 managers of SMME development/ financing units of the DIFs and the sample size was 11. Through snowball sampling, three credit officers also became part of the study.

The initial stage of the study was qualitative and exploratory in nature and therefore was limited only to research participants that were believed to be the most relevant to the study, implying that the size of the sample was allowed to be small (Payze, 2004).

In qualitative research, the content of the information is more important than the size of the sample. Denzin and Lincoln (2000) indicate that since qualitative research is not focused on statistical significance, there is no requirement that samples should be of a significant scale to achieve this. The sample size is allowed to be reasonably small in order to do justice to the rich evidence as allowed for qualitative studies and to make the best use of the resources available for intensive research (Ritchie & Lewis, 2003). According to McMillan and Schumacher (2001), a purposive sample size can range from n = 1 to n = 40 or more. In qualitative research, saturation is important. Once saturation is reached and no new themes emerge during the data collection, the researcher can cease to continue with data collection (Nieuwenhuis, 2007).

The population was 14 managers (9 provincial DFIs and 5 national DFIs); only government DFIs were included in the study and any other development institutions were excluded. The targeted purposive sample was 13 (4 heads or managers and 3 credit officers (through snowball sampling) at national level and 6 from provincial level) of the DFIs in South Africa who are engaged in the financing of small businesses and who therefore, have direct contact with finance application requests from small businesses. From the provincial DFIs only 6 had participated after which saturation was reached. This phase of the research was conducted between 8 September 2013 and 4 November 2014 and depended heavily on the availability of research subjects. The other research subjects that were invited to participate declined the invitation.

5.4.2 Sampling frame for Phase 2

For Phase 2, the population of the study was 3 789 entrepreneurs who are in the databases of the DFIs and Local Economic Development (LED) unit of Tshwane Metro Municipality of Gauteng region and whose businesses were financed by the DFIs during the period, 1996 - 2014.

Simple probability sampling was used in selecting the respondents of Phase 2 of the study, as a complementary to Phase 1. A probability sample which is denoted a letter “n” was constructed from the population (denoted by the letter “N”), that is n/N is a representative of the population. According to Cooper and Schindler (2014) the acceptable sample size is at 5% or more. Although the actual size of the sample would be correct at 189 derived from (3789 x 0.05), a sample of 500 was therefore, deemed acceptable. Accordingly, the sample consisted of 500 small businesses located in Wonderboom, Soshanguve, Mamelodi, Mabopane, Hammanskraal, Centurion, Atteridgeville, Laudium, Ga-Rankuwa, the central business district (CBD), Eersterus and Eastlynne. A total of 500 questionnaires, as shown in Table 5.2, were distributed and 301 were returned, representing a 62% response rate. The sample was believed to be sufficiently representative of the total population to provide the much desired outcomes of the research questions, because each member in the population had an equal opportunity of being included in the sample (Bryman & Cramer, 2001).

Table 5.2: Sample size of second phase of the study and successful responses

Item	Value
Population	3789
Sample	500
Responses	301
Response rate	62%

Source: Author's compilation

The response rate of 62% is considered a very successful rate, given that the sample size was more than an acceptable value of 5%.

5.5 DATA COLLECTION

Jack and Anderson (2002) state that the major aspect of field research is decisions on who to collect data from, as well as ways in which data is to be collected, whereas Sakaram (1992) mentions that data can be collected in different ways from different sources and settings. Primary data is the most important source of information in this study. Data was collected by means of in-depth interviews and questionnaires over the period of nine months. The benefit of combining both qualitative and quantitative data is that it offers more insights and results in more questions for future research. Using a mixed-method approach to research maintains the strengths and eliminates the weakness of using a single research approach (Creswell, 2012).

5.5.1 In-depth interviews

In this study, the researcher personally conducted face-to-face and telephonic in-depth interviews to ensure that no relevant information could possibly be lost during the interviews, either by lack of probing or through overlooking of certain information. Due to logistical constraints, such as costs, telephonic interviews were used to conduct interviews that would have implicated more costs than using face-to-face interviews, especially during follow-up interaction with the research participants. Babbie (2010) shows that the presence of the researcher increases clarity of the interview by probing for answers. The presence of the researcher helped to clarify questions unclear to respondents, while the latter were allowed to ask questions as well. The researcher, however, needs to be the medium of neutrality through which questions and answers are transmitted. For this reason, the different researchers should be able to obtain exactly the same response from the same participant (**reliability**). The presence of the researcher therefore plays a critical role in qualitative interviews. This is also backed by Babbie and Mouton (2001) who argue that the researcher is the main instrument in the research process.

According Lodico *et al*. (2006), **credibility** is used to establish whether the perceptions of the research participants match up with the researcher's portrayal of them in the research report. Just like the aspects of reliability and validity in quantitative research, credibility in qualitative inquiry helps to establish the extent to which the instrument used by the researcher measures what it is intended to measure; and is likely to yield an accurate and true picture of the research setting and participants. In-depth interviews were used as the instruments of inquiry in this first phase of the study with the help of the interview guide to quest the phenomenon of development finance from the perspective of finance providers (the DFIs – supply-side). The instrument did measure what it was meant to measure. Given that reliability is defined as the reproducibility of the measure (Nobel & Smith, 2015), it implied therefore, that if the study were to be done again the same results would still be found.

The use of different data sources (Lincon & Cuba, 1985) and the amount of time spent (no less than 1 hour per interview, the months spent on the desktop study and follow-up emails and telephonic communication techniques, ensured the credibility of the methods. Similar to the word **validity** as used in quantitative research, the words such as credibility (Lincon & Cuba, 1985), truth, value, trustworthiness (Glaser & Strausss, 1967) are commonly used in qualitative research (Brink, 1993). The method was found to be the best way to reach the desired results of the first phase of the study and no other way would be more appropriate (Lincoln & Cuba, 1985**).**

5.5.2 Questionnaires

To help the researcher to gather quantitative data, questionnaires were used as instruments to conduct a survey study. The researcher personally administered the questionnaires. By personally administering the questionnaire a researcher has the advantage of creating and maintaining a connection/understanding with research subjects. The understanding also helps the researcher to solve any obstacle that the subjects may encounter during the questionnaire completion. Furthermore, personally administering questionnaire increases the chances of a high response rates among the research participants.

As a procedure, an introductory section was included to clarify the reason for the study. The research subjects were informed of their voluntary consent to participate and that no incentive was to be offered as the study is purely for educational purposes and not for commercial gain.

In formulating the questionnaires, attention was given to the criteria as highlighted by Eselen *et al.* (2005) that questions should:

- Be short, simple and to the point;
- Have clear instructions;
- Not contain double negatives;
- Be phrased neutrally;
- Not contain emotive language;
- Not make respondent feel guilty;
- Not have prestige bias;

- Accommodate all possible answers;
- Not make assumptions;
- Not talk about a hypothetical situation; and
- Responses alternatives should be:
  - Mutually exclusive; and
  - Asked to express opinions about their own views not what they think the view of somebody else might be.

In formulating questions, attention was given to the above-mentioned guidelines. Although there are two-question formats that can be used in questionnaire surveys: open-ended and close-ended questions, the latter was preferred and used in this study. The former, also referred to as unstructured or free response questions, were used during the pilot study to help in the formulation of some questions. Due to time constraints and the impracticability of such questions during this phase of the study, the researcher opted to use mainly the close-ended questions although the open-ended questions were also used for some questions in order to ensure that no information had been omitted and to clarify other responses to closed or coded questions (Bulsara, 2015). The main concern was whether the chosen format would help to answer the relevant research questions, and the chosen format was found to provide the desired outcomes.

5.5.2.1 Pre-testing and pilot study

The questionnaires were administered to a research team of academics in the Department of Business Management at the University of South Africa. The individuals were well acquainted with the nature of the study which helped them in providing constructive inputs with regard to the design and reorganisation of the questionnaires. The redesigned questionnaires were the used in the pilot study. The purpose of the pilot study was to establish the content validity of scores on the questionnaire and to improve the questions' format and scales (Creswell, 2014). As a rule of thumb (De Vos, 1998 and Kumar, 1996) suggest that the pilot study must not be administered to the same sample used in the main survey. According to Bryman (2001) some of the benefits of the pilot study for the main survey research include:

- The generation of fixed-choice answers where the main study is intended to make use of close-ended questions, the pilot study can use open-ended questions;
- Rephrasing of questions by the researcher upon realising that questions are not clearly understood or confusing after the pilot study;
- The adequacy of instructions given to the respondents for answering the questions can be established; and
- The researcher can determine whether or not the flow of the questions needs to be rearranged in order to improve data acquisition.

A sample of 40 entrepreneurs located in Pretoria East, were chosen for the pilot study. The overall feedback received from the pilot study showed that the entrepreneurs did not encounter any difficulty in understanding the instructions or wording of the questions. Therefore, no major adjustments were made to the questions in this regard. However, the feedback from the open-ended questions indicated that close-ended questions relating to “stokvels” and "small business development bank” could be added to the main survey.

After making appropriate adjustments to the questions, the questionnaires were administered to the sample of the study.

5.5.2.2 Reliability

Tavakol and Dennick (2011) point out that validity and reliability are elements fundamental for the evaluation of the measurement instrument for conventional knowledge, skill or attitude test of survey questionnaires. The instruments are used to measure concepts, skills or affective values. Reliability is the consistency of a set of measurements. The reliability determines whether the measurement of the same instrument gives or is likely to give same values (test-retest). A Cronbach's alpha value of very close to 1 is considered a good indicator of the reliability of a measuring instrument. The Alpha coefficient was developed to measure the internal consistency of the test or the scale. The internal consistency or reliability concept assumes that uni-dimensionality exists in the sample of test items (Cronbach, 1951).

This coefficient value generally increases parallel to the increase of the correlations between the items (or questions) of the measurement, and hence the value is also referred to as the internal consistency of the test. Any value from 0.8 and higher is good, while a value between 0.6 and 0.8 implies that reliability is regarded as acceptable, but reliability with a Cronbach's alpha value of less than 0.6 is unacceptable (Bryman & Cramer, 2001). Similarly, a value that is greater than 0.9, suggests possible redundancies and that the test length must be shortened. The concept of alpha measures latent factors on the same scale and therefore triggers the items on a scale as revealed by factor analysis (Graham, 2006).

5.5.2.3 Validity

Neuman (1997) defines validity as the extent to which the conceptual and operation definitions match each other, implying that the measure is greatly valid if the fit is better. Similarly, according to Bryman and Cramer (2001), a validity test is meant to determine how far the instrument of measure actually measures the item it is supposed to measure. In developing a new measure, a researcher is supposed to establish that the measure is reflective of the content of the concept. With regards to the concurrent validity of the concept, Bryman and Cramer (2001) suggest that the researcher must use a criterion on which people are known to differ and which is relevant to the concept.

Factor analysis is a statistical technique used for assessing validity and to describe variability among observed variables. In examining whether or not the questions in the questionnaire were actually measuring what they were intended to measure by using a face or content validity test, the pilot study was used. The individual entrepreneurs that took part in the pilot study validated the questions. More details of factor analysis are discussed in Chapter 7.

5.5.2.4 Fieldwork for data collection

The fieldwork for the survey was conducted over four months from 4 February 2016 to 31 May 2016 among DFI-financed entrepreneurs based in the Tshwane Metropolitan District Municipality. Four BCom (honours) students from the University of South Africa were recruited and well trained for data collection with the support of the researcher. The decision to select BCom (honours) students was based on the fact that the students are familiar with the subject, and were believed to be responsible enough to carry out the project.

5.6 DATA ANALYSIS

Data analysis is defined as the systematic process of applying statistical and logical techniques to illustrate, condense and evaluate data (Mouton, 1996) and whereby a researcher inspects, cleans, transforms and models data into distinctive (De Vos, 1998) parts in order to obtain the answers to research questions. The purpose of this section is to demonstrate how the data analysis plan corresponds to the research questions.

5.6.1 Qualitative data analysis

The same day each interview was done, the researcher personally transcribed the recordings using the Atlas Ti 7.5.10 program. This was done while the information was still fresh and the researcher still had all the details pertaining to the interview. To affirm the familiarity of the data before transcribing, the researcher replayed the tape-recorded interviews on the audio device a number of times. The recordings were checked alongside the field notes. To supplement the interviews and to verify some information, follow-up telephonic interviews and emails were conducted with the relevant research subjects.

During this phase of the study, with the help of the Redundant Coding Analyser (RCA) of the Atlas Ti, content analysis was used as the analysis tool. Content analysis refers to a systematic observation and classification of human communication through open-ended and unstructured interviews (van Buuren, 2008). Babbie (2004) goes further to indicate that content analysis is a methodology in social sciences for studying the content of recorded human communication and a coding operation. Coding in essence is the process of transforming raw data into a standardised form. This approach was found to be the most appropriate to analyse the data from this first phase of the study, because according to Nieuwenhuis (2007), content analysis is an approach used to systematically analyse qualitative data such as transcripts, news reports and written documents, which were the instruments of Phase 1 of the study.

The tool is used by the researcher looking and assessing the data from different angles in order to identify keys in the text that will help the researcher to understand and interpret the data; and also looking at similarities and differences in the text helps to corroborate or to disconfirm a theory. Content analysis was used in this study to analyse the recorded transcripts of the interviews with the study participants. Data from this phase of the study was transcribed, coded, categorised and matched to the themes that were pre-determined. Therefore, the analysis of data in this study is limited to the context in which the messages were presented in the interviews. According to Descombe (2007), the process of data interpretation involves four tasks:

- Code the data;
- Categorise these codes;
- Identify themes and relationships among codes and categories;
- Develop concepts and arrive at some generalised statements.

Noting the above-mentioned tasks, in the current study the researcher used the pre-determined themes developed from the literature and research questions. Data was then transcribed verbatim from the open-ended interviews with the research participants. The transcriptions were coded and grouped into the categories and were matched to the themes which were developed from the literature study and research questions.

5.6.2 Quantitative data analysis

In a quantitative inquiry, the questions are very limited with regards to probing and cover a large sample size. As the information per respondent varies; it therefore requires a researcher with special skills such as statistical, summarisation and usage of various models (Bhatnagar, 2012).

During the second phase of the study, the analysis of questionnaires was divided into the following sections:

i) Section A: Demographic information of respondents (demographic questionnaire – DQ);
ii) Section B: Characteristics of small businesses (small business questionnaire – SBQ).
iii) Section C: The perceptions of the entrepreneurs on the DFIs (DFIs questionnaire – DFIsQ); and
iv) Section D: The perceptions of the entrepreneurs on the development finance and growth strategies (development finance and growth strategies questionnaire – DFGSQ)

v) Section E: Propositions of entrepreneurs with regard to development financing for sustainable development of the small business sector using open-ended questions (development finance questionnaire – DFQ).

DQ was developed to gather information on the demographic status of the participants (gender, race, age, education, as well as English proficiency); and SBQ was developed in order to collect information on the understanding of the entrepreneurs' knowledge of small business development strategies. The perceptions of entrepreneurs on the DFIs questionnaire (DFIQ) and development finance and growth strategies questionnaire (DFGSQ) were administered in order to collect information on the perceptions of financed entrepreneurs about the role of the DFIs on business growth against the Phase 1 findings; and development finance and business growth strategies. DFQ was developed to gather the propositions of the entrepreneurs with regard to development finance as deemed possible solutions for sustainable growth and development.

5.6.2.1 Statistical analysis

After the data was processed and coded from the questionnaires onto electronic media, the SPPS program (IBM SPSS Statistics 24 package) was then used to read the raw data into an SPSS dataset for analysis. Data was then cleaned up and validated in SPSS. Different statistical methods were used to analyse the data. Exploratory analysis was done through the use of descriptive statistics and graphs in order to understand the data. Thereafter, the data was ready for statistical analysis. Statistical analysis is often broken into two main categories: descriptive and inferential statistics. Statistical procedures provide accurate information only when data and design meet the rules or assumptions of a specific procedure of a relevant statistical procedure (Bryman & Cramer, 2001). These statistical techniques as used in this study include:

- Descriptive statistical methods;
- Assessment of internal validity of research instrument with the use of factor analysis;
- Assessment of internal reliability of the research instrument using Cronbach Alpha as a technique;

- Assessment of the normal distributions; and
- Exploring the existence of significant differences between identified groups of respondents using independent samples T-Test, ANOVA.

Some of the key elements relating to statistical analyses and techniques will be briefly discussed below.

Descriptive and inferential statistics

Descriptive statistics allows the researcher to describe or summarise data. A descriptive analysis can include the sample size, mean, percentages and a range of scores on the study measures, and for this study, this is presented in the first part of Chapter 7, where the findings of the study are discussed. According to Harris (1995)

Inferential statistics are most important to the statistical analysis of a thesis or article. Inferential statistics allow a researcher to make statistical inferences from which conclusions can be drawn. According to Harris (1995), the inferential statistical focus is on the use of statistical techniques that enable the researcher to draw inferences from a sample which can be either applied or generalised to the population the sample is derived from. Inferential statistics is applicable on condition that the latter has been selected through random sampling method, as was the case in this phase of the study. Inferential statistics have important component parts which are statistical tests. Harris (1995) maintains that in order to decide which statistical test is most appropriate to use, a distinction needs to be drawn between parametric and nonparametric tests.

Variables

Variables are quantities that are measured, controlled or manipulated in research. Variables differ with respect to, for example, the role they are given in the research and the type of measures that can be applied to them.

Variables differ in how well they can be measured or in how much information their measurement scale can provide. Another factor that determines the amount of information that can be provided by a variable is own type of measurement scale as discussed next.

Various scales of measurement

Harris (1995) suggests that the level of measurement relates to the rules used to assign scores and which indicate the kind of information each individual score provides. Variables as used by researchers are classified into nominal, ordinal, interval, ratio and likert scales. Each of these will be briefly discussed below.

(a) Nominal measurement

Nominal variables only allow for qualitative classification and can be measured in terms of whether the individual items belong to some distinctively different categories which cannot be rank-ordered, such as gender that has only the two categories of “male” and “female” which can presented by percentages. According to Shaughnessy and Zechmeister (1997), the nominal measurement is the lowest scale and just places research objects into categories that are mutually exclusive. Dillon, Madden and Firtle (1994) further argue that nominal measurement is the correct measure of central tendency for nominal data.

(b) Ordinal measurement

Ordinal variables allow the researcher to rank-order the items in terms of which item has less and which has more of the quality represented by the variable but does not allow one to say how much more. A typical example of an ordinal variable is a Likert scale (Strongly disagree, disagree, Neutral, agree and strongly agree). Percentages can be calculated for each category.

(c) Interval scales

Interval variables allow the analyst to quantify and compare the size of the differences between the variables. A good example of an interval variable is a person’s height in metres. Interval variables can allow the analyst to do calculations to determine the measures of location or centrality and dispersion, such as mean and standard deviation. Harris (1995) asserts that the most important feature of interval-scaled data is that the gap between two numbers or scores reflects the distance between the values of the characteristic that is being measured. As suggested by Churchill (1995), the aptitude test is an example of an internal measurement which is used to measure intelligence. If a student's performance score on an aptitude test is below 50, the score is considered a ‘fail’; whereas a score between 50 and 80 is considered ‘fair’ while a score above 80 is regarded as ‘good.’

(d) Ratio scales

Ratio variables are similar to interval variables in terms of properties; they also feature an identifiable absolute zero point, thus the ratios allow for a comparison between items; for example, the ratio allows for statements such as ‘x’ is two times more than ‘y’. One can collectively refer to interval or ratio data as continuous data. Bryman and Cramer (2001) state that both interval and ratio variables exhibit the quality that the differences between categories are identical. The two measures are considered as the highest level of measurement as they provide more information than nominal and ordinal scales.

(e) Likert scales

The Likert scale was used as an instrument to measure people’s perceptions about a particular item, for example, in this study the perceptions of the entrepreneurs in Tshwane Metropolitan Municipality as the recipients of financing by the DFIs. Bryman and Cramer (2001) proclaim that Likert scaling is a prevalent approach to the creation of multiple-item measures where research subjects are presented with a number of statements that relate to a common theme. The respondents indicate their level of agreement or disagreement on either a five-point or seven-point array. The Likert scale which also referred to as a summated scale that can be analysed on an item-by item basis, can be summated to include a particular score for individual respondents. The major setback of the Likert scale, as indicated by some researchers, lies with its inability to quantify and to sufficiently explain a single score (Hawkins & Tull, 1994; Zikmund, 1994). Nonetheless, the Likert scale is believed to be the most appropriate measurement of perceptions. The study used the following decoding:

1. Strongly disagree
2. Disagree
3. Neutral
4. Agree
5. Strongly agree

Factor Analysis

Factor analysis is a technique used to reduce data from measurable and observable variables to fewer hidden variables sharing similar or common variances

(Bartholomew, 1980). This technique requires a large sample size as research shows that a sample size that has 100 cases is poor; 200 cases, is fair; 300 cases, is good; 500 cases, is very good; while 1000 cases, is considered excellent (Comrey & Lee, 1992; Tabachnick & Fidell, 2013). This study had 301 valid cases and therefore, is considered to be very good. Factor analysis was used to assess structural validity in the current study. As the distinguishing role, factor analysis was also used in the study to try and eliminate any possibility of inter-correlations between variables when factors were extracted, as the latter themselves took care of inter-correlations; implying that the variables were conditionally independent. Thereafter, the correlation matrix was done during which the factor loadings were analysed to identify which variables loaded into which specific factor since latent variables are believed to be unobservable (Bartholomew *et al.*, 2011).

As suggested by Yong and Pearce (2013), variances were used in the factor analysis in order to produce communalities between variables (where the variance is equivalent to the square of the factor loading). In this case, the commonality was the variance in the observed variables which was counted for by a common factor or variance (Child, 2006). The common factor model (commonality) is therefore the basis for factor analysis.

The factors were then rotated to enable for logical interpretation and to eliminate ambiguity (Child, 1990) which is associated with unrotated factors.

Factor analysis has two commonly used techniques namely: exploratory factor analysis (EFA) and confirmatory factor analysis (CFA). Both techniques are used with the development of measurements, such as the satisfaction scale and customer service questionnaire, as is the case in the current study. Nonetheless, the two differ in application. While the EFA is used to identify the number of latent dimensions, the CFA is used to test the hypothesis or validate the variables. In this study, EFA rather than CFA was used on the grounds that the study did not have prior hypotheses to test or confirm, and therefore, no idea about the number of factors (Rahn, 2012) were anticipated. Although the researcher had an idea of what factors ought to appear, no specific hypotheses were pre-determined. Therefore, the EFA was found to be the most relevant and applicable technique for this section of the study.

Similarly, in order to determine the factors that influenced the variables, an EFA was used. This technical aspect of factor analysis was used to explore the relationship among the variables. Since the researcher had no prior fixed number of factors, the technique therefore helped in determining which factors to retain, through a dimension reduction tool (Bartholomew *et al.*, 2011). EFA allows for examining the relationships between various variables without deciding on the extent to which the results fit a specific model (Bryman & Cramer, 2001) and it also explains the maximum amount of variance (Suhr, 2008).

Exploratory Factor Analysis (EFA)

EFA is a statistical analysis tool that is used to determine factor structure or model, as well as to explain the amount of variance (Suhr, 2008). The variables were inspected individually. Distributions of variables were drawn along with graph production in order to understand the data. Thereafter, the relationships between variables were assessed. The following guidelines were followed in assessing relationships between variables:

- The relationship between two nominal/ordinal variables can be assessed with a cluster Bar chart or table;
- The relationship between a nominal and ordinal variable and continuous variable can be assessed with a Box Plot; and
- The relationship between two continuous variables can be assessed with a Scatter plot.

Unlike CFA which assumes that the researcher has a predetermined number of factors to be encountered and which variables load to the individual factor, EFA depends on the data and the researcher’s interpretation of factors.

Some scholars suggest that in order to perform factor analysis, there has to be univariate and multivariate normality within the data (Child, 2006) with an absence of univariate and multivariate outliers (Field, 2009). On performing the EFA, the Kaiser-Meyer-Olkin and Bartlett's tests were performed as discussed below.

Kaiser-Meyer-Olkin (KMO):

KMO is a measure of sampling adequacy. On the one hand, the values for KMO vary between 0 and 1 with values close to 1 to a minimum of 0.6, being considered good as the value implies that there is a strong correlation structure.

Bartlett's Test of sphericity:

In contrast, the p-value of the Bartlett test (Tabachnick & Fidell, 2007) is considered if the p-value is smaller than 0.05. The Bartlett's test of sphericity tests the null hypothesis that the correlation matrix is an identity matrix. In an identity matrix all diagonal elements are 1 and all elements that are not diagonal are 0 (zero), therefore the null hypothesis is rejected. Both these tests (KMO and Bartlett's) provide the basis for which factor analysis should be conducted (Sidanius, 2017).

In determining the number of factors the following conditions were ensured:

- Eigenvalues needed to be greater than 1;
- The cumulative percentage explained by the factors was greater than 60%; and
- The significant decline of the screen plot.

In EFA, variables are not readily interpretable (Reise *et al.*, 2000) therefore, after the initial extraction, the variables were subjected to the rotation algorithm Varimax in order to maximise a single structure (Thurstone, 1947).

Homogeneity (equality) of variances

Levene's test is used to test whether continuous responses by categories, such as male and female, have equal variances. Equal variances across categories or levels are referred to as homogeneity of variances. The Levene's test can be used to verify the assumption of equal variances while standard deviation is used to inspect the differences.

The T-test

The T-test is used to assess whether there is a statistical difference between the means of the two groups. The strength of the tests is dependent on the size of the sample or the variation in the data. Like all other statistical techniques, independent T-test depends on certain assumptions:

- The data must be normally distributed.
- The variances of the two groups must be homogeneous; implying that the standard deviations calculated from the groups must be in the same order (no significant difference).

Analysis of Variance (ANOVA)

Analysis of variance (ANOVA) is a statistical test that is used to determine if there are differences among the means of two or more independent samples. The One-way ANOVA is used to test for differences among at least three groups, since two groups can be covered by a T-test. Multiple comparison post-hoc tests are used to determine whether a significant difference exists between specific groups. These multiple comparisons tests (post-hoc) are used to determine significant differences for specific comparisons. ANOVA therefore, differs significantly from the t-test. Zikmund (1994) suggests that when independent groups are scaled using interval measurements, it is suitable to use ANOVA. The author further states that ANOVA is commonly referred to as a “one-way” as it is a bivariate statistical test with only one independent variable.

The technique allows researchers to establish if different groups within a sample vary with regard to the independent variable being investigated. If, however, this variance within the group is compared with the variance of the means of the group around the grand mean, it can still be established if the means are significantly different.

The F-test is a statistical tool that is used to identify if there is more variability in the scores obtained for one group compared to the scores of other unrelated sample groups (Bryman & Cramer, 2001). The F-test was used in this study as it uses variance as opposed to standard deviation as the latter cannot be summed, while the former allows for summation. The F-test helps to measure, as Zikmund (1994) asserts, if there is more variability in the scores obtained from one sample group when compared to another sample group. The F-test, was therefore, used in this study to determine if significant differences existed in the perceptions of the entrepreneurs that differed with regards to their race group, level of education and the period of existence of the business, regarding the impact of financing from the DFIs on business growth, development finance and growth strategies, DFIs loan pricing, business performance, business skills, development finance and bridging gap finance gap towards that growth and development of small businesses in South Africa.

The following underlying assumptions of ANOVA were considered:

- Independence of cases, which is a requirement of the design.
- The distribution in each of the groups is normal (using the Shapiro-Wilk test).
- The variance of data in groups should be the same.

Tools that were used to ensure that the assumptions of ANOVA were not violated:

- Normality: with the use of histograms to check overall and for each group and each variable;
- Homogeneity of variance: through use of Levene's test conducted as part of the ANOVA statistical output;
- Sample size: greater than 20 per cell although not essential, is preferred to assist in the robustness to prevent violation of the first two assumptions;
- Scores of one variable or group was not dependent on another variable or group (independent observation)

Pearson's Product Moment Correlation Coefficient

The Pearson's Product Moment Correlation Coefficient is a statistical technique used to measure the intensity or strength of a relationship between two intervals or ratio-scaled variables. This measure of correlation (commonly referred to as Pearson's r), presumes the use of interval variables, and it is illustrated on the scatter diagrams in order to highlight the fundamental features of correlation. Each case on the scatter diagram represents each respondent's position in relation to each of these variables. The magnitude of the correlation 'r' denotes the strength as well as the direction of the relationship that exists between two variables. The values of Pearson's r only reside between -1 and +1. Norusis (2006) states that if all the points fall exactly on a line with a positive slope, the coefficient is 1 (perfect positive linear relationship; and if the all points fall exactly on a line with a negative slope (perfect negative linear relationship), then the correlation coefficient is -1. However, the scholar advises that the absolute value coefficient of 0 (zero) does not necessarily imply that the two variables are not related, instead, the value may mean that the relationship exists in a nonlinear way.

In this study, The Pearson's Product Correlation Coefficient was used to investigate whether a significant relationship exists between development finance, business skills, business performance, growth strategies, DFI loan pricing and access to finance.

The following four assumptions of the Pearson's Product Moment Correlation Coefficient were made, as Harris (1995) suggests:

- Variables were measured on either the interval or scale ratio scales;
- Pearson's r was used to evaluate the extent of the linear relationship between two variables;
- The researcher ensured that the population from which the scores were obtained, was normally distributed; and
- The scores were from the population that had been randomly sampled.

Content analysis

The open-ended questions part of the questionnaire was analysed through thematic and content analysis.

5.7 ETHICAL CONSIDERATIONS

Extra care was taken to ensure that strict ethical rules were adhered to when conducting this study. Researchers are obliged to respect the rights, values and interests of the respondents. Therefore, the relevant financing institutions were telephonically contacted to propose participation in the study for Phase 1 of this study. Upon the respondents' consent to the proposal, appointments for interviews were arranged with the targeted participants. Before any interview began, the aim of the research and the length of the interview were explained to the participants. The purpose of the study was explained to the respondents and confidentiality was guaranteed. The research subjects were informed of their freedom to participate in the study or not, as suggested by Babbie and Mouton (2001). The participants were asked to voluntarily sign consent letters to formalise their participation in the study. During Phase 2, at the beginning of the questionnaires, instructions were given including informing the respondents that they could consent to voluntarily participate in the study.

5.8 TRIANGULATION OF RESULTS

Triangulation is a process of validating the findings from two or more sources. According to Creswell (2014), triangulating different data sources of information entails examining evidence from the sources and using it to build a coherent justification for themes. Establishing the latter is based on covering several sources of data or perspectives from participants, and increases the validation of the study.

5.9 CONCLUSION

Chapter 5 provided an outline of the research objectives and research questions as well as the methodology employed in the study. The chapter explained the choice of research methods applicable to this study. Reasons were provided for the choice of utilising a sequential mixed-methods research approach which existed in consisted of two phases, Phase I and Phase 2, the qualitative and quantitative approaches, respectively. Data sources play a very crucial part of research; therefore, population and data samples were detailed in this chapter along with the research instruments (interviews and questionnaires) as used to gather the desired information for this study. Details were also provided of how the collected data was presented, analysed and interpreted as per the two chapters that follow.

The next chapter present the data of the study. Chapter 6 is based on the data presentation of Phase 1 and Phase 2 of the study.

CHAPTER 6: DATA ANALYSIS AND PRESENTATION

6.1 INTRODUCTION

Chapter 5 discussed the research design and research methodology, which included a description of the research methods used, as well as the data collection tools. This chapter presents a detailed data analysis and interpretation of the data collected in both Phase 1 and Phase 2 of the study. The first part of the chapter presents an analysis of Phase 1 of the study that was based on qualitative research which consisted of in-depth interviews. A computer program, Atlas Ti 7, was used to analyse the qualitative data. The second part of the chapter relates to Phase 2 of the study which was based on quantitative research methods. The quantitative data was subjected to rigorous statistical analysis using the Statistical Package, SPSS, which codes and analyses quantitative data.

6.2 DATA PRESENTATION AND FINDINGS OF PHASE 1

This section deals with the presentation and findings of the results obtained from the respondents that participated in the study, as illustrated in Figure 6.1. The DFIs were represented by only ten institutions, six from the provincial and four from the national level. Despite the researcher's best efforts; there were some targeted respondents that, due to various reasons, did not participate in the study. The Land Bank did not respond to the request and therefore could not participate in the study. The NEF uses a call centre contact system which made it impossible to contact the relevant department; and despite multiple attempts to contact them, including physically approaching the institution, this proved unsuccessful, and therefore they were excluded from the study. Only institutions that responded to the request to participate were accepted to form part of study participants.

Although there are nine provincial institutions that were expected to form part of the study, only six actually participated. The researcher, however, found that saturation was reached after conducting six interviews, as there was no other new information coming out. However, the possibility that this conclusion of saturation might have been over-estimated cannot be ruled out.

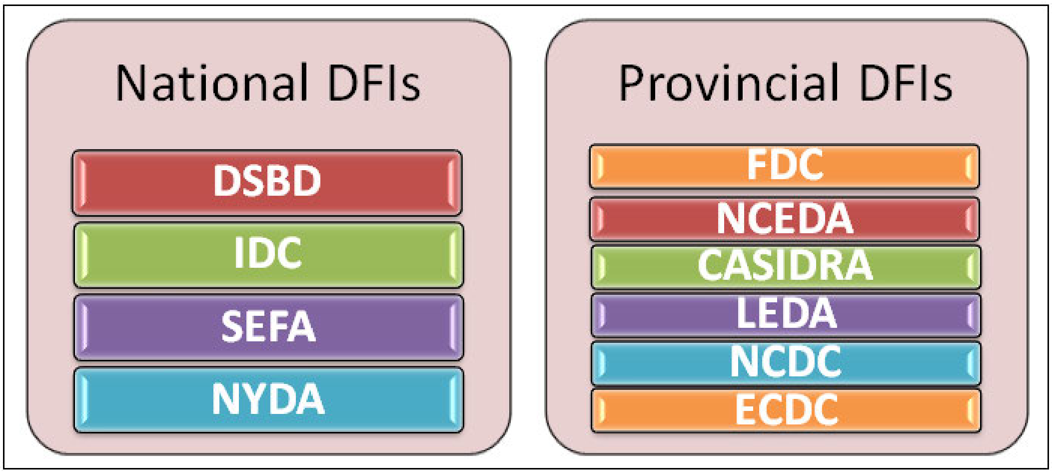
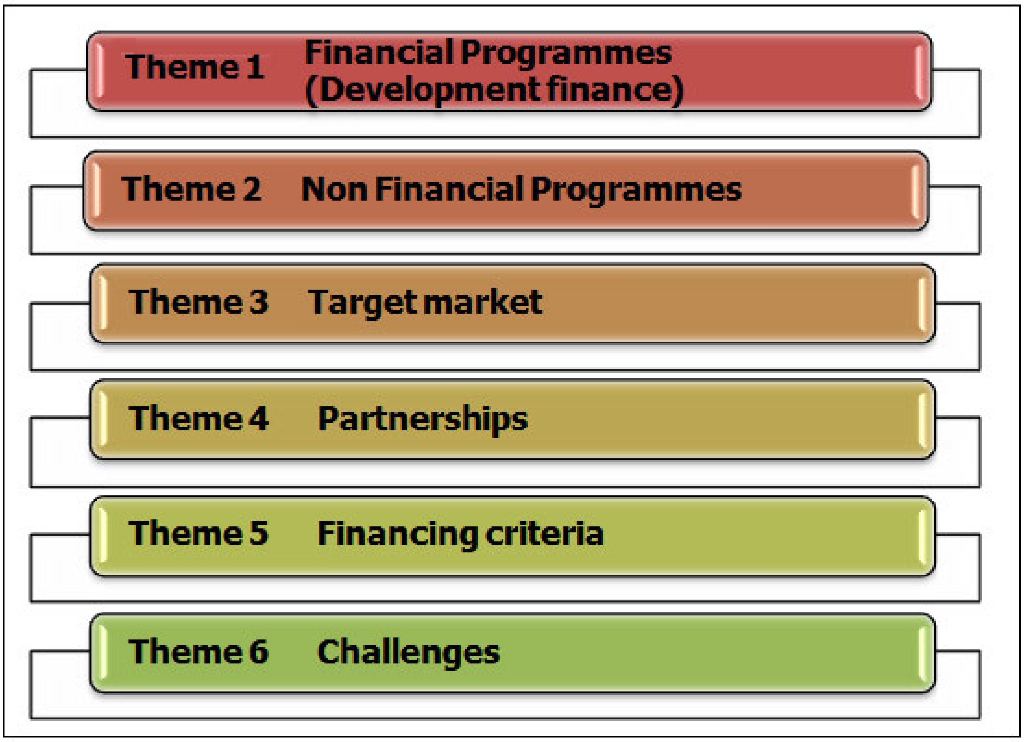


Figure 6.1: DFIs that participated in the study

Source: Author's compilation

6.2.1 Main themes

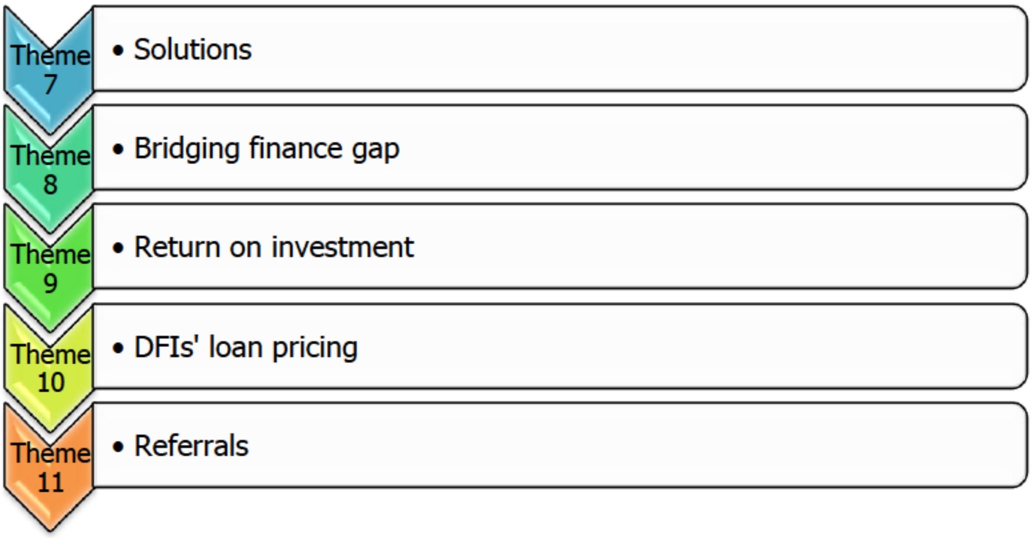
This phase of the study is qualitative of nature, therefore prior coding was used in the analysis of data. Prior coding was used whereby the researcher used the predetermined themes established from the literature review and interview guide. Figure 6.2 illustrates the predetermined themes.



Source: Author's own compilation

Figure 6.2: Pre-determined themes of the study

As the study progressed, new themes emerged from the interviews. These themes are illustrated in Figure 6.3.



Source: Author's compilation

Figure 6.3: Newly emerged themes of the study

Figures 6.2 and 6.3 present the themes that define the model for the role DFIs play in financing small business as the strategic tool for growth and development of the sector. Figure 6.2 presents the predetermined themes of the study, while Figure 6.3 presents the newly emerged themes.

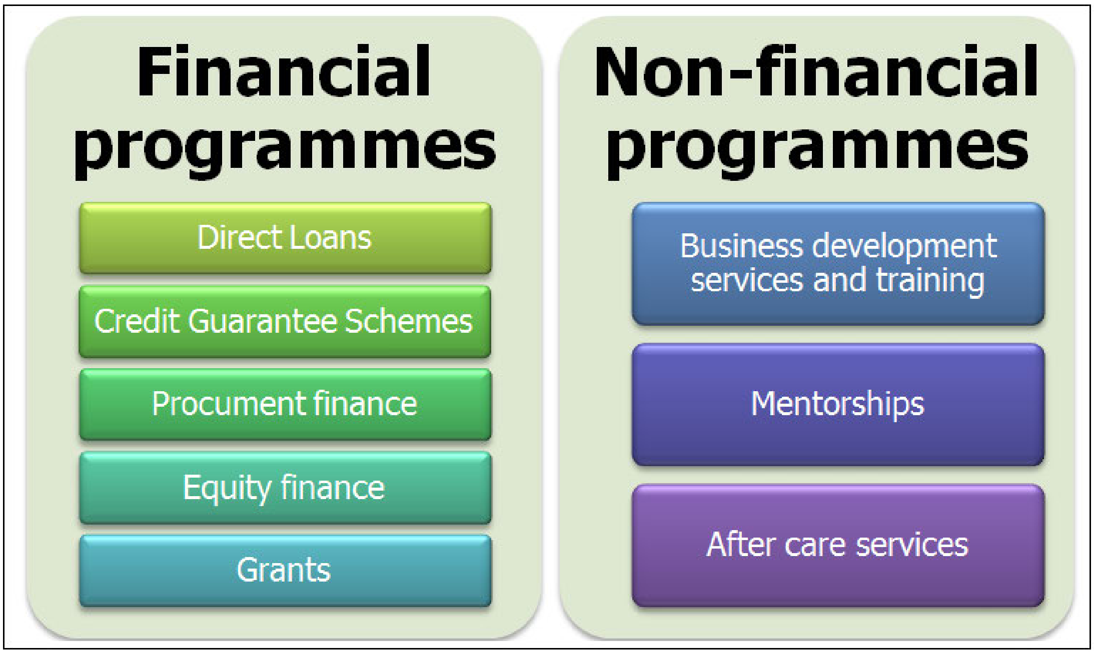
Financial and non-financial programmes (development finance) were placed as number one and two on the theme list, respectively in order to explore the programmes that the DFIs have in financing small businesses. To ascertain that both the financial and non-financial programmes of the DFIs are indeed tailored to serve small businesses, the third theme: 'the target market' was developed. 'Partnerships' was placed as the fourth theme on the list in order to deepen the understanding of the financial programmes that the DFIs have for small businesses. Theme four was supplemented by theme five of 'financing criteria' by the DFIs as the second last predetermined theme. Theme six 'challenges' was the last theme on the predetermined list, and its purpose was to examine the limiting factors that the DFIs experience in financing small businesses.

The five themes shown in Figure 6.3 were new themes that emerged during the interviews. Although these themes emerged as new themes, there was an element of overlap with the predetermined themes. Theme seven 'solutions' emerged as a theme that naturally followed on theme six 'challenges'. The seventh theme emerged from probing on the challenges, and to determine how the challenges were dealt with. The researcher could have predetermined themes eight, nine and ten: 'bridging finance gap'; 'return on investment'; and 'DFIs' loan pricing' (interest charged on loans), however, there was no indication from the literature how the themes could have been predetermined, and therefore they were left to emerge from the interviews. Theme 10: 'DFIs' loan pricing' was purposely left out to emerge from the predetermined themes as the researcher anticipated a different narration from a development perspective. The last newly emerged theme, 'referrals' was discovered as a strategy beyond which the DFI was capacitated to help.

Both the results from the predetermined themes of the study, as well as the newly emerged themes will be discussed in more detail in the next sections.

6.2.2 Development financial and non-financial programmes (development finance)

All ten institutions of the DFIs (100%) indicated that they have programmes available to finance small businesses. Both financial and non-financial programmes are available in support of the growth and development of small businesses. These programmes are illustrated in Figure 6.4 below.



Source: Author's compilation

Figure 6.4: Financial and non-financial programmes by the DFIs

As seen from Figure 6.4, the DFIs offer various development financial programmes that include: direct loans, credit guarantee schemes, procurement finance, equity finance, as well as grants. The IDC is one of the institutions that offer business loans; similarly, SEFA indicated that the institution also offers loans and credit guarantee schemes, while the DSBD stated that their main focus is on grants, and the provincial DFIs offer development finance ranging from loans, procurement finance and equity finance.

The DFIs do not only offer development finance programmes for small businesses as shown in Figure 6.4, but they offer non-financial programmes as well. In order to find out what programmes the DFIs have for small businesses, it was discovered that all ten of the DFIs (100%) have both financial and non-financial programmes. The non-financial programmes, or support programmes as they are commonly referred to, include business development services and training, mentorships, and aftercare services. The NYDA stated that the institution offers business development programmes for young entrepreneurs that approach them for funding: *"… we offer a range of these services…from your business registration, website development and bank account…lack of information is one of those things these people need"*. SEFA also mentioned that after providing development financial support, the institution assigns an employee to monitor the progress and offer any support the business may need (after-care support).

6.2.2.1 Development financial programmes

Table 6.1 provides an illustration of the number of the DFIs that have development financing programmes designed exclusively for small businesses; these programmes are aspects of development finance that are meant to support and help small businesses grow.

Table 6.1: DFIs with development financial and non-financial/support programmes

Programme	No. of DFIs	%
Development financing specifically for SMMEs	4	40
No special financing for SMMEs	6	60
Total	10	100

Source: Author's compilation

The results in Table 6.1 show that only four of the ten institutions (40%) have development financial programmes that are intended specifically for small businesses, while six or 60% of the DFIs do not have specific programmes for small businesses, but businesses in general, regardless of size, however, the findings revealed that their programmes are more biased towards small businesses than large businesses. All ten DFIs (100%) indicated that they have non-financial programmes which are available for the support of small businesses.

One of the national DFIs, the IDC, mentioned that the institution does not have financing that is tailored exclusively for small businesses. The respondent indicated that all businesses, both large and small businesses that meet the IDC financing criteria are eligible *"…there is no specialised product for small businesses per se but we fund entrepreneurs who seek financing that amounts from one million rand, just any other businesses…yes that is our minimum amount"*. The IDC agreed that their financing programmes are aligned to the NDP. From the provincial DFIs, one institution (NCEDA) stated that the DFI's funding is heavily centred towards developmental projects that are aimed at uplifting the community, more than small business funding. On record, the respondent said: *"…with the collaboration with IDC in 2006 until, the mandate was identification of investment projects to ensure economic activities in the province in order to address the challenges, of triple challenges of unemployment, poverty and inequality …"*.

Financial programmes issued by the DFIs include start-ups; business expansion finance; procurement; and grants. The former three types of financing are in the form of loans. The latter is in the form of an asset and credit guarantee scheme. The figure below illustrates the spread of financial programmes offered by the DFIs.

Source: Author's own compilation

Figure 6.5: Development financial programmes offered by the DFIs

Development financial programmes offered by the DFIs include loans, grants, credit guarantee schemes, and procurement finance as discussed below.

a) Loans and asset and equity finance

The DFIs offer finance for start-ups that would not necessarily be able to get financing from banks. LEDA, for example, said: "*Our funding is different from banks; it caters for people that are* ***un-bankable*** *…"* referring to people who did not have a regular income, who did not have a bank account that indicates a regular flow of income. This forms part of the loan, as LEDA stated that unlike other types of loans where the DFI supports the business through a third party, the amount is deposited straight into the business account to be utilised as **working capital**. *"…This amount makes about at the most 20 or 30% of the loan amount required … we cannot inject lots of cash for working capital …people have tendency of misusing funds…".*

Two institutions (FDC and LEDA) categorically stated that they offer asset finance. These are loans that are meant for the purchases of assets such as equipment and machinery. For example, LEDA stated that the institution provided at least 14 asset loans at an average of R1.5 million per year during the period 2012/2013. The FDC also affirmed that the development finance portfolio of the institution includes asset finance and further stated that: *"…the institution takes up to 65% of equity on the asset*, *and the client is only liable to service only 35% of the asset finance…once the principal amount has been settled, FDC exits*…"

The DFIs stated that financing is categorised according to the following different stages of the businesses:

- Start-up for the introductory stages of the business cycle (0-2 years);
- Expansion of existing businesses (including franchise finance, equity and buy-out finance) for the growth stage of the business cycle (>2 years);
- Concessions during either the early or growth stage of the business cycle, depending on the need.

(b) Procurement or Concession finance

The DFIs expressed that they offer procurement finance or concession finance to help bridge the financial challenges that arise after the businesses is awarded a tender to provide a service: "…*this is the type of finance where the financing institutions assist small businesses to be able to provide a service to the government with a pledge to recover cover costs immediately when payment is made*…". Upon receiving a business deal or a tender from government an entrepreneur approaches a financing institution to pledge for financial support to enable the entrepreneur to complete the project. Six of the ten DFIs (60%): FDC, CASIDRA, SEFA, LEDA, ECDC and NYDA were institutions that had indicated that they had this particular programme for small business. SEFA claimed: "*…we support government contracts for the suppliers... the government will actually provide us with the leads to the suppliers and we would finance the suppliers."* The other three (30%) of the DFIs (IDC, NCEDA and DTI) did not mention if they offered concessions or procurement finance.

(c) Credit Guarantee Schemes

Only one DFI is providing a credit guarantee scheme and it is not given directly to the entrepreneurs: *"…we are not selling this product to the end-user, we wholesale it through the banks by way of crediting them by indemnifying the loan to the bank…"* SEFA stated that the facility of the credit guarantee scheme still exists within the institution, however, the facility is not very operational due to the challenge of capital requirement by banking regulations: *"…the entrepreneur can approach the bank for finance and if after the assessment by the bank it appears that the client meets all the lending requirements but lacks collateral or security, and then SEFA offers to fill that gap by providing the* ***credit guarantee scheme.*** *However we are shifting away from (it) because the product is not very successful due to Basel III…this programme was inherited from the then Khula Ltd., but had not earned the much desired results…"* The credit guarantee scheme (see Section 2.2.13) was an indemnity against the loan should the recipient of the loan fail to pay back the loan. SEFA usually pledged to pay 80% of the loan amount. *"…but you see this thing of capital requirements …now it should be 100%, not 80% as it used be during the Basel II…"* This is regarding the bank risk exposure which used to be at the ratio of 20:80 for the bank. The new regulation requires a 100% pledge. *"…no, no, the interest is still the same, you see that it another problem with the facility…"*

(d) Equity finance

The FDC stated that *"…in the event that small business requires an asset but cannot afford to finance it, FDC can come on an agreed terms, usually at 65% sharing. FDC purchases the asset and holds 65% ownership of the asset until full payment has been done…"*. In the case where the entrepreneur defaults, FDC repossesses the asset and the client is only liable for 35% of the cost of the asset, instead of the whole 100%. Should the entrepreneur manage to settle the whole amount, the asset becomes the entrepreneur's property and the FDC pulls out.

This strategy helps entrepreneurs to gain assets for their businesses, one of the predicaments identified that limits access to finance for small businesses.

(e) Franchise

This form of financing is provided to the business that wants to buy a stake of an existing business. The franchisor or the mother company (usually a foreign or multinational business) is responsible for all marketing and operations of the business and provides the training and mentorships. This form of financing is mostly available at provincial DFIs such as FDC and LEDA.

(f) Grants

The three DFIs: DSBD, NYDA and NCEDA do offer grants to their clients. NCEDA stated that the financial support they provide to projects is not intended to uplift the community. The DTI also mentioned that they provide finance for fixed assets like machinery and equipment: *"...the department provides grants to a maximum of R800 000 for equipment, machinery and tools, and up to R200 000 for business development and training. That can be in matters such as corporate governance, management, marketing ..."*

6.2.2.2 Non-financial/support programmes

Table 6.3 shows that all ten DFIs (100%) indicated that they provide support services to their clients.

Table 6.2: Non-financial programmes offered to SMMEs by DFIs

Non-financial programmes	Yes	%	No	%	Total %
Mentorship	SEFA, NYDA,	20	FDC,IDC LEDA, ECDC, CASIDRA, NCEDA, DTI	80	100
Training	SEFA, NYDA, IDC	60	FDC, LEDA, ECDC, CASIDRA, NCEDA, DTI	70	100
Marketing and website development	NYDA	10	FDC, LEDA, ECDC, CASIDRA, NCEDA, DTI, SEFA, IDC, DTI	90	100
Business formalisation	ALL DFIs	100			100
Business Plan	All DFIs	100			100

Source: Author's own compilation

The IDC had indicated that: *"We facilitate external learning and development by arranging applicable courses for potential clients and even for non-potential clients".* NYDA also had shown that they had realised that their clients (young people aged 18-35), do not only require financial support, but other support mechanisms as well, and therefore they (NYDA) provide mechanisms such as website development and legal advice: *"If a young person comes and says I am having a business and I need a website for my business, we get a consultant who is going to assist you and organise a website for you… If you are looking for a legal advice, we get you a lawyer…bill boards, business cards…"* NYDA insisted that their mandate was to help their clients in every way to make sure that their businesses grow. SEFA also demonstrated that they provide capacity building for the co-operative and they offer basic financial management training to the co-operative manager.

SEFA mentioned that they offer pre-loan and post-loan mentoring for SMMEs, depending on the individual needs: *"We specialise in mentorships… we are providing advice to a client as far as what products can be suitable for their needs and we also make sure that if they have an idea, we refer them to the right agencies or financial institutions. But if there is a gap… we have got mentors, accredited mentors that operate for SEFA… accredited with the Institute of Business Advices…"* SEFA further pointed out that on contracting a mentor they (SEFA) make sure that their client and the mentor sign the terms of reference and service level agreement to the satisfaction of the client. Two (FDC and NCEDA) of the ten DFIs indicated that they referred the clients to other institutions such as the Small Enterprise Development Agency (SEDA) which is a non-financial DTI institution for any developmental need other than finance. NCEDA stated that although they do not offer any direct support to SMMEs, they may refer them to the relevant institutions that provide the required services, including SEFA and SEDA, *"…although we work exclusively with projects, we do provide small businesses with information and make referrals to relevant institutions that can offer the services our SMMEs require…"*

All ten of the DFIs (100%) that participated in the study agreed that they strive to convert small businesses from being informal businesses to becoming formal businesses, as well as helping businesses to build relationships with banks. LEDA, for example, mentioned that one of the conditions for a finance application is that the business must have a bank account to which funds will be channelled, *"…funds are deposited into a business account not a personal account…a proof of a cancelled cheque in business name is one of the requirements…"*; while ECDC stated that the business must provide a copy of a tax clearance certificate as well as proof of registration *"…even if the business is not registered, we encourage them to register their businesses and must provide a tax clearance certificate…".*

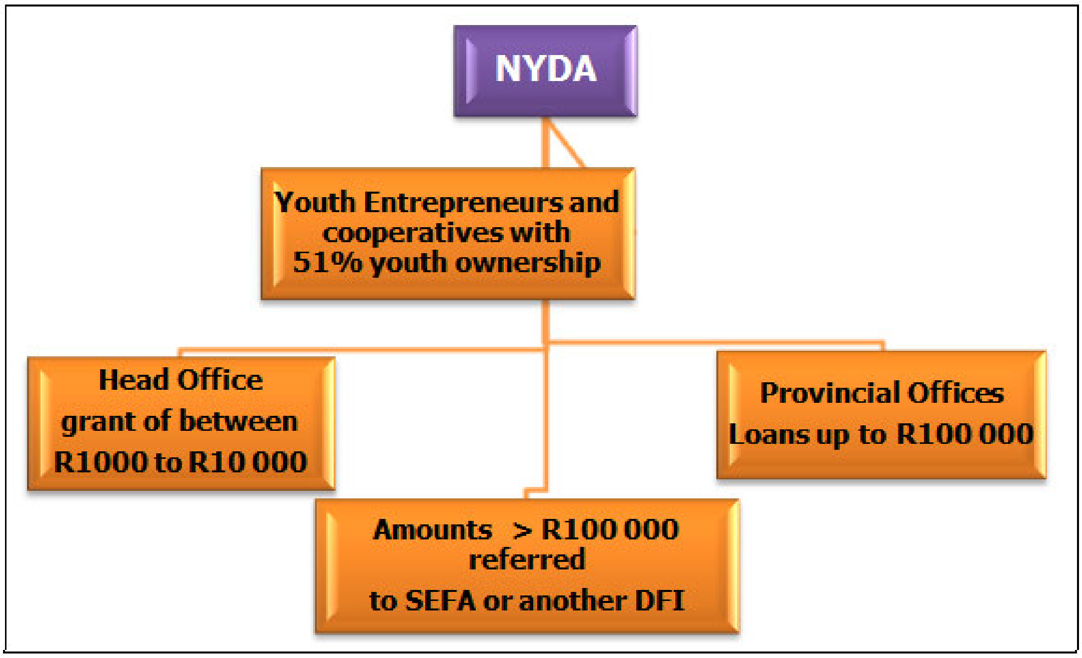
The DFIs have all stated that a business plan is a very important tool that helps to identify the growth plans for the business. Although business planning is a challenge for the entrepreneurs, the DFIs stated that either they (the DFIs) offer in-service business planning or they refer to the entrepreneurs to other institutions like SEDA to assist. The business plan then is used by the DFIs to decide on the type of financing that is required and also to determine the type of additional support necessary for business growth.

6.2.3 Target markets

The DFIs have their differentiated target markets within the SMME sector. These markets that are served by DFIs would possibly not be served by the banks because they do not meet the bank's lending criteria. Each institution has its own specific mandate pertaining to their exclusive products. This section is therefore based on those markets together with the loan limits as explained by various DFIs. The Provincial DFIs seem to have a more or less similar approach with regard to their target market, with the exception of NCEDA that works with a range of projects and not just small businesses. The standard target market for the provincial DFIs therefore includes more or less:

- South African owned company
- 51% black-owned
- Registered with Company and Intellectual Property Commission
- Has tax clearance certificate
- Operates within the borders of the province
- Be BEE compliant

This section also highlights some specific exclusions to the national DFIs' target markets as illustrated in the figures following below and on the next few pages.

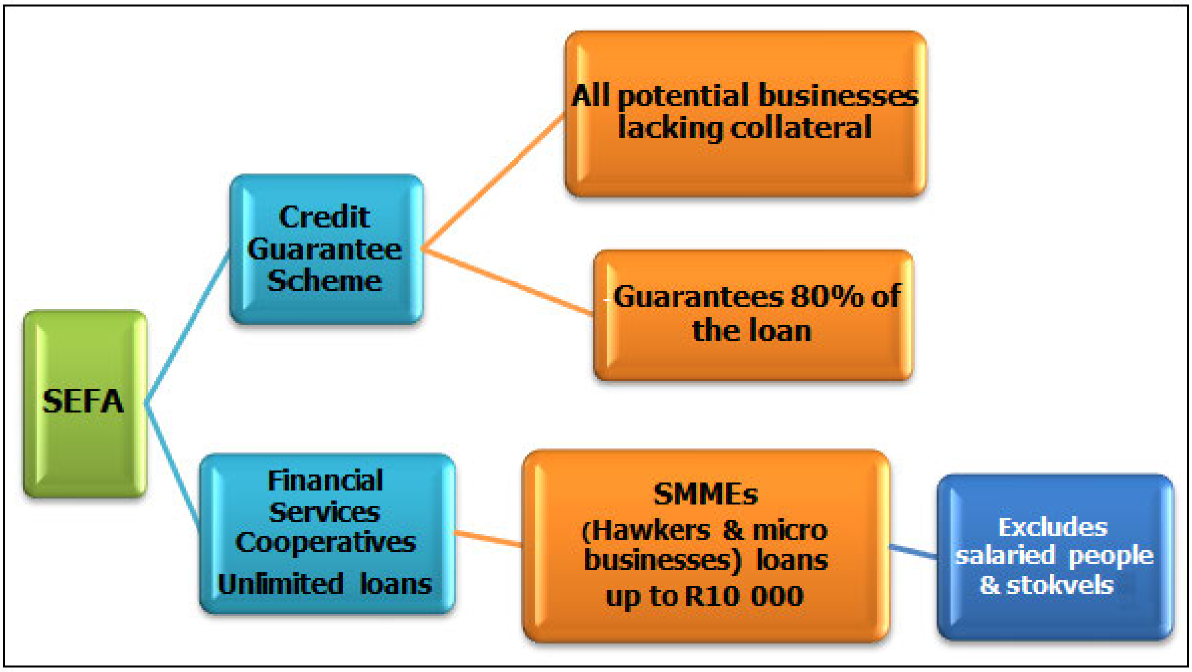


Source: Author's own compilation

Figure 6.6: NYDA's target market

Figure 6.6 is an illustration of NYDA's target market which is young people and entrepreneurs (18-35 years) and co-operatives that have young people owning the minimum of 51% shares to enable skills transfer to the youth of SA. NYDA offers loans up to R100 000 from the provincial offices. while loans exceeding R100 000 are handled at the institution's head office in Midrand. *"…Young entrepreneurs can make their applications at the provincial offices for assessment. When all the requirements* *have been met, the applications are submitted to head office for finalisation…"*. This implies that the provincial offices do not make the final decision on whether the application is successful or not. All the decisions are made at the head office for consistency and control.

Figure 6.7 provides a summary of the lending programmes provided by SEFA.



Source: Author's own compilation

Figure 6.7: SEFA's target market and lending programmes

SEFA states that wholesale lending has proven more successful than direct lending. *"…intermediaries reach out to a broader market than direct lending because the RFIs are spread across the country…they are well placed, capacitated and have an established market…"*

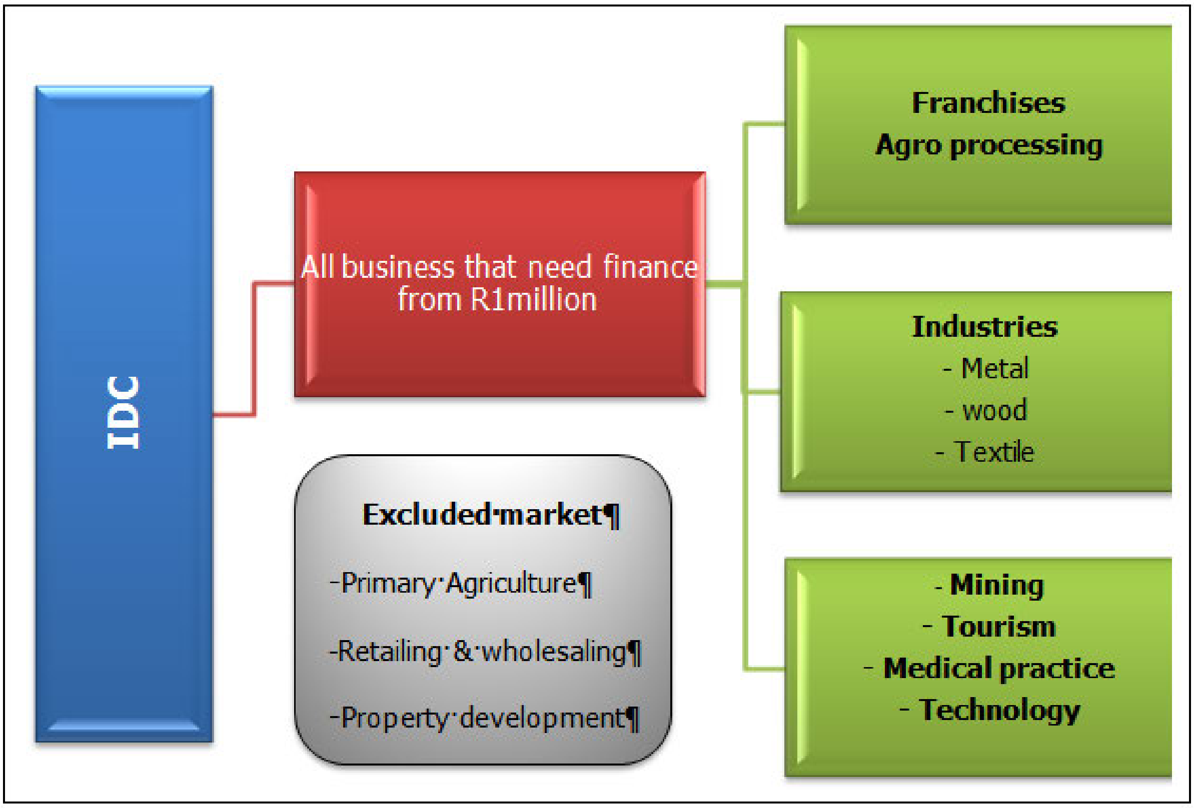
- The developmental mandate includes not only employment creation but to alleviate poverty and reduce inequality. Although wholesale lending does not directly impact on employment, people's livelihoods are positively affected.
- The industries in which small businesses operate are already saturated, and unless entrepreneurs become innovative, the exploration and development of new markets become difficult. Usually small businesses fail to deliver to new markets and old markets get compromised and ultimately the business fails.

Figure 6.7 shows that all businesses seeking finance but that do not have collateral can approach the Credit Guarantee Scheme (formerly Khula) which is available to fill the collateral gap. Khula, however, offered only 80% of the required loan amount. The entrepreneur was then liable to pay the other 20% to provide 100% security against the loan. The 20% can be in a form of an asset or cash. SEFA believes that there should be some level of commitment by the client to make their own contribution as well. Nonetheless, this is a big challenge for a good business opportunity that cannot afford the 20% contribution. SEFA also states that another challenge with the credit guarantee scheme is the new Basel III which states that the hedge must now be 100% as opposed to the Basel II which allowed for 20:80 risk sharing: "…*SEFA is bound by the pillars of Basel III which expects 100% capital requirements…*"

This new rule means that the financial instrument which was already almost insignificant; now only exists in theory. Ultimately, the use of the instrument can no more be considered as an option to address the financing gap, with the exception of recipients who benefited before the implementation of the Basel III.

The other challenge that relates to the use of a credit guarantee scheme is that although the scheme is meant to reduce the price of the loans due to the liquidity of the instrument, the prices of the loans remain significantly high: "…*one will never know if there is manipulation of …but the interest charged on the loan covered by the credit guarantee scheme remains high…the client bears the burden…*"

Figure 6.8 represents IDC's target market which includes all the industrial sectors of small businesses that need financing from a minimum of R1 million. IDC have decided to make R1million their minimum loan amount because it is so expensive to approve a facility which is said to cost the IDC about R250 000,00: "…*at one stage we costed our process and we said, look it's costing us about R250 000,00 just to approve a facility. So just to break even on that, we must at least provide larger amounts than R250 000,00. So a few years ago we decided on a minimum of R1 million. So, yes that we can at least cover our costs and our efforts to grant that facility*…" The businesses funded by IDC were franchises, agro-processing, mining, tourism, professional practices such as medical practices, and lastly industries in metal, wood and textiles. IDC, unfortunately, do not finance the primary agriculture, retailing, wholesaling and property development sectors because these markets are serviced by commercial banks and the Land Bank.



Source: Author's own compilation

Figure 6.8: IDC target market

DSBD's target market includes all businesses that seek loans to buy machinery with the value of higher than R1 million. The Black Business Supplier Development Programme of the DSBD is an incentive programme aimed at black-owned enterprises that have the potential to be competitive in providing goods and services to the general public, and the public sector of private sector corporations on a sustainable basis and in so doing increase employment.

6.2.4 Partnerships

In their efforts towards financing SMMEs, the DFIs have developed some strategic partnerships with other institutions to mobilise their lending programmes. The decision-making on who to lend to and pricing was one of the crucial issues in the partnerships. For example, NCEDA stated that the institution does not offer financing to small businesses but works through a partnership with the IDC, so that small businesses in the Northern Cape are able to get support through a strategic partnership between the two DFIs.

The FDC had partnerships with some banks and NYDA. In its partnership with one of the banks, the FDC took over all the clients that the bank considered to be un-bankable. The FDC would use its lending criteria, including 65% equity where collateral was not available, to assist the client. Upon approval, FDC passed all the documents to the bank to make its own assessments. It is important to note that final financing decision rests with the partnering bank and not the FDC. FDC also had strategic partnership with NYDA where the two institutions each contribute 50% towards assisting their youth clients. The fund was managed by FDC; NYDA only referred applicants that approached them to the FDC.

Regarding credit guarantee schemes, SEFA is working in partnership with the banks, where SEFA provides the guarantee to the relevant bank where the client has applied for finance. The bank has decision-making power regarding the whole process of loan assessment and pricing, SEFA's contribution is in with regards to issuing the guarantee.

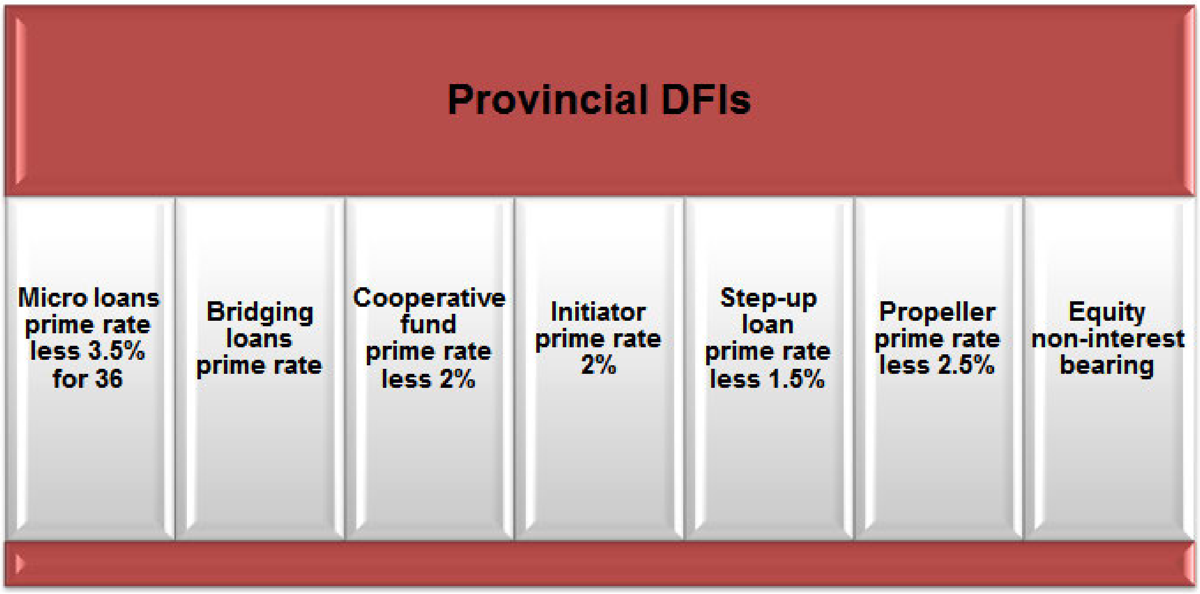
6.2.5 Funding criteria

The results reveal that the DFIs have their different financing criteria, which depends mostly on what each financial product/programme is intended to achieve. With the provincial DFIs, the criteria differ across the various types of financing.

NYDA has taken over the loan book of the UYF and continues with the existing clients where the DFI prefers a constitution for **group lending: "***Young people group themselves 5-10 each with their different individual businesses…give their group a constitution and a name to own the account at bank or post office…they apply for individual loans and they sign the security for each other in the group… the group will be a sort of security…".* NYDA further requested a saving of at least 10% of the requested amount (up to R10 000) from the group to encourage them to develop a culture of saving. As for the other loans, NYDA uses assets that the client puts on the table, or it (NYDA) took equity in the business for loans between R100 000 up to 5 million rand. Signing of surety is one of NYDA's requirements, while existing assets catered for collateral or NYDA took equity in the business: "… *collateral to us does not determine business success, the capacity of the entrepreneur and cash flow are the key issues… and for other types of businesses like tuck-shops, we do not require business plans".* NYDA further stated that with the new establishment and arrangement with SEFA and IDC, the DFI mostly provides grants ranging from R1 000 to R10 000, while larger amounts are provided as loans and referred to either SEFA or IDC, depending on the amount required.

6.2.6 DFIs loan pricing

The DFIs at provincial level, wherever possible, use equity finance where: *"…the business is liable to service only about 35% of the loan at the discounted rate, the 65% is held as equity by FDC…"*. This finding implies that the business will only pay discounted interest on 35% of the principal loan, and once the business has paid the principal, the business is in the position to wholly own the asset.

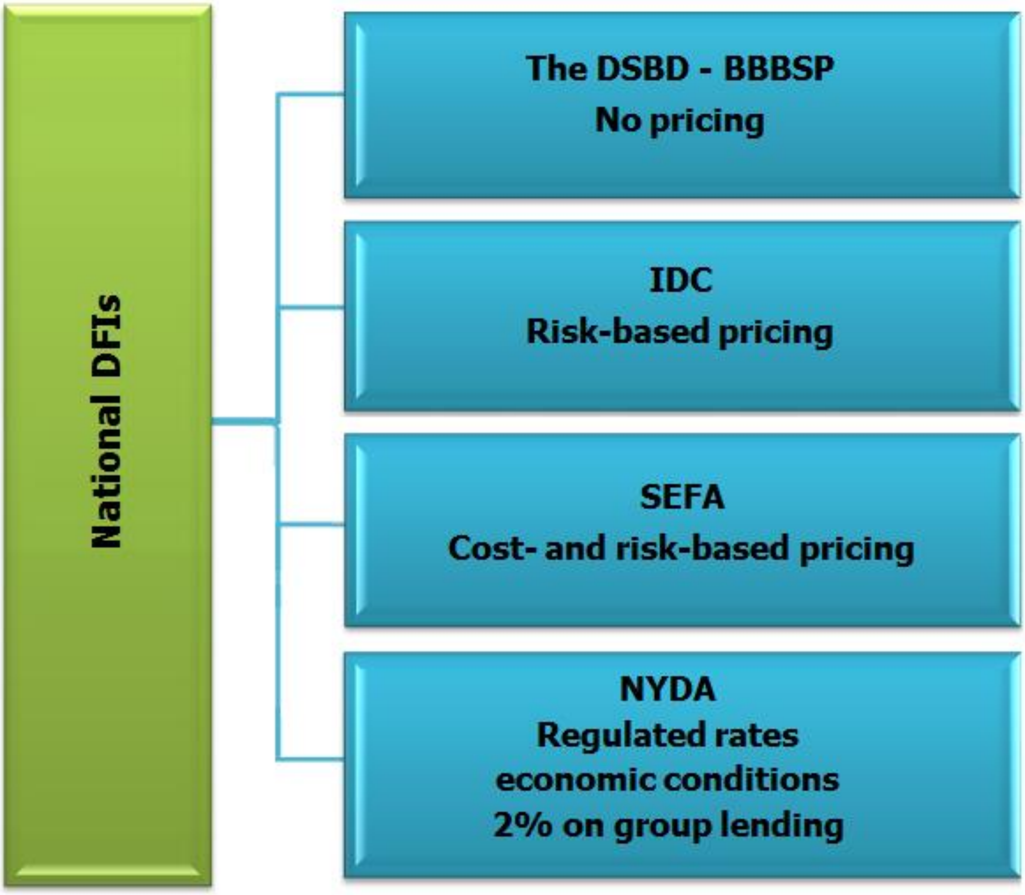


Source: Author's own compilation

Figure 6.9: Provincial DFIs pricing model

Provincial DFI that offers loans have different pricing structures for different types of loans as shown in Figure 6.9. However, the interest rates charged by the DFIs are prime-based less a certain percentage (ranging between 2% and 3.5%). In the cases where the DFI offers equity financing, the portion held by the DFI has no interest-bearing until the business settles the capital amount. The findings show that the DFIs use the prime rate pricing strategy and the prices never exceed the prime rate.

As illustrated in Figure 6.10, the national DFIs have a different pricing approach because they offer different financing, as opposed to the provincial DFIs which provide more or less similar financial products, although variations still exist depending on the individual provincial needs.



Source: Author's own compilation

Figure 6.10: National DFIs' various pricing plans

The DSBD does not have any pricing because the institution offers grants not loans. NYDA's pricing model incorporates risk-based pricing, the regulation (prime less x), economic growth, credit checks: *"…we take it in line with regulations, NCA regulations, these regulations guide us… we just take general economic growth… when the recession started, we dropped the interest rates by 2%... we drop it when we see young people are struggling to…for loans above R10 000 we charge 1.42% a month, so if you pay that loan in three months somewhere, you pay… 4 point something percent..."*. The results might mean that NYDA's pricing depends more on the regulation and market forces.

The IDC stated that their pricing strategies are risk-based but are aligned to the National Growth Plan: *"…At IDC we relax the burden of repayments during the first or second year of the loan until the business begins to make money …we use moratorium where interest is not paid on the capital…"* IDC reported that they use risk-based pricing. In addition, IDC also include the level of empowerment (where skills were transferred to previously disadvantaged communities/population) and the economic merit of the business as illustrated by the owner's projections. Seemingly, IDC's pricing model was determined by the business risk as banks do and level of empowerment within the business (BEE). Similarly, SEFA uses both risk-based and cost-based pricing in issuing its loans: *"…for wholesale loans, cost-based pricing is used otherwise we use risk-based approach…".* Another respondent from SEFA agrees that SEFA loans are higher because they are serving a very risky market: *"…banks offer cheaper loans, but you see, we have to make up for the risk factor of the client…"*

6.2.7 Challenges

The financing institutions indicated that they were faced with some problems in their attempts to assist small business to access finance. It was therefore crucial to highlight the problems that these financing institutions believed to be the stumbling blocks towards SMMEs funding. The problems were:

- Limited budgets,
- Misuse of credit guarantee schemes,
- Turnaround period,
- Ineffective products and low number of applications
- Credibility of clients,
- Unethical behaviour of some DFI personnel,
- Poor marketing and
- Regulation

The challenges presented by the problems experienced by DFIs will be briefly discussed in the section below.

(a) Limited budgets

One of the identified challenges encountered by the DFIs in financing small businesses is limited budgets. For example, NYDA confirms: *"We would like to reach out to as many young entrepreneurs as possible in a given year, but we are working the budget of, say this financial year, we only have Rxxx… That is so little, the demand exceeds that by at least three times…*" This might be due to the limitations of the proposed budget at the beginning of the year, or based on the performance of the previous year.

(b) Misuse of credit guarantee schemes by strategic partners

SEFA, through the former Khula's credit guarantee scheme, is the only institution that offers this type of facility, and hence the only DFI with the problem. The DFI has strategic partnerships with some banks through the use of the credit guarantee facility. However, the institution does not have any influence over the issuing and pricing of the loans, as the banks are the sole decision-makers, but in the case of default, the DFI is liable to pay: "…*should the client default …banks will recall that security of Khula…black SMMEs are still not being able to access this facility...I am sitting with a portfolio of 100% whites. So you see…"* SEFA further claimed that the interest rate charged to the clients remains the same regardless of the availability of the indemnity which should reduce the risk profile, as it is more liquid: "…*do not charge more than prime because we give you a guarantee that is soft money. So the security is more liquid that what you could… but banks want to charge prime plus…"*

The challenge might be caused by the institutions that work as partners, although the decision to finance lies with one partner and the other partner does not participate in decision-making during the loan application. The fact that there are only white people as the institution's existing recipients of the facility implies that the intended development support does not meet its mandate of serving the previously marginalised communities. The respondent was unable to provide information on the gender and age distribution of the recipients which could help in drawing a conclusive picture of the demographics of the facility beneficiaries (gender and age variables). These two variables form part of the criteria for inclusion in determining the marginalised community (youth and women).

(c) Turnaround period

The centralisation of business units or departments within the institutions made their processes lengthy. An IDC respondent, for example, blamed the centralisation of the institution for the delay in the processes. Nonetheless, the respondent claimed that it was due to the requirements of the corporate governance: "…*every approval is done at the head office: which makes the process a bit longer, more cumbersome…"* FDC, LEDA and ECDC also mentioned that decisions rest with investment committees of the DFIs that meet at certain times, implying therefore that even if the entrepreneur anticipated a certain turnaround period, the delay caused through the processes may affect the targets the entrepreneur had. While the centralisation of business units of the DFIs ensures good governance, the practice prolongs and prevents subjective decisions that could benefit small businesses.

In addition to the problem of the prolonged funding process, another challenge is the lack of relevant skills by the entrepreneurs relative to the success of the business. A respondent from NYDA affirms that the majority of young entrepreneurs lack the requisite business skills required by their business ventures, so the institution has to provide some training before any funding can be made, this in turn affects the anticipated turnaround period of the application /financing process.

(d) Ineffective/ non-performing products and low number of applicants

The institutions do not get as much benefit from some products as they expected. For example, a respondent from LEDA stated that working capital loans reflect higher risk of non-collection: *"…in the scarce resource environment, the institution faces the risk of non-payment from the borrowers… The institution opts to focus more on performing loans such as bridging/procurement financing where there is a high prospect of repayment…"* The respondent further reported that no applications have been made for franchises during the period 2013-2014.

Another challenge that affects DFIs in financing small businesses is the low number of applications. DSBD was concerned that there were not as many applicants approaching the department as the**y** anticipated. The DBSD stated that small businesses are not making use of the support that is available to develop black entrepreneurs; this is the facility that can enhance competitiveness and reduce unemployment.

This problem may be blamed on a lack of appropriate marketing or awareness and outreach campaigns and initiatives by the institution.

(e) Dishonesty and repayment defaults

One of the challenges identified by the DFIs relates to the dishonesty of clients. Some DFIs stated that sometimes the clients do not provide the entire truth about the state of their businesses. For example, SEFA stated that the financing decisions are made based mostly on information provided in the business plan. However, the DFI still do their own assessment of the business and insists that the client is expected to inform the institution about any development that may arise or occur on the business, outside what is shared among the two parties, that can potentially have a negative effect on the repayment of the loan **(loan repayment defaults)**: *"…some of these people will not notify us… what do we do? We will try to help but in the end, we have to take legal action…"* The DFI assumes that at times the problem lies with people who help to compile the business plans (contracted service providers): *"…some of them are not entirely honest, they portray a different picture from the reality…"* The DFI further stated that based on dishonesty and default, clients at times end up facing legal actions which may end up in the loss of personal property, such as houses. The FDC and IDC shared the same sentiment that in extreme cases, people end up losing their property. The FDC stated that this action is usually considered as a last resort after all other efforts to resolve the matter have been exhausted.

(f) Unethical behaviour of some of the DFIs personnel

Some DFIs reported that some personnel within the institutions commit unethical behaviours that affect the institutions' agenda to effectively render services to the clients. A respondent, who wanted to keep the identity of the institution confidential regarding this matter, stated that there people within the institution who are unethical and practise corruption: *"…some applicants raise concerns of unethical behaviour or treatment by some people here…some senior people within the institution will want to force the decisions to benefit some clients that would not necessarily be financed in principle…"* However, the respondent has stated that there are mechanisms in place to control such practices if reported accordingly.

(g) Poor marketing

One of the dilemmas facing the DFIs in assisting small businesses is reach-out programmes. The DFIs have mentioned that some of their products do not receive any applications, for example, LEDA stated that some of their products are not utilised: *"…no applications were received for franchise loans, we are planning to intensify our marketing strategy to attract businesses…"* Considering that the issue of access to finance is among problems reported by small businesses, the fact that some products that are tailored to address the financing needs of SMMEs are not utilised indicates that people are not aware of such programmes. This can be related to the problem of marketing by the DFIs.

(h) Regulations

Legislation plays an important role in financial services, but it may also disadvantage parties in the lending contract. Financial institutions operate through a framework of regulation and institutional policies. One respondent indicated that legislation was, to some extent, responsible for the way financial institutions behaved towards the issuing of credit which, he acknowledged was disadvantaging SMMEs: *"…banks, for example, have their shareholders that they've got to satisfy. So they can't just do reckless lending…NCA has made it a lot tougher for people to access finance for small businesses".* Another respondent also confirmed that while the NCR was protecting both the client and the institution, it may be very difficult for entrepreneurs that do not qualify according to the NCR regulations to access funding. FDC stated that it was their policy to hand over non-payment accounts to their legal departments which made people reluctant to approach them in case everything did not go according to plan. All the respondents from the DFIs have indicated that they operated within the parameters of their institutional policies, which set who and how to finance. The DFIs stipulated that they were given the mandate by government and they follow individual institutional regulation and policies, however, the DFIs acknowledged that the NCR regulates their operations just like any other financial institutions. It was observed that legislation might be too rigid towards SMME lending.

Regulations that relate to financial institutions seem to be another challenge facing the DFIs in financing small businesses. The DFIs have to abide by the Credit Regulation Act that prescribes the terms of reference for the DFIs, which at times, have shortcomings to assisting small businesses. A SEFA respondent claimed that due to BASEL III regulations the use of credit guarantee schemes: "…*does not yield much of the desired result…"*

(i) High loan prices

Some DFIs (SEFA and IDC) offer loans at higher prices than bank loans. IDC, for example, appreciates that their loans are priced higher than bank loans to cover the risk factor associated with the SMME sector: *"…there is a risk high involved with lending to them (small businesses), but we do not discriminate them…but we have to cover for that…".* SEFA also agreed that their loans are much higher: "…*banks offer cheaper loans but this people cannot get them…yes, our loans are much expensive…depending on individual applicant, maybe 15% or even higher…*" The latter also stated that lending through the RFIs makes loan prices even higher: "…*the RFIs also attach their own interests…"* Although the effort is to increase access to finance for desperate businesses that are less price sensitive to the RFIs loans, high loan prices can still be excluding some SMMEs that are sceptical of high loan prices. The IDC also stated that they use cost-based loan pricing. This type of pricing makes loan prices higher than what would be charged by the general financial markets.

(j) Lack of shared growth plans

Entrepreneurs are said to lack an understanding of growth strategies, and financing therefore fails to achieve the intended purpose. Some of the DFIs stated that due to lack of understanding of growth strategies, some entrepreneurs require financing that does not match their plans, in the end the financing ends up not serving any purpose and not benefitting anyone. For example, DSBD and FDC provide asset finance in the form of machinery or equipment but some entrepreneurs end up with assets that are not properly being utilised to match projections: *"…we are at time faced with a situation where we end up repossessing the equipment because even after being assisted, the businesses would still not perform, which means that the entrepreneur might have made wrong projections during finance applications….yes, I think the problem may lie with growth plans*…" FDC stated.

Limited understanding of growth strategies by the entrepreneurs was highlighted by other DFIs, for example, SEFA mentioned that some applications fall short of clear growth plans and at times cause the applications being declined.

6.2.8 Expected return on investment (ROI)

Another theme that emerged from the interviews relates to return on investment. When asked about what their expected return on investment is, the DFIs gave differing views. One institution stated that full repayment with interest is what the DFI expects:*"…the institution needs to be sustainable and be able to assist other clients …our plan is to be self-sustainable as we operate on limited budget, if we can generate some revenue, hopefully we will reach there……no, we have no specific targets in terms of numbers, our facing cannot be the only factor for employment…".* Another DFI, the NYDA stated that, among other things, the contribution towards job creation for young people is one of the cornerstones of the institution: *"…it gives us pleasure if we see a young person funded by the agency being able to create an additional employment for other people, especially young people and women…not just temporary employment, but permanent employment …" The* FDC also stated that job creation is one of the targets that the institution hopes to see as the ultimate result of the funding provided. The IDC considers empowerment and the business's ability to generate "*revenue within two years of funding"* as measure for the success of the investment.

DBSD mentioned that other than employment creation as the burning issue for the government, the institution considers: "…*competitiveness and growth of small businesses to match mostly at least international standards (for exporting business)… for all growth potential businesses of course…"* as good measures of return on investment by the department.

6.2.9 Bridging a financing gap

From the interviews, a theme that is considered to relate to bridging the financing gap also emerged. The DFIs mentioned that through both their financial and non-financial programmes, they are trying to making financing accessible to small businesses and also create a conducive environment that will help small businesses to establish a relationship with the financial market. For example, the NYDA stated that they advise their clients to open bank accounts where the funds will be channelled. The FDC stated that they help their clients where possible with the purchasing of assets; the same assertion alluded to by the DBSD that they help their clients with the main challenge they usually face when seeking external finance, lack of tangible assets. The machinery the department assists small businesses with does not only improve production, but increases the asset base for the clients (small businesses).

6.2.10 Solutions and suggestions

The participants have recommended that the SMME sector needs more support from all the stakeholders involved, both government and private sector. A respondent from SEFA, for example, suggested that institutions need to be more lenient in terms of pricing the SMMEs: "…*the pricing plays a big factor because the pricing on money lent, pricing on the service fees, on cash deposit fees, all of these are factors that cost the small businesses at the end of the day…"* The other solution suggested from the same DFI has recommended that government should monitor the programmes very closely: *"…I think start off with government, it must intervene and regulate development pricing accordingly. I think that is my main thing..."*

The other recommendation was that the consultants/ advisors that provided business plans to SMMEs should include the clients in the whole process of business planning. This was because in most cases the entrepreneur hardly knew the contents of their business plans: "… *somebody else drew up the business plan but the owner still doesn't understand it… or does not even know the details…"*

More efforts are needed to communicate with the consumers or the market. For example: *"We still have people who do not know about the help we provide, let alone our individual products…we need to advertise in such a way that target market is reached to the capacity of our budget to say the least".* One respondent claimed that the marketing of the programmes needed to reach their target market.

6.2.11 Referrals

Each individual DFI has its own specific development financial programmes that are aimed to specifically cater for the individual DFI's target market. However, the DFIs mentioned that in the event that the DFI which is approached is not able to offer the support required by the entrepreneurs, the institution refers the client to the relevant DFI that is more capacitated to provide the support. For example, NCEDA stated: "*…we do not offer development finance to small businesses but we always assist our entrepreneurs every possible way we can… we make proper arrangements including securing appointments for them*…*we have a working relationship with SEFA, we refer* *entrepreneurs to SEFA…".* NYDA and SEFA also conveyed similar efforts. NYDA said that the institution is limited to offer development finance up to R100000 (see figure 6.6), however, if the required amount exceeds the stated amount, the client is referred to SEFA. Similarly, SEFA also refers the client to IDC, on condition that the entrepreneur requires development finance that exceeds SEFA's limit: "…*the institution does not give the client a cold shoulder and say, sorry we are unable to help you…instead, we advise the client accordingly that their need can be best handled by IDC*…"

This result shows that even when the DFI is not in the position to directly provide finance to small businesses, the working relationship between the DFIs enables them to make referrals to the other DFIs.

6.3 DATA PRESENTATION FINDINGS OF PHASE 2

This second part of the chapter deals with the statistical methods utilised in analysing the quantitative data gathered during the second phase. Although the current study is an exploratory research, working assumptions were used to guide the second phase. As such, this study did not solely depend on the assumptions, however, the emergence of hidden constructs was allowed to further deepen the understanding of the phenomenon of development finance, and not only decisions based on the assumptions. Therefore the second phase delves the assumptions that followed and developed from the conclusions of the first phase in order to help derive the implications that were used to reach the completion of this dissertation. This phase of the study was designed to help provide answers to these research questions:

- How do the entrepreneurs across demographic variables (gender, race, gender and education) perceive the role of development finance towards the performance of their businesses?
- What propositions do entrepreneurs have for development finance?
- What are the perceptions of the respondents on the role of the DFIs' financing support to small business development with regards to bridging the financing gap?

Assumptions

In order to answer the research questions of Phase 2 of the study, they were translated into hypotheses as proposed by Tredoux and Durrheim (2002).

- There is a significant difference in the perceptions of the respondents (the entrepreneurs) from Tshwane Metropolitan Municipality on the impact of the DFIs' financing to small business growth across respective demographic variables (gender, race, age and education).
- There is a significant difference in the perceptions of the respondents regarding propositions to development finance for small businesses.
- There is a significant difference in the perceptions of the respondents on the role of the DFIs' financing support to small business development in terms of bridging the financing gap.

A total of 301 questionnaires were fully completed by entrepreneurs based in Tshwane Metropolitan Municipality, which is a respectable sixty-two percent (62%) response rate.

6.3.1 Presentation and analysis of research results

This section is based on the data presentation and analysis of Phase 2 of the study. The section is divided into five sections: Section A, B, C and D, with Section E consisting of open-ended questions. Sections A and B are analysed through descriptive statistics. Sections C and D are based on the perceptions of the respondents regarding the main themes of Phase 1, while Section E is based open-ended questions and therefore analysed using content analysis techniques.

6.3.1.1 Section A: Biographical data

Entrepreneurs were requested to provide information regarding their gender, age, race and highest educational level. The following table shows their gender differences.

a) Gender classification of respondents

Question 1 asked about the gender of the respondents and the answers were analysed to reveal the findings summarised in Table 6.3.

Table 6.3: Summary of respondents' biographical data on gender differences

Demographic variable	Frequency	%	Cumulative %
Male	130	43.2	43.2
Female	171	56.8	100.0
Total	**301**	**100.0**	

Source: Author's own compilation

Table 6.3 shows that the majority, 171 respondents (about 57%) of entrepreneurs in In Tshwane are females. This statistics therefore, implies that more females than males were financed through the DFIs' financing programmes. This is no surprise that more female than males opt to operate their own businesses, as StatsSA (2014) shows that females represent the largest gender group (51%) of the population.

Table 6.4 below presents a summary of the respondents' biographical data on age groups.

b) Age categories of respondents

Question 2 requested that respondents indicate their age categories. The results were summarised according to the following Table 6.4.

Table 6.4: Summary of respondents' biographical data on age groups

Biographic variable: Age	Frequency	%	Cumulative %
18 - 35 years	82	27.2	27.2
36 - 45 years	152	50.5	77.7
46 - 55 years	53	17.6	95.3
56+ years	14	4.7	100.0
Total	**301**	**100.0**	

Source: Author's own compilation

Table 6.4 illustrates that almost more than half (51%) of small businesses financed by the DFIs were owned by people in the 36 – 45 age group. Almost a third (about 27%) of small businesses is owned by the age group 18 – 35 years (youth). Less than a quarter (22.3%) of small businesses is owned by the age group 46 and older. It can be due to the fact that the majority of this age group are in full-time employment or have graduated to established businesses which can easily access financing from the financial markets and therefore do not need DFI support.

c) Racial classification of respondents

Question 3 required that respondents classify their demographic information in terms of race and the results are summarised in Table 6.5

Table 6.5: Summary of respondents' biographical data on racial differences

Race	Frequency	%
African	182	**60.5**
White	46	**15.3**
Indian*	25	**8.3**
Coloured	48	**15.9**
Total	301	**100.0**

*Indian includes Chinese, Indian, and other Asian

Source: Author's own compilation

From Table 6.5 above, it can be seen that the majority (almost 61%) of small businesses financed by the DFIs were owned by Africans, this is followed by Coloured and White entrepreneurs who owned at least 16% and 15% of small businesses, respectively. About 25 (8%) of the small businesses taking part in the study are owned by Indian entrepreneurs. These statistical figures correlate positively with the national racial demographics. Africans represent the highest racial group in SA (about 80%) with Coloureds and Whites representing about 9% and 8% of the population respectively, while Indians/ Asians only make up about 3% of the population (StatsSA, 2014).

d) Highest educational level of respondents

Question 4 of the questionnaire asked the respondents to indicate their highest level of education. The results are presented in Table 6.6 below.

Table 6.6: Summary of respondents' biographical data on education level

Education	Frequency	%
Below Grade 12	108	35.9
Grade 12	67	22.3
Tertiary	81	26.9
Failed Grade 12	45	15.0
Total	**301**	**100.0**

Source: Author's own compilation

It is apparent from Table 6.6 above that most (108) of small businesses financed by the DFIs were owned by people who did not study up to Grade 12, equally interesting though, is that about 64% (that is 22 % + 27% +15%) of small business owners had at least studied up to Grade 12, with the majority (27%) of them having studied even further to tertiary level. With the unemployment levels at about 26% in the country, the people who do not have at least Grade 12, have lower employment prospects and operating their own businesses is the most viable option, and the group require more developmental support for their businesses to grow. The last group who "failed grade 12" is placed after the respondents themselves included it under the "other" section of the question.

The tertiary education level may include vocational training, post matric certificates, diplomas, bachelor's degrees and B.Tech and Honours degrees as well as masters in various fields. The next Section B presents the characteristics of small businesses.

6.3.1.2 Section B: The characteristics of the business

The purpose of Section B of the questionnaire was to collect the information on the characteristics of small businesses. The respondents were asked questions that relate to the characteristics of their businesses. The respondents were once again reminded and ensured that the information they provide in this section would be treated with confidentiality and would only be used for illustrative purposes. The results presented in this section gives priority focus on demographic variables as these are used as factors that determine designated or previously marginalised groups as per the Small Business Development Strategy Policy of the SA government.

a) The choice of business language

In Question 5 of the questionnaire, respondents were asked to indicate the language they choose as the business language for their businesses other than their own home language. The results are highlighted in Table 6.7.

Table 6.7: Summary of use of English as a language of -choice

Language	Frequency	%	Cumulative %
English	266	**88.4**	88.4
Other	35	**11.6**	100.0
Total	**301**	**100.0**	

Source: Author's own compilation

It is evident from Table 6.7 that the majority of the respondents (84%) are conversant in English, with only about 12% of respondents preferring another language. It means in providing development support for small business the information can be made available in English. However a provision can be made to accommodate people who cannot understand English. The following table provides information on the age of the business.

b) Age of the business

Question 6 required the respondents to show how long they have been operating their businesses. The respondents were asked to mention the period in which they have been in business. The results are tabled in Table 6.8.

Table 6.8: Summary of age of the business

Age of the business	Frequency	%	Cumulative %
0 -1 year	65	21.6	21.6
More than1 year but less than 5 years	96	31.9	53.5
5 years but less than 10 years	87	28.9	82.4
10 years and above	53	17.6	100.0
Total	**301**	**100.0**	

Source: Author's own compilation

Table 6.8 represents a summary of the age of the businesses that participated in the study. About 22% of the businesses have not existed beyond the age one year, while only about 18% of the businesses have been in existence for at least ten years or more. The majority of the businesses (31.9% + 28.9%) have existed beyond one year but less than ten years, almost 32% of them being in the less than five years of existence category, while almost 29% have been in existence for more than five years.

The next tables demonstrate cross-tabulation of the age of the businesses across the demographic variables of the respondents.

Table 6.9: Age of the respondent per the age of the business

Age group of respondents	Categories of the business existence				Total
	0 -1 year	more than1 year but less than 5 years	5 years but less than 10 years	10 years and above	
18 - 35 years	39	26	17	0	**82**
36 - 45 years	28	50	46	28	**152**
46 - 55 years	6	16	20	11	**53**
56+ years	1	4	4	5	**14**
Total	**65**	**96**	**87**	**53**	**301**

Source: Author's own compilation

Table 6.9 demonstrates a cross-tabulation of the categories of the business existence (categories) against the age of respondents. Of the 82 businesses operated by young people (18 -35 years), 65 (79%) are still within the less than five years of existence category, with almost 48% (39 of 82) of the business in the category of less than one year and no businesses in the category of ten or more years old.

The majority of businesses, 152 out of 301 businesses (50.5%) are owned by the age group of 36 – 45, the group which also has the highest number in the category of business existence of more than one year but less than five years. While it is not surprising that young people have more businesses in the less than one year category, it is interesting that the age group of 56+ years has the lowest number in each of the categories of business years of existence.

Below is Table 6.10 which presents a cross-tabulation of age of the business relative to the gender variable.

Table 6.10: Age of the business per gender variable

Gender of respondents	Categories of the business existence				Total
	0 -1 year	more than1 year but less than 5 years	5 years but less than 10 years	10 years and above	
Male	46	43	30	11	130
Female	56	61	39	15	171
Total	**102**	**104**	**69**	**26**	**301**

Source: Author's own compilation

When asked to provide details of age of their business, the respondents provided answers that are analysed according to the categories of the business' period of existence as presented in Table 6.8. The results show that in all the business age categories, there are more females than male owners. The results show that, of the 130 male-owned businesses, about 35% have not existed beyond a period of one year, while their female-owned businesses in the same age category make only 32% (56 of the 171). The majority of female-owned businesses (about 58%) have been established for more than one year but less than ten years; while many (about 68%) of male-owned business are in the age categories of less than five years.

The next table displays a cross tabulation of business age relative to the race of the respondents.

Table 6.11: Age of the business per race variable of respondents

Race group of respondents	When was business established?				Total
	0 -1 year	more than1 year but less than 5 years	5 years but less than 10 years	10 years and above	
African	68	64	34	16	182
White	11	14	19	2	46
Indian	6	8	8	3	25
Coloured	17	18	8	5	48
Total	**102**	**104**	**69**	**26**	**301**

Source: Author's own compilation

The results in Table 6.11 show that African-owned businesses dominate any other race (almost 61%) in all the business age categories, with about 73% of the African-owned businesses in the age category of less than five years. Coloured and white-owned businesses on the other hand, occupy about 15% each in all business categories. Indian-owned businesses trail with only about 8%, the results indicate that their businesses demonstrate they have about 64% of the latter have been in business in more than one year but less than ten years.

The next Table 6.12 provides a summary of the industries in which the respondents operate their businesses.

c) The industry in which the business operate

In question 11, the respondents were required to indicate the industry in which they are operating their businesses. The results are shown in frequency Table 6.12, while the custom as well as corresponding graphs thereof, illustrate the results across demographic variables.

Table 6.12: Summary of the industry of the business

Industry	Frequency	Percentage
Retail + motor trade and repairs	24	8.0
Manufacturing	7	2.3
Cleaning / catering/accommodation	35	11.6
Construction	64	21.3
Wholesale trade/ commercial agents and allied services	48	15.9
Finance and business services	33	11.0
Transport, storage and communication	32	10.6
Agriculture	11	3.7
Mining + quarrying + electricity + gas + water	25	8.3
Community and personal services	22	7.3
Total	**301**	**100.0**

Source: Author's own compilation

It can be seen from Table 6.12 that most of the businesses financed by the DFIs in the Tshwane Metropolitan District Municipality are in construction industry (2.3%). The manufacturing industry has the smallest number (7%) of all the industries represented. This can be because the industry is well saturated in the Ekurhuleni District within the same province of Gauteng.

The following custom Table 6.13 and the graph in Figure 6.11 illustrate the demographic variables per industry distribution.

Table 6.13: Gender distribution per industry

Industry	Gender of respondent			
	Male		Female	
	Count	Row N %	Count	Row N %
Retail + motor trade and repairs	9	40.9%	13	59.1%
Manufacturing	2	28.6%	5	71.4%
Cleaning / catering/accommodation	15	42.9%	20	57.1%
Construction	22	41.5%	31	58.5%
Wholesale trade/ commercial agents and allied services	23	53.5%	20	46.5%
Finance and business services	14	42.4%	19	57.6%
Transport, storage and communication	11	36.7%	19	63.3%
Agriculture	6	54.5%	5	45.5%
Mining + quarrying + electricity + gas + water	12	48.0%	13	52.0%
Community and personal services	16	38.1%	26	61.9%

Source: Author's own analysis

Table 6.13 and Figure 6.11 both illustrate the gender distribution per industry. The illustrations show that more women than men are represented in all the industries, with the exception of two industries, "wholesale trade/commercial agents and allied services" and agriculture where more men (53.5% and 54.5%) than women (46.5% and 45.5%) own small businesses, respectively.

The majority of women (71.4%) operate businesses in the manufacturing industry compared to only about 29% men. Interestingly, more women (63.3% and 52% respectively) operate businesses in what are predominately male-run industries (transport, storage and communication; and mining, quarrying, electricity and gas), while men own only 36.7% and 48% respectively.

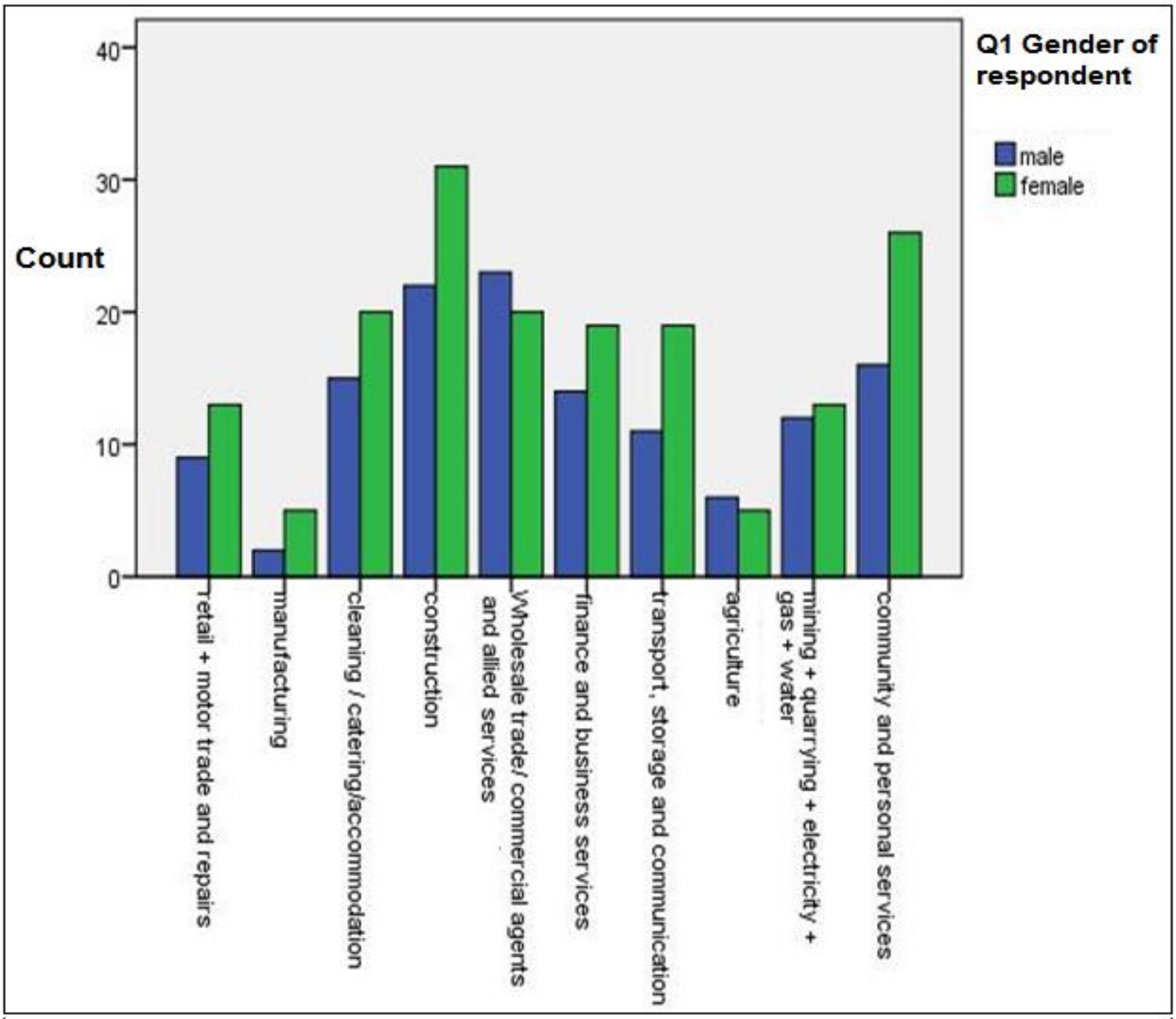


Figure 6.11: Gender distribution per industry

Source: Author's own compilation

The following Table 6.14 presents the industries in which respondents operate their businesses in terms of the race variables.

Table 6.14: Race distribution per industry

Industry	Race of respondent							
	African		White		Indian		Coloured	
	No.	%	No.	%	No.	%	No.	%
Retail + motor trade and repairs	13	59.1	2	9.1	2	9.1	5	22.7
Manufacturing	3	42.9	2	28.6	1	14.3	1	14.3
Cleaning / catering/accommodation	20	57.1	6	17.1	1	2.9	8	22.9
Construction	35	66.0	9	17.0	5	9.4	4	7.5
Wholesale trade/ commercial agents and allied services	26	60.5	6	14.0	5	11.6	6	14.0
Finance and business services	22	66.7	4	12.1	4	12.1	3	9.1
Transport, storage and communication	17	56.7	7	23.3	2	6.7	4	13.3
Agriculture	5	45.5	1	9.1	2	18.2	3	27.3
Mining + quarrying + electricity + gas + water	15	60.0	6	24.0	0	0.0	4	16.0
Community and personal services	26	61.9	3	7.1	3	7.1	10	23.8

Source: Author's own compilation

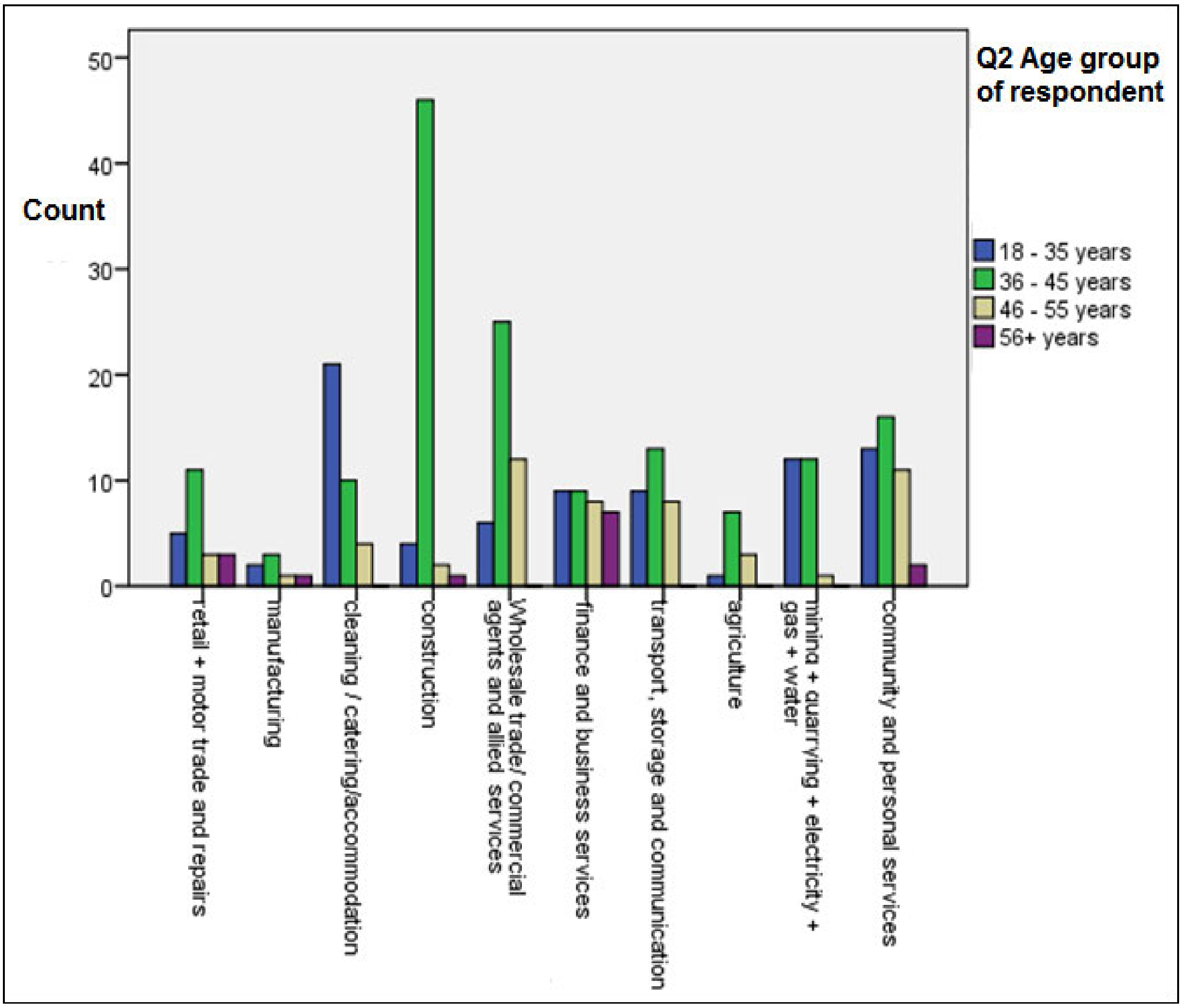


Figure 6.12: The industry in which the business operates

Source: Author's own compilation

d) The size of the business

The respondents were asked to describe the size of their businesses in terms of the number of people employed and in terms of the annual turnover. The following tables (6.15 and 6.16) illustrate the information per the relevant responses.

Table 6.15: The size of the business in terms of employees

Size	Frequency	Percentage
Micro (1 - 5)	169	56.1
Very small (6 - 20)	98	32.6
Small (21 - 50)	30	10.0
Medium (51 - 200)	4	1.3

Source: Author's own compilation

The small businesses sector in Tshwane Metropolitan Municipality is dominated by micro businesses, the category that represents more than half (56.1%) of all SMMEs as shown in Table 6.15. The results also reveal that medium businesses, which employ between 51 and 200 people (see Section 2.2.4), are the minority of all small businesses accounting for only 1.3%, while the category of very small and small account for about 42.6% combined.

Table 6.16: The size of the business in terms of annual turnover

Turnover	Frequency	Percentage
Less than R50 000	158	52.5
R50 000 - R 100 000	111	36.9
R101 000 - R500 000	31	10.3
R501 000 - R15 000 000	1	0.3
Total	301	100.0

Source: Author's own compilation

Table 6.16 shows that in terms of annual turnover, the majority (52.5%) of small businesses in Tshwane Metropolitan Municipality are in the category of less than R50 000. The category of R50 000 – R100 000 accounts for about 37%, making this category the second highest of small businesses in Tshwane. The categories of small businesses that have the highest annual turnover (101 000 – R500 000 and R501 000

– R15 000 000) represent the lowest number of businesses, accounting for only about 11% combined.

e) The outcome of first finance application

The respondents were asked to mention the outcome of their first application at a DFI.

The next Table 6.17 presents a summary of the result of the first finance application, while Tables 6.18; 6.19; and 6.20 show the results of the first finance application by the respondents across demographic variables analysed through cross-tabulation. The last table in the current sub-section is Table 6.21 portraying the outcome of the first finance application per the age of the business.

Table 6.17: First finance application outcome

Outcome	Frequency	Percentage
Successful	190	63.1
Unsuccessful	111	36.9
Total	301	100.0

Source: Author's own compilation

The data in Table 6.17 indicates that the majority (about 63%) of entrepreneurs in Tshwane were successful in their first finance application at the DFIs. Only about 37% of entrepreneurs were unsuccessful in their first DFI finance application. The next Table 6.18 presents the outcome of first finance application in terms of gender variables.

Table 6.18: The outcome of first finance application per gender variable

Gender of respondents	Successful	Unsuccessful	Total
Male	80	50	130
Female	110	61	171
Total	190	111	301

Source: Author's own compilation

The majority (110 of 190) of successful entrepreneurs in their first finance application at the DFIs were females. The results in Table 6.18 show that about 62% of the male respondents indicated that their first finance application with the DFIs was successful, while about 38% of male respondents indicated that their first application was declined. The results further show that more women (58%) than men (42%) succeeded in the first finance application. Interestingly, out of the 111 respondents who indicated that their first applications were declined, there were more women who had their applications declined than men (55% and 45% respectively), showing almost a similar gender pattern between the successful and unsuccessful outcomes. The following

Table 6.19 provides a summary of the result of the first finance application per race variable.

Table 6.19: The outcome of first finance application per race variable

Race of respondent	Successful	Unsuccessful	Total
African	114	68	182
White	31	15	46
Indian	15	10	25
Coloured	30	18	48
Total	190	111	301

Source: Author's own compilation

Table 6.19 shows the cross-tabulation of the outcome of the first finance application at the DFIs according to race. About 114 of the 182 (62%) African entrepreneurs succeeded in their first application for funding, while 38% (62 of the 182) were unsuccessful in their first application. About 63% of the 46 businesses owned by white people were successful in their first finance application, against 37% of the latter's businesses which were not successful. Of the 25 businesses owned by Indian people, 60% of first finance applications were successful, while only 40% were unsuccessful. Almost 63% of the 48 businesses owned by coloured people were successful in their first finance application and about 37% were unsuccessful.

The findings therefore, indicate that the majority of respondents (60%) that were successful in their first finance application at the DFIs are Africans. The rest of the 40% of the respondents that succeeded in their first finance application were in the White, Indian and Coloured racial groups, with Indian respondents having the lowest percentage at only 7%.

Table 6.20 below presents the results of the first finance application cross-tabulated by the age of the respondents.

Table 6.20: First finance application outcome per age variable of the respondents

Age group of respondent	Finance application 1st outcome		Total
	Successful	Unsuccessful	
18 - 35 years	43	39	**82**
36 - 45 years	102	50	**152**
46 - 55 years	35	18	**53**
56+ years	10	4	**14**
Total	**190**	**111**	**301**

Source: Author's own compilation

As Table 6.20 depicts, that the majority (about 54% of 190) of businesses that succeeded in the first finance application are owned by entrepreneurs in the age category 36 - 45 years, representing almost a third (67% of 152) of all businesses in the same age category that applied for finance. Entrepreneurs in the age category 56 and above represent the smallest percentage (5% of 190) of all entrepreneurs that succeeded in the first finance application and also the smallest percentage (3% of 190) of businesses that had their application declined. The majority of young people 52% (43 of 82) that applied for finance, succeeded in their first application.

While the preceding three tables above highlight the results of the first finance application in terms of the demographic variables of the respondents, the following table provides a portrait of the results of the first application in terms of the age of the businesses.

The respondents were asked to indicate the outcome of their first finance application at the DFIs in Table 6.17; this was cross-tabulated with the age of the business variable in Table 6.21 below.

Table 6.21: The outcome of first finance application per the age of the business

Age of the business	Finance application 1st outcome		Total
	Successful	Unsuccessful	
0 -1 year	62	40	102
more than1 year but less than 5 years	68	36	104
5 years and more but less than 10 years	46	23	69
10 years and above	14	12	26
Total	**190**	**111**	**301**

Source: Author's own compilation

Table 6.21 provides a summary of the first application by the age of the business. The results show that more than half of the businesses (63% of 301) in all the categories combined were successful in their first finance application, against 37% (all categories combined) which were declined. The majority of the businesses that were successful in their loan applications (54% of 190) were in the business age category of more than 1 year but less than 5 years. This business age category is hierarchically followed by the category of businesses that were in the age category of less than one year (33%); 5 years and more but less than 10 years (24%); and 10 years and above, which represented the least number of businesses (7%). The results (that more businesses within the early age stages of the businesses life stage were more successful in their first finance applications) are not surprising as these are the target groups identified by the DFIs. The well established businesses (five years and older) are more likely to be financial markets clients than early business entrants (less than five years).

The next sub-section portrays the frequency table of start-up finance and the cross-tabulation of the source of start-up finance by the respondents across demographic variables.

f) Source of start-up finance

The respondents were asked to indicate the source of start-up finance for their businesses, and the results are presented in tables below.

Table 6.22 presents a summary of the source of start-up finance, while the tables that follow show the results of the source of start-up finance by the respondents across demographic variables analysed through cross-tabulation.

Table 6.22: Summary of source of start-up finance

Source of start-up finance	Frequency	%	Cumulative Percent
Family/personal savings	41	13.6	13.6
Banks	17	5.6	19.3
DFI	**155**	**51.5**	70.8
Stokvels	88	29.2	100.0
Total	301	100.0	13.6

Source: Author's own compilation

From the results as shown in Table 6.22, more than half of the entrepreneurs in Tshwane (almost 52%) have sourced their start-up finance from the DFIs, while close to a third of the entrepreneurs (29%) sourced start-up finance from stokvels. The results further show that the lowest percentage of start-up finance was sourced from family or personal savings and banks, representing about 14% and 6% respectively. The next three Tables (6.23; 6.24; 6.25) and Table 6.26 illustrate the results of the source of start-up finance per the biographic variables as well as the age of the business.

Table 6.23: Cross-tabulation of start-up finance per gender

Gender of respondent	Family/personal savings	Bank	DFI	Stokvel	Total
Male	15	9	61	45	130
Female	26	8	94	43	171
Total	**41**	**17**	**155**	**88**	**301**

Source: Author's own compilation

Table 6.23 provides a portrait of the cross-tabulation of source of start-up finance per the gender of the respondents. The results show that more females than males, that is, about 61% (94 of 155) of female entrepreneurs in Tshwane Metropolitan Municipality sourced start-up finance from the DFIs, against 39% of the male entrepreneurs. Interestingly, even though the difference is marginally small, more males than females (about 51%) of the entrepreneurs that sourced start-up finance from stokvels are males, against 49% of the entrepreneurs being females. Even more interesting, the results reveal that family/personal savings and banks are the sources least utilised for start-up finance for both male and female entrepreneurs in Tshwane Metropolitan Municipality, representing about 18% of 130 males and 20% of 171 female entrepreneurs, respectively. The next Table 6.24 presents the results of the source of start-up finance per the age groups of respondents.

Table 6.24: Cross tabulation of source of start-up finance per age group

Age group of respondents	Family/personal savings	Bank	DFI	Stokvel	Total
18 - 35 years	7	3	**42**	30	82
36 - 45 years	20	9	**82**	41	152
46 - 55 years	12	4	**23**	14	53
56+ years	2	1	**8**	3	14
Total	41	17	**155**	88	301

Source: Author's own compilation

Table 6.24 presents a cross-tabulation of source of start-up finance per age group of the respondents. The results demonstrate that the majority of the respondents that sourced finance from the DFIs, are in the age group 35-45, representing about 52% of the 155 respondents. The second highest age group (27%) that sourced start-up finance from the DFIs are the youth (in age category of 18-35). The age categories 46-55 and 56+ represent the lowest number (31% combined) of entrepreneurs who sourced start-up finance from the DFIs.

The following Table 6.25 illustrates a cross-tabulation of source of start-up finance per the race groups of the respondents.

Table 6.25: Cross-tabulation of source of start-up finance per race group

Race of the respondent	Family/personal savings	Bank	DFI	Stokvel	Total
African	0	3	**101**	78	182
White	23	9	**14**	0	46
Indian	9	2	**12**	2	25
Coloured	9	3	**28**	8	48
Total	41	17	**155**	88	301

Source: Author's own compilation

On analysing the responses from the entrepreneurs regarding the source of start-up finance in terms of racial variable, the results, as illustrated in Table 6.25, revealed that the majority (65%) of the entrepreneurs that sourced start-up finance from the DFIs were Africans. The second category was the Coloured entrepreneurs denoting 18%, while the White entrepreneurs (9%) who sourced start-up finance from the DFIs came in at third place. The Indians represented the lowest category (about 8%) to obtain start-up finance from the DFIs. Worthy of note is the findings that the entrepreneurs in Tshwane Metropolitan Municipality who sourced finance from "family/personal savings" category, have White entrepreneurs as the majority (58%) compared to 0% of African entrepreneurs. Similarly, the majority of African entrepreneurs (89%) used stokvels as the source of start-up finance, while none of the White entrepreneurs (0%) used stokvels. The Indian (8%) and Coloured (17%) entrepreneurs recorded low percentages of securing start-up finance from stokvels.

The last table in the current subsection, Table 6.26, portrays a cross-tabulation of the age of businesses that have used DFIs as source of start-up finance.

Table 6.26: Cross-tabulation of source of start-up finance per age of the business

Age of the business	Family/ personal savings	Bank	DFI	Stokvel	Total
0 -1 year	12	4	**55**	31	102
more than1 year but less than 5 years	13	5	**51**	35	104
5 years but less than 10 years	14	7	**31**	17	69
10 years and above	2	1	**18**	5	26
Total	41	17	**155**	88	301

Source: Author's own compilation

According to Table 6.26 above, the majority of businesses that used the DFIs as sources of start-up finance were at less than five years, representing about 68% on the one hand. On the other hand, only 32% (31 +18) of all businesses that sourced start-up finance from the DFIs were at least five years or older, of which businesses ten years and older made up only 11%. The same age categories of businesses (less than five years) were in the lead (75%) in all the age categories that sourced start-up finance from stokvels. Banks were recorded the least by all age categories of businesses, though strangely, businesses that are older than ten years recorded the lowest (5%) of all businesses that sourced finance from banks for start-up.

g) Additional support provided by the DFIs

When asked to provide information on additional support based on the outcome of their first finance application, the responses are illustrated in the Table 6.27 below.

Table 6.27: Summary of additional support provided by the DFIs

Type of support	Frequency	Percentage
Offered non-financial support	190	63.1
Referred to another DFI	111	36.9
Total	301	100.0

Source: Author's own compilation

Data from Table 6.27 reveals that based on the outcome of the first finance application (see also Table 6.17) the 190 entrepreneurs that were successful in their first finance application were also provided with additional support by the same DFI (see Section 6.2.2.2). The results which further confirm the findings from the DFIs that other than financial support, the DFIs also provide non-financial support.

h) Type of finance received from the DFIs

The respondents were required to indicate the type of finance received from the DFIs and the results are presented in the following Table 6.28.

Table 6.28: Type of finance received from the DFIs

Finance type	Frequency	Percentage
Loan	198	**65.8**
Credit guarantee scheme	22	**7.3**
Procurement	66	**21.9**
Grant	15	**5.0**
Total	301	**100.0**

Source: Author's own compilation

The results from Table 6.28 above illustrate that loans are the most highly sought-after type of finance from the DFIs (66%), while credit guarantee schemes and grants are the least received type of financing from the DFIs, representing the low rates of 7% and 5%, respectively. Although indicating the low rate of 22% (less than a quarter of respondents), procurement finance stands as the second most sought-after finance, after loans. The results confirm the information provided by the DFIs that credit guarantee schemes are a form of financing that is not functioning very well as a result of banking regulations (see Section 6.2.7(b)).

i) The area of the business that improved after DFI funding

The respondents were requested to indicate the area of the business that has improved after received development finance from the DFIs. The results are presented in Table 6.29.

Table 6.29: Business area that improved due to DFI's finance

	Frequency	Percent
Revenue	5	1.7
Sales	9	3.0
Stock	14	4.7
Additional product	147	48.8
Additional personnel	126	41.9
Total	301	100.0

Source: Author's own compilation

The results presented in Table 6.29 show that the majority of the respondents (49% and 42%) believe that both additional product and additional personnel respectively, are the areas that have improved the most after financing by the DFIs. Only less than 10% of the respondents reported that revenue, sales and stock, combined, improved after financing by the DFIs. The results imply that the entrepreneurs in the last category may not have an understanding of growth strategies, since additional products and additional personnel require an increase in revenue in order to be attained.

Table 6.30 presents the results of the meaning of business growth according to the entrepreneurs in Tshwane Metropolitan Municipality.

Table 6.30: Meaning of growth of the business

Meaning of business growth	Frequency	percent
Increase employment	84	27.9
Business expansion	105	34.9
Sales growth	34	11.3
Increased turnover	78	25.9
Total	301	100.0

Source: Author's own compilation

When asked to define their own understanding of business growth, the respondents provided the answers as illustrated in Table 6.30. The results reveal that more than a third of the respondents (35%) consider business growth in terms of business expansion, and about 28% of the respondents believe an increase in the number of employees imply business growth, almost equivalent to about 27% of the respondents who view business growth as an increase in turnover. Interestingly, while the three groups mentioned are fairly equal, only the smallest number of the respondents (about 11%) view business growth in terms of an increase in sales.

The next Section C focuses on the perceptions of the respondents with regard to the DFIs.

6.3.1.3 Section C: The perceptions of the entrepreneurs on DFIs

Descriptive Analysis

The current section is based on the perceptions of the respondents regarding the financing of small businesses by the DFIs. This section presents the results that were analysed through descriptive analysis. Meaningful results are expressed according to the critical themes of Phase 1 that are contextualised within the parameters of the research objectives

The measurement scale is the Likert scale and scale measurement or decoding is highlighted below:

1. Strongly disagree
2. Disagree
3. Neutral
4. Agree
5. Strongly

The following tables are related to the results of the perceptions of the study's respondents regarding the main themes of Phase 1: Part A: the development financing of the DFIs (financing programmes/products), non-financial programmes and bridging financing gap, while Part B is based on the perceptions of the entrepreneurs regarding development finance and growth strategies as well as propositions thereof.

Part A

I. Development financial programmes

The respondents were asked to indicate their views on the development financial programmes offered by the DFIs as identified in Phase 1.

a) Development financing programmes of the DFIs increases the growth of small businesses

The results shown in Table 6.31 present the responses of the participants regarding whether development financing has helped their businesses.

Table 6.31: DFI funding has helped to grow my business

	Frequency	Percent
Disagree	2	0.7
Neutral	84	27.9
Agree	147	48.8
Strongly agree	68	22.6
Total	301	100

Source: Author's own compilation

The results presented in Table 6.31, show that 71.4% of entrepreneurs in Tshwane Metropolitan Municipality are of the opinion that funding provided by the DFIs helped to grow their businesses. Only a small percentage of the respondents (almost 28%) feel indifferent, while just about 1% of the respondents disagreed that funding by the DFIs has helped to grow their businesses.

The results imply that although small businesses are faced with financing constraints, the availability of development financing by the DFIs attributes to the growth of small businesses. The 1% percent of entrepreneurs that disagreed that DFIs' financing might be those that were financed through RFIs

b) DFIs' programmes and employment

Table 6.32 presents the responses of the participants regarding development finance on employment.

Table 6.32: Development finance helped me to create additional employment

	Frequency	Percent
Strongly disagree	4	1.3
Disagree	8	2.7
Indifferent	94	31.2
Agree	154	51.2
Strongly agree	41	13.6
Total	301	100

Source: Author's own compilation

The results shown in Table 6.32 reveal that 64.8% of the responses either agreed or strongly agreed that development finance programmes help entrepreneurs to create employment, followed by 31.2% that were neutral, while only 4% either disagreed or strongly disagreed.

The results imply that the development finance programmes of the DFIs help small businesses to create employment.

c) Development finance programmes and sales growth

Table 6.33 displays the findings of the participants' responses regarding development finance programmes on sales growth.

Table 6.33: Development finance helped increase sales

	Frequency	Percent
Disagree	18	6
Neutral	36	12
Agree	143	47.5
Strongly agree	104	34.6
Total	301	100

Source: Author's own compilation

It can be seen from Table 6.33 that the majority of the respondents (82.2%) either agreed or strongly agreed that the DFIs' development finance programmes increased the sale volumes of small businesses, and 12% of the respondents were neutral, while only a small portion (6%) disagreed.

The overall results imply that the development finance offered by the DFIs positively affects the short-term growth plans, such as sales, of small businesses.

d) Development finance and business turnover

Table 6.34 displays the results of the participants' responses regarding the effect of development finance on business turnover.

Table 6.34: Finance increased my turnover

	Frequency	Percent
Disagree	43	14.3
Neutral	140	46.5
Agree	115	38.2
Strongly agree	3	1
Total	301	100

Source: Author's own compilation

The results in Table 6.34 show that 39.2% of respondents agreed or strongly agreed that development finance increased business turnover, followed by 46.5% who were neutral, while 14.3% disagreed.

Interestingly, a significant proportion of the respondents were indifferent. This revelation may mean that the entrepreneurs either do not have a clear understanding of growth strategies or they do not necessarily associate business turnover with development finance.

e) The prices of DFIs' loans

Table 6.35 presents the findings of the responses of the participants that the interest rates charged on the DFIs' loans (development financing programmes) are very high.

Table 6.35: The interest rates charged on DFIs' loans are very high

	Frequency	Percent
Strongly disagree	5	1.7
Disagree	50	16.6
Indifferent	94	31.2
Agree	152	50.5
Total	301	100

Source: Author's own compilation

The results show that 50.5% of the participants responded that they agree that the interest rates charged on the DFIs' loans are too high, 31.2% were neutral, while 18.3% either disagreed or strongly disagreed.

Based on the results in Table 6.35, there is a proof that the DFIs' loan prices are too high for small businesses with a small number of responses who were neutral or disagreed. The high number of responses who were neutral may be the entrepreneurs who received forms of development finance other than loans.

f) Development finance (loans) and cash flow

Table 6.36 presents the results to the responses of the participants that development financing (loans) by the DFIs increases the business cash flow.

Table 6.36: Development finance and business cash-flow

	Frequency	Percent
Strongly disagree	120	39.9
Disagree	13	4.3
Neutral	145	48.2
Agree	23	7.6
Total	301	100

Source: Author's own compilation

The results in Table 6.36 indicate that 44.2% of the respondents either disagreed or strongly disagreed, 48.2% were neutral and only 7.6% agreed that development financing by the DFIs through loans increases business cash flow.

The results show that although the majority of the responses are neutral, however, the responses are biased more towards disagreed than towards agreed. This can be associated with the fact that the loans from DFIs are deemed to be expensive.

II. Non-financial programmes

Table 6.37 illustrates the perceptions of the respondents on the non-financial programmes provided by the DFIs.

Table 6.37: Non-financial programmes improved my business skills

Non-financial programmes improved my business skills	Frequency	Percent
Strongly disagree	0	0.0
Disagree	0	0.0
Neutral	0	0.0
Agree	247	82.1
Strongly agree	54	17.9
Total	301	100

Source: Author's own compilation

Table 6.37, interestingly, indicates that all the entrepreneurs, that is, 100% of the respondents in the study believe that non-financial programmes have increased their business skills.

The results therefore, provides an indication that the DFIs are addressing the problem of the shortage of management and business skills which has been identified as one of the challenges that contribute to the high failure rates among small businesses.

III. Effects of DFIs' loan pricing

Table 6.38 shows the perceptions of the respondents regarding the impact of the DFIs' loan prices on their cash flow.

Table 6.38: The high loan prices charged by the DFIs reduce cash flow

DFIs loans are too expensive	Frequency	Percent
Strongly disagree	1	0.3
Disagree	10	3.3
Neutral	33	11.0
Agree	238	79.1
Strongly agree	19	6.3
Total	301	100.0

Source: Author's own compilation

With a majority of 85.4%, as shown in Table 6.38, the respondents agree that high loan prices charged by the DFIs are too expensive and therefore affect cash flow. The results demonstrate that while the DFIs have made access to finance easy for small businesses, the prices charged are believed to be too high.

DFIs' loan prices and business growth

Table 6.39 provides the results of the responses of the participants regarding DFIs' loan prices and business growth.

Table 6.39: DFI interest rates show lack of shared framework of business growth

	Frequency	Percent
Strongly disagree	13	4.3
Disagree	34	11.3
Neutral	29	9.6
Agree	216	71.8
Strongly agree	9	3
Total	301	100

Source: Author's own compilation

The result overall reported that 15.6% either disagree or strongly disagree, 9.6% were neutral, while 72.1% agree or strongly agree that the DFIs' interest rates show lack of the shared framework of business growth.

IV. Bridging the financing gap

The DFIs through their development finance programmes and non-finance programmes bridge the finance gap facing small businesses. Lack of tangible assets; credit worthiness; collateral; and information asymmetry are some of the challenges that small businesses overcome with the help of development programmes from the DFIs.

a) Development support and relationship banking

Table 6.40 provides the result to the respondents' responses regarding the support of the DFIs that help small businesses establish relationships with financial markets.

Table 6.40: Development support of the DFIs increases relationship banking

	Frequency	Percent
Strongly disagree	2	0.7
Disagree	28	9.3
Neutral	41	13.6
Agree	212	70.4
Strongly agree	18	6
Total	301	100

Source: Author's own compilation

The results revealed that an overwhelming 76.4% of respondents either agreed or strongly agreed that the development support of the DFIs helps small businesses to establish a relationship with financial markets, followed by 13.6% who were neutral. Only 10% of the respondents either disagreed or strongly disagreed.

Based on the respondents, it is granted that there is a growing admission amongst entrepreneurs that through the support of the DFIs, small businesses can overcome some of financing barriers through relationship banking.

b) The DFIs' support reduces the high-risk premiums of bank loans

Table 6.41 provides the results to the perceptions of the respondents regarding the impact of the DFIs towards reducing the high-risk premiums of bank loans.

Table 6.41: The support of the DFIs reduces high-risk premium of bank loans

	Frequency	Percent
Strongly disagree	140	46.5
Disagree	16	5.3
Neutral	123	40.9
Agree	22	7.3
Strongly agree	0	0.0
Total	301	100

Source: Author's own compilation

Table 6.41 reveals that the majority of the respondents (51.8%) strongly disagree and disagree or are indifferent that the support of the DFIs reduces the high-risk premiums of the bank loans, while only 7.3% of the respondents agreed that the DFIs' support reduces the high-risk premiums of the bank loans.

The findings may be attributed to the fact that even with the availability of a credit guarantee scheme, the high interest rates that risky small businesses are charged by the financial markets remain unchanged, and hence the DFIs' support does not have any impact on the high bank loan prices.

c) Development financial support by the DFIs (loans) increases credit worthiness of entrepreneurs

Table 6.42 presents the participants' responses regarding development financing by the DFIs through loans that increase the credit worthiness of entrepreneurs.

Table 6.42: Development financial support of the DFIs increases credit worthiness

	Frequency	Percent
Strongly disagree	2	0.7
Disagree	48	15.9
Neutral	65	21.6
Agree	174	57.8
Strongly agree	12	4
Total	301	100

Source: Author's own compilation

The findings on Table 6.42 divulge that more than half of the respondents (61.8%) either agreed or strongly agreed that development financing of the DFIs through loans increases the creditworthiness of the entrepreneurs, followed by about 22% of the respondents who were neutral, whereas 16.6% either disagreed or strongly disagreed.

The results showed a mixture of responses from the respondents. Although the majority agreed, there was also a considerable proportion of the respondents who were neutral. This can be attributed to the fact that either this group of the participants have not yet encountered financial markets; or that small businesses remain an unfavourable market for financial markets. Lack of creditworthiness is considered in literature as one of the aspects that trigger access to finance for small businesses in the financial markets.

d) Development support and information asymmetry

Table 6.43 exhibits the results of the participants' responses to the question of development support on information asymmetry.

Table 6.43: The support by the DFIs reduces the problem of information asymmetry

	Frequency	Percent
Strongly disagree	10	3.3
Disagree	36	12
Neutral	27	9
Agree	196	65.1
Strongly agree	32	10.6
Total	301	100

Source: Author's own compilation

The results in Table 6.43 illustrate that 75.7% of the respondents either agreed or strongly agreed that support by the DFIs reduces the problems associated with information asymmetry for small businesses. Of the respondents, 9% were neutral while 15.3% either disagreed or strongly disagreed.

The results imply that the problem of access to finance for small businesses that is associated with information asymmetry can be reduced through the support of the DFIs.

e) Support of the DFIs and collateral

Table 6.44 shows the results from the responses of the participants regarding support of the DFIs and the problems related to collateral.

Table 6.44: The support of the DFIs reduces the problem of lack of collateral

	Frequency	Percent
Strongly disagree	11	3.7
Disagree	31	10.3
Neutral	38	12.6
Agree	196	65.1
Strongly agree	25	8.3
Total	301	100

Source: Author's own compilation

From Table 6.44 above, it can be seen that the majority of the respondents (73.4%) either agreed or strongly agreed that development support by the DFIs reduces the problem of lack of collateral, followed by 12.6% who were neutral, and 14% who either disagreed or strongly disagreed.

The findings deduce that through the support of the DFIs, small businesses are able to reduce the problem of access to finance that is related to lack of collateral in the financial markets.

f) Support of the DFIs and lack of credit record

Table 6.45 displays the results of the participants' response with regard to the DFIs' support and the problem of lack of a credit record.

Table 6.45: DFI support eliminates problems associated with lack of credit record

	Frequency	Percent
Strongly disagree	136	45.2
Disagree	17	5.6
Neutral	123	40.9
Agree	23	7.6
Strongly agree	2	0.7
Total	301	100

Source: Author's own compilation

The results reveal that only 8.3% of the respondents either agreed or strongly agreed that the support of the DFIs eliminates the problems associated with the lack of a credit record. About 41% of the respondents were neutral and 50.8% either disagreed or strongly disagreed.

The findings can be attributed to the fact that, after being funded by the DFIs, the entrepreneurs have not yet sought additional funding from the banks.

Part B:

V. DFIs' financing and business growth strategies

a) Effects of development financing on growth plans

Table 6.46 shows the results of the participants' responses regarding the DFIs' financing and business growth plans.

Table 6.46: The development finance helped me achieve my growth plans

	Frequency	Percent
Disagree	43	14.3
Neutral	143	47.5
Agree	112	37.2
Strongly agree	3	1
Total	301	100

Source: Author's own compilation

The results in Table 6.46 show that 38.2% of the respondents either agreed or strongly agreed that development finance have helped achieve business growth plans, followed by 47.5% who were neutral; and 14.3% who disagreed.

b) Shared understanding of long-term growth plans

Table 6.47 displays the result of the participants' responses regarding the sharing of long-term growth plans.

Table 6.47: Long-term growth plans discussed with the DFI

	Frequency	Percent
Disagree	43	14.3
Neutral	130	43.2
Agree	108	35.9
Strongly agree	20	6.6
Total	301	100

Source: Author's own compilation

The results in Table 6.47 show that 42.5% of the respondents either agreed or strongly agreed that long-term growth plans were discussed with the DFI, followed by 43.2% who were neutral, and 14.3% who disagreed.

c) Shared understanding of growth plans

Table 6.48 illustrates the results of the participants' responses regarding the DFIs' understanding of the entrepreneurs' growth plans.

Table 6.48: The DFI understands my business growth plans

	Frequency	Percent
Strongly disagree	244	81.1
Disagree	57	18.9
Total	301	100

Source: Author's own compilation

The results in Table 6.48 demonstrate that all the respondents (100%) either disagreed or strongly disagreed that the DFIs understood their growth plans.

These worrisome findings may indicate that there is a shortage of knowledge or a lack of shared understanding of business growth plans between the DFIs and the entrepreneurs.

VI. The propositions for development finance

Tables 6.49 to 6.60 present the results of the participants' opinions on development finance suitable for small businesses in South Africa.

a) High DFI loan prices need to be developmental

Table 6.49: High DFIs' loans must be developmental

	Frequency	Percent
Disagree	15	5
Neutral	54	17.9
Agree	195	64.8
Strongly agree	37	12.3
Total	301	100

Source: Author's own compilation

It is evident from Table 6.49, that the majority (77.1%) of the respondents are of the opinion that the high prices of the DFIs' loans must be developmental. Of the respondents, 17.9% were neutral while only 5% disagreed.

Table 6.50 presents the perceptions of the respondents regarding DFI loan prices in terms of employment.

Table 6.50: DFI loan prices must reflect employment factor

	Frequency	Percent
Strongly disagree	3	1
Disagree	42	14
Neutral	94	31.2
Agree	145	48.2
Strongly agree	17	5.6
Total	301	100

Source: Author's own compilation

The results in Table 6.50 show that 53.8% of the respondents either agree or strongly agree that DFI loan prices need to reflect employment factors for loans to be developmental; followed by 31.2% who were neutral and 15% who either disagreed or strongly disagreed.

b) DFIs' loans and gender

Table 6.51 shows the results of responses of the participants regarding the prices of the DFIs and gender disparity.

Table 6.51: DFIs' loan prices must be accommodative of gender disparity

	Frequency	Percent
Disagree	17	5.6
Neutral	61	20.3
Agree	206	68.4
Strongly agree	17	5.6
Total	301	100

Source: Author's own compilation

The results show that the majority of the respondents (74%) either agreed or strongly agreed that the loan prices of the DFIs be accommodative of gender disparity, followed by 20.3% who were neutral and 5.6% who disagreed.

c) DFI loan prices and development

Table 6.52: DFI loan prices must factor-in development agenda

	Frequency	Percent
Strongly disagree	11	3.7
Disagree	50	16.6
Neutral	30	10
Agree	197	65.4
Strongly agree	13	4.3
Total	301	100

Source: Author's own compilation

Table 6.52 shows that 69.7% of the respondents either agreed or strongly agreed that the DFIs' loan prices must factor-in the development agenda, while 10% were neutral and 20.3% either disagreed or strongly disagreed.

d) Loan prices and growth

Table 6.53 displays the results of the participants' responses regarding the DFI loan prices and business growth.

Table 6.53: DFI loan prices must to reflect growth factor

	Frequency	Percent
Strongly disagree	8	2.7
Disagree	41	13.6
Neutral	28	9.3
Agree	205	68.1
Strongly agree	19	6.3
Total	301	100

Source: Author's own compilation

Table 6.53 shows that 74.4% of the participants agreed and strongly agreed that the DFIs' loan prices must reflect the growth factor; while 9.3% were neutral; and 16.3% either disagreed or strongly disagreed.

e) Credit guarantee schemes and development loan prices

Table 6.54 displays the results of the participants' responses with regard to the effect of credit guarantee schemes on development loan prices.

Table 6.54: Credit guarantee schemes need to reduce loan prices

	Frequency	Percent
Strongly disagree	7	2.3
Disagree	44	14.6
Neutral	30	10
Agree	210	69.8
Strongly agree	10	3.3
Total	301	100

Source: Author's own compilation

From Table 6.54, it can be seen that the majority (73.1%) of the participants agreed and strongly agreed that credit guarantee schemes need to reduce development loan prices, while 16.9% disagreed and strongly disagreed, and only 10% were neutral.

f) Structural repayments and repayments defaults

Table 6.55 presents the results of the participants' responses with regard to the approaches to loan repayments to reduce incidents of default by entrepreneurs.

Table 6.55: Industry's structural-based repayment approach can reduce defaults

	Frequency	Percent
Strongly disagree	3	1
Disagree	54	17.9
Neutral	64	21.3
Agree	152	50.5
Strongly agree	28	9.3
Total	301	100

Source: Author's own compilation

The results from Table 6.55 reveal that 59.8% of the respondents either agreed or strongly agreed that industry's structural-based repayment approach is developmental and can reduce bad loans. Of the respondents, 21.3% were neutral, while 18.9% either disagreed or strongly disagreed.

g) Stokvels versus banks

Table 6.56 presents the results of the participants' responses with regard to choosing stokvels over banks.

Table 6.56: Stokvels are a better saving platform for development of SMMEs than banks

	Frequency	Percent
Strongly disagree	5	1.7
Disagree	30	10
Neutral	60	19.9
Agree	172	57.1
Strongly agree	34	11.3
Total	301	100

Source: Author's own compilation

According to the results displayed in Table 6.56, 68.4% or the participants either agreed or strongly agreed that stokvels are a better saving platforms for the development of SMMEs than banks, followed by 19.9% who were neutral and 11.7% either disagreed or strongly disagreed.

h) Stokvels and development finance

Table 6.57 presents the results of the participants' responses with regard to stokvels and development finance.

Table 6.57: Stokvels are a form of development finance ideal for small businesses, not RFIs

	Frequency	Percent
Disagree	17	5.6
Neutral	61	20.3
Agree	206	68.4
Strongly agree	17	5.6
Total	301	100

Source: Author's own compilation

Table 6.57 indicates that 74% of the respondents either agreed or strongly agreed that stokvels are a form of development finance ideal for small businesses, while 20.3% were neutral, and 25.9% either disagreed or strongly disagreed.

i) RFIs make the loans of the DFIs even more expensive

Table 6.58 displays the responses of the entrepreneurs with regards to prices of the RFIs.

Table 6.58: RFIs prices make DFIs' loan prices even higher

	Frequency	Percent
Strongly disagree	6	2
Disagree	10	3.3
Indifferent	8	2.7
Agree	130	43.2
Strongly agree	147	48.8
Total	301	100

Source: Author's own compilation

It is evident from Table 6.58 that the entrepreneurs believe that the prices of the RFIs make the DFIs' loan prices even higher, with 92% of them agreeing and strongly agreeing; only 2.7% were neutral; and 5.3% of them disagreed or strongly disagreed.

j) Establishment of an SMME development bank

Table 6.59 shows the results of the participants' responses regarding the establishment of an SMME development bank.

Table 6.59: Establishment of SMME development bank can address the financing gap

	Frequency	Percent
Agree	191	63.5
Strongly agree	110	36.5
Total	301	100

Source: Author's own compilation

The results in Table 6.24.10 show that all the respondents (100%) either agreed or strongly agreed that the establishment of an SMME development bank is necessary to address the financing gap.

k) Stokvels and development bank

Table 6.60 displays the results of the participants' responses regarding the housing of stokvels within the SMME development bank.

Table 6.60: SMME development bank can better house stokvels

	Frequency	Percent
Disagree	37	12.3
Neutral	41	13.6
Agree	161	53.5
Strongly agree	62	20.6
Total	301	100

Source: Author's own compilation

Table 6.60 shows that 74.1% of the respondents either agreed or strongly agreed that an SMME development bank can better house stokvels than banks, followed by 13.6% who were neutral, and 12.3% who disagreed.

6.4 INFERENTIAL STATISTICS

Inferential statistics was used to establish whether the results of the chosen sample are likely to be found in the wider population from which the random sample was drawn. Inferential statistics also allows the researcher to determine if the differences in the results imply that a relationship exists.

6.4.1 Testing internal reliability, internal validity and normal distribution

The following sections focus on the internal reliability, internal validity, as well as the normal distribution tests.

6.4.1.1 Internal reliability of research instrument

To evaluate the internal consistency of the questionnaire, Cronbach's Coefficient alpha was used. A reliability analysis of the questionnaire reveals that Cronbach's alpha is 0.824, as shown in Table 6.61. The value for the questionnaire being above 0.7 indicates that the questionnaire's study variables have internal consistency and reliability.

Table 6.61: Cronbach's Alpha of the 62 items of the questionnaire

Reliability Statistics

Cronbach's Alpha	N of Items
0.824	62

Source: Author's own compilation

6.4.1.2 Validity of research instruments

As illustrated in Table 6.62, a KMO statistic of 0.823 and a Bartlett's p-value of 0.000 on all 62 items were identified, that provided grounds that justified for factor analysis to be performed on the items as a strong correlation structure exists between individual items in the questionnaire.

Table 6.62: KMO and Bartlett's Test

Kaiser-Meyer-Olkin Measure of Sampling Adequacy.		.823
Bartlett's Test of Sphericity	Approx. Chi-Square	12161.303
	Df	1891
	Sig.	.000

Source: Author's own compilation

6.4.2 Factor analysis

Factor analysis is performed for two main reasons: (i) data reduction; and (ii) structure detection (Zimkund, 2003; Cooper & Schindler, 2014). Factor analysis was performed to determine if individual questions contributed or loaded onto the dimensions that appear in the questionnaire. An Exploratory Factory Analysis (EFA) was used to identify the hidden constructs which may or may not be apparent from direct analysis.

Before the factor analysis was done, the following tests were done: the p-value of the Bartlett test was done. The p-value was found to be (0.000) which is smaller than 0.05, then the correlation structure of the construct was found to be strong enough to conduct a factor analysis; and the Kayiser-Meyer-Olkin (KMO) measure of sampling adequacy was also conducted to test for correlation between each item within the dimensions of the questionnaire. A KMO value towards 1 also implied a strong enough correlation structure (Yong & Pearce, 2013).

To determine the number of factors, the following steps (as stated in Section 5.6.2.1) were followed:

- Cumulative explained by factors must be greater than (>) 60%
- Eigen values must be greater than (>) 1
- A significant decline in the screen plot

Number of factors/dimensions

Factor analysis was performed and 17 constructs were identified, being the factors that had Initial Eigen values greater than 1 at cumulative 70.24% of Rotation Sums of Squared Loadings. However, with the help of the scree plot shown in Figure 6.13, only nine constructs were considered for this analysis; the other eight dimensions were eliminated for two reasons: either (i) their factor loading showed more values less than 0.3, which shows a weak relationship between the variables and constructs/ factors; or (ii) they loaded with fewer items to rely on. Moreover, those with less than 0.3 factor loading were cross-loading items and showed a higher than 0.3 factor loading value on other constructs.

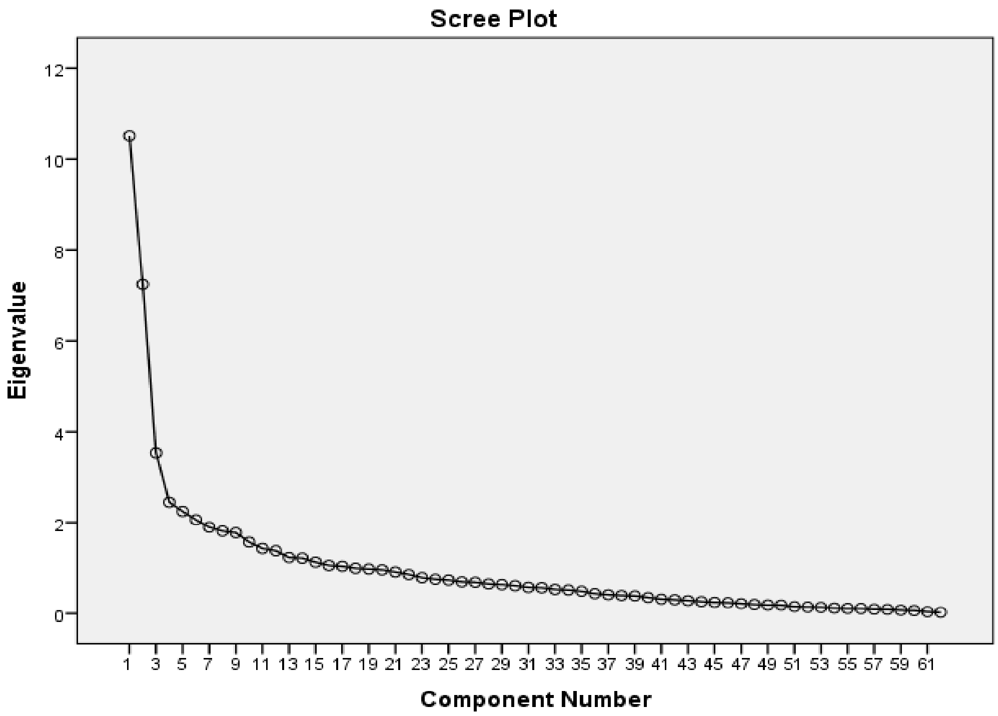


Figure 6.13: Scree plot for factor analysis

Source: Author's own compilation

Thereafter, factor analysis was performed on individual constructs that have adequate correlation between its items. Table 6.63 below illustrates the subsequent factor analysis to test structural validity for each construct/dimension.

Table 6.63: Structure validity for individual dimensions

Section	Dimension	KMO statistic	Bartlett's p-value	Cumulative % of variance explained
C1	Development financing programmes (11 items)	.929	0.000	65.943
C2	Business performance and growth strategies (10 items)	.922	0.000	70.549
C3	DFIs' support programmes (4)	.845	0.000	55.286
C4	Development finance (5)	.637	0.000	58.040
C5	Bridge finance gap (15)	.813	0.000	60.728
B6	DFIs' interest rates (7)	.835	0.000	63.400
C7	DFIs' loan rationing (5)	.897	0.00	66.002
C8	Small business development bank (4)	.978	0.000	68.575
C9	Stokvels and development finance (4)	.993	0.000	71.055

Source: Author's own compilation

Table 6.64: Factor analysis

Statements	Factor1	Factor2	Factor3	Factor4	Factor5	Factor6	Factor7	Factor8
C1.1	**0.855**							
C1.2	**0.840**							
C1.3	**0.828**							
C1.4	**0.806**							
C1.5	**0.805**							
C1.6	**0.795**							
C1.7	**0.788**							
C1.8	**0.767**							
C1.9	**0.731**							
C1.10	**0.783**							
C1.11	**0.575**							
C2.1		**0.889**						
C2.2		**0.880**						
C2.3		**0.879**						
C2.4		**0.858**						
C2.1		**0.855**						
C2.2		**0.848**						

Statements	Factor1	Factor2	Factor3	Factor4	Factor5	Factor6	Factor7	Factor8
C2.3		0.825						
C2.4		0.743						
C2.5		0.705						
C2.6		0.699						
C3.1			0.774					
C3.2			0.771					
C3.3			0.738					
C3.4			0.685					
C4.1				.772				
C4.2				.759				
C4.3				.607				
C4.4				.607				
C4.5				.618				
C5.1					.746			
C5.2					.746			
C5.3					.726			
C5.4					.726			
C5.5					.726			
C5.6					.723			
C5.7					.723			
C6.1						.720		
C6.2						.722		
C6.3						.727		
C6.4						.727		
C6.5						.725		
C6.6						.730		
C6.7						.730		
C6.8						.730		
C6.9						.731		
C6.10						.739		
C6.11						.734		
C6.12						.737		
C6.13						.736		
C7.1							.599	
C7.2							.990	
C7.3							.574	
C7.4							.574	
C8.1								.629
C8.2								.640
C8.3								.640
C8.4								.629

Statements	Factor1	Factor2	Factor3	Factor4	Factor5	Factor6	Factor7	Factor8
C9.1							0.802	
C9.2							0.800	
C9.3							0.692	
C9.4							0.441	
C9.5							0.397	

Source: Author's own compilation

Table 6.64 displays the grouping of the 9 factors that were identified with a factor loading greater than 0.3. The values for each factor are all greater than 0.3 indicating that strong relationships exist between factors and variables.

Internal consistency was also evaluated for each of the factors and the results are illustrated in Table 6.65 below.

Table 6.65: Reliability statistics for individual dimensions

Section	Identified factors	Cronbach Alpha
C1	Development financing programmes (11 items)	0.728
C2	Business performance and growth strategies (10 items)	0.795
C3	DFIs' support programmes (4)	0.603
C4	Development finance (5)	0.782
C5	Bridge finance gap (15)	0.885
C6	DFIs' interest rates (7)	0.785
C7	DFI loan rationing (5)	0.798
C8	Small business development bank (4)	0.659
C9	Stokvels and development finance (4)	0.701

Source: Author's own compilation

Table 6.28 presents the reliability statistics for the identified factors. Cronbach Alpha for every individual factor is above the lower limit of acceptability, 0.6. The results therefore, show that the questionnaire (Sections C1, C2, C3, C4, C5 and C6) as used in this study have a high level of reliability.

6.4.3 T-Test: Gender

The t-test is used to determine whether there is a significant difference in the sample means between two groups. The main purpose of the t-test is to establish the probability that the observed relationship is due to a sampling error. Levene's test was used to test the equality of variances. In this study, the t-test was used to determine whether or not there is a significant difference in the perceptions of gender groups (male and female entrepreneurs in Tshwane) with regard to development finance, loan pricing, finance gap reduction, business growth strategies, business performance, development bank and stokvels. The results are displayed in Table 6.66.

Table 6.66: Gender differences of Tshwane entrepreneurs' perceptions of SMME development financing by the DFIs

Independent Samples t-test							
		Levene's Test for Equality of Variances		**t-test for Equality of Means**		
		F	**Sig.**	**t**	**df**	**P-Value**
Growth strategies	Equal variances assumed	0.441	0.507	-0.836	299	0.404
	Equal variances not assumed			-0.831	271.808	0.407
Loan prices	Equal variances assumed	1.845	0.175	-1.114	299	0.266
	Equal variances not assumed			-1.108	272.414	0.269
Development finance	Equal variances assumed	0.653	0.42	-0.5	299	0.617
	Equal variances not assumed			-0.495	267.626	0.621
Finance gap	Equal variances assumed	2.241	0.135	0.586	299	0.558
	Equal variances not assumed			0.594	289.051	0.553
Business growth	Equal variances assumed	2.43	0.12	1.039	299	0.300
	Equal variances not assumed			1.045	283.448	0.297
Performance	Equal variances assumed	0.077	0.781	0.504	299	0.615
	Equal variances not assumed			0.502	273.414	0.616
Stokvel banking	Equal variances assumed	0.032	0.859	0.243	299	0.808
	Equal variances not assumed			0.242	275.302	0.809

Independent Samples t-test						
		Levene's Test for Equality of Variances		t-test for Equality of Means		
		F	Sig.	t	df	P-Value
SMME development bank	Equal variances assumed	1.94	0.165	-0.807	299	0.42
	Equal variances not assumed			-0.802	270.769	0.423

Source: Author's own compilation

Table 6.66 shows that the t-tests for gender perceptions regarding the impact of development finance; rationing of loan prices; finance gap reduction; increased finance access; the use of stokvels, and the establishment of an SMME development bank all have p-values above 0.05. The p-values that are above 0.05 imply that there are no significant differences between gender groups towards these variables.

For example, the t-test for gender perceptions on the impact of development finance by DFIs shows that males have a mean score of 3.6 and females have a mean score of 3.71. The p-value (2-tailed) is 0.558, the p-value that is greater than 0.05 indicates that there is no significant difference between mean development finance scores of males and females at a 95% level of confidence. One of the assumptions of the t-test is equal variances. The Levene's Test is 0.135, which is larger than 0.05, indicating, therefore, that the variances are equal.

The conclusion, therefore, is that both male and female entrepreneurs have similar views and perceptions with regard to development financing of small businesses. The DFIs can be assured that that there should not be any significant difference between the perceptions of male and female entrepreneurs with regards to development financing by the DFIs.

6.4.4 Analysis of variance

Analysis of variance (ANOVA) was used to compare more than two samples which the t-test could not perform. Moreover, unlike the t-test, ANOVA imposes no restrictions on the sample means. Therefore, ANOVA was performed to determine the difference in the perceptions of the entrepreneurs in terms of race, gender, age groups, level of education, and the age of their businesses, regarding the impact of DFI financing.

Table 6.67: ANOVA test for entrepreneurs' perceptions on impact of the DFIs' financing

		Sum of Squares	Df	Mean Square	F	P-Value
Age	Between Groups	2.916	4	0.729	1.147	0.334
	Within Groups	188.081	296	0.635		
	Total	190.997	300			
Race	Between Groups	2.4	4	0.6	0.462	0.763
	Within Groups	384.238	296	1.298		
	Total	386.638	300			
Education	Between Groups	5.663	4	1.416	1.197	0.312
	Within Groups	350.151	296	1.183		
	Total	355.814	300			
Period in business	Between Groups	5.171	4	1.293	1.424	0.226
	Within Groups	268.63	296	0.908		
	Total	273.801	300			

Source: Author's own compilation

From Table 6.67, it can be seen that all the P-values are greater than 0.05, therefore there is no significant difference between the perceptions of the entrepreneurs across biographical variables with regard to the impact of development financing by the DFIs.

Table 6.68 represents the results of the ANOVA test for the perceptions of the entrepreneurs belonging to different groups regarding the impact of the finance gap reduction.

Table 6.68: ANOVA test for entrepreneurs' perceptions on finance gap reduction

		Sum of Squares	df	Mean Square	F	P-values
Age	Between Groups	14.291	30	0.476	0.728	0.851
	Within Groups	176.705	270	0.654		
	Total	190.997	300			
Race	Between Groups	26.708	30	0.89	0.668	0.908
	Within Groups	359.93	270	1.333		
	Total	386.638	300			
Education	Between Groups	37.997	30	1.267	1.076	0.366
	Within Groups	317.817	270	1.177		
	Total	355.814	300			
Period in business	Between Groups	37.881	30	1.263	1.445	0.068
	Within Groups	235.92	270	0.874		
	Total	273.801	300			

Source: Author's own compilation

Table 6.68 shows that the p-values of the F-tests are all greater than 0.05, therefore there are no significant differences between the perceptions of the entrepreneurs across biographical variables with regard to finance gap reduction.

ANOVA tests on DFIs' non-financial programmes (support programmes)

Table 6.69 presents the results of the perceptions of the entrepreneurs across demographic variables regarding DFIs' support programmes drag.

Table 6.69: ANOVA test for entrepreneurs' perceptions on DFIs' support programmes

		Sum of Squares	df	Mean Square	F	P-values
Age	Between Groups	2.676	10	0.268	0.412	0.94
	Within Groups	188.32	290	0.649		
	Total	190.997	300			
Race	Between Groups	11.497	10	1.15	0.889	0.544
	Within Groups	375.141	290	1.294		
	Total	386.638	300			
Education	Between Groups	7.951	10	0.795	0.663	0.759
	Within Groups	347.863	290	1.2		
	Total	355.814	300			
Period in business	Between Groups	16.399	10	1.64	1.848	0.052
	Within Groups	257.402	290	0.888		
	Total	273.801	300			

Source: Author's own compilation

The results in Table 6.69 show that all the P-values are greater than 0.05, therefore there is no significant differences between the perceptions of the entrepreneurs across biographical variables with regard to the impact of non-financing programmes by the DFIs.

6.4.5 Pearson Coefficient

The Pearson Coefficient was to assess the strength of the identified association between the variables.

a) Correlation between development finance and business performance

Table 6.70 presents the correlation between development finance and business performance.

Table 6.70: Pearson correlation between development finance and business performance

Development Finance	Pearson Correlation	1	.673**
	P-value		0.003
	N	301	301
Performance	Pearson Correlation	.673**	1
	P-value	0.003	
	N	301	301

** Correlation is significant at the 0.01 level (2-tailed).

Source: Author's own compilation

Table 6.70 shows that the correlation between development finance and business performance has a p-value of 0.003 which is less than 0.05. This result implies that development finance and business performance have a statistical significant correlation. The positive (+) sign implies both variables have a positive correlation and a Pearson product correlation coefficient r value of .673, which indicates that there is a low correlation between both variables. The entrepreneurs believe that receiving good development finance is accompanied with good business performance.

b) Correlation between business performance and DFIs' loan pricing

Table 6.71 present the results of the Pearson's correlation between business performance and the DFIs' loan pricing (loan price rationing) variables.

Table 6.71: Pearson's correlation between business performance and DFIs' loan pricing

		Performance	**DFIs' Pricing**
Performance	Pearson Correlation	1	.396**
	P-value		0.000
	N	301	301
DFIs' Pricing	Pearson Correlation	.396**	1
	P-value	0.000	

	N	301	301

** Correlation is significant at the 0.01 level (2-tailed).

Source: Author's own compilation

The results displayed in Table 6.71 show the correlation between business performance and the DFIs' loan pricing has a p-value of 0.000, which is less than 0.05. This finding means that business performance and DFIs' loan pricing have a statistically significant correlation. The positive (+) sign indicates that both variables have a positive correlation and the Pearson's product correlation coefficient r value of 0.396 indicates a medium correlation between business performance and the DFIs' loan pricing variables. The entrepreneurs believe that good business performance is accompanied by good DFIs' loan pricing; and as DFIs' loan pricing improves, business performance also improves.

c) Correlation between DFIs' loan prices and business performance

Table 6.72 displays the results of the Pearson's correlation between the DFIs' loan prices and business performance variables.

Table 6.72: Pearson's correlation between loan prices and business performance

Loan Prices	Pearson Correlation	1	-.743*
	P-value		0.013
	N	301	301
Performance	Pearson Correlation	-.743*	1
	P-value	0.013	
	N	301	301

* Correlation is significant at the 0.05 level (2-tailed).

Source: Author's own compilation

Table 6.72 shows that the correlation between the DFIs' loan prices and business performance has a p-value of 0.013 which is less than 0.05. The result indicates that there is statistically significant correlation between the DFIs' loan prices and business performance. The Pearson's product correlation coefficient r value of -.743, indicates a strong correlation between the two variables. The negative (-) sign indicates that both variables have a negative correlation. The entrepreneurs believe that high loan prices go along with low business performance, and loan prices that are low go along with high business performance.

d) Correlation between DFIs' loan prices and development finance variables

Table 6.73 displays the results of the Pearson's correlation between the DFIs' loan prices and development finance variables.

Table 6.73: Pearson Correlation between loan prices and development finance

Loan Prices	Pearson Correlation	1	.710**
	P-value		0.000
	N	301	301
Development Finance	Pearson Correlation	.710**	1
	P-value	0.000	
	N	301	301

** Correlation is significant at the 0.01 level (2-tailed).

Source: Author's own compilation

The results in Table 6.73 show that the correlation between the DFIs' loan prices and development finance has a p-value of 0.00 which is less than 0.05. This finding means that loan prices and development finance have a statistically significant correlation. The Pearson's product correlation coefficient r value of 0.710 indicates that there is a strong correlation between these two variables. The positive (+) sign indicates that both variables have a positive correlation. The entrepreneurs believe that good DFIs' loan prices go along with increased development finance.

6.5 SECTION E

The current section of is based on the key themes that arose from open-ended questions in the questionnaire.

The findings from the in-depth interviews with the entrepreneurs were categorised under the following three key themes: Performance, challenges and suggestions/ solutions that either directly or indirectly relate to the development financing, as shown in Figure 6.14 below.

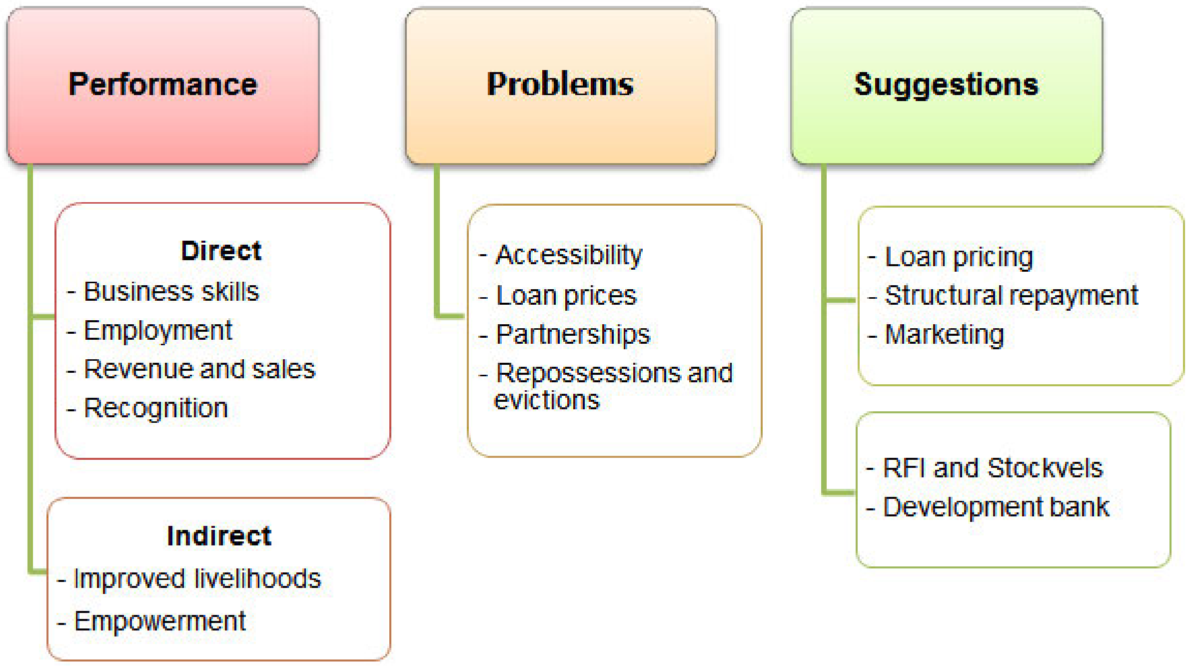


Figure 6.14: Key themes of Phase 2

Source: Author's own compilation

6.5.1 Performance

The results revealed that support through development finance (both financial and non-financial programmes) by the DFIs have led to increased performance in small businesses in Tshwane Metropolitan Municipality. Under the key theme **Performance,** the two sub-themes emerged: direct performance and indirect performance as shown in Figure 6.14. Direct performance was found to be directly linked to the businesses, while indirect performance was found to be linked to the entrepreneurs themselves.

6.5.1.1 Direct performance (business benefit)

i) Business skills

The respondents have indicated that their business skills have improved through the support of the DFIs, for example, one of the respondents stated that he has learned to keep a record of all business activities, which was not the case prior to receiving the support: "*…receiving support from the DFI has helped me change the way I was doing things in my business. I keep record of everything that happens in the business…in the past, I just ignored small things and took notice of major matters, even those, I did* *not always keep written record of them but at least I would write them in my head, I do not forget easily…"* Another respondent confirmed the statement by the DFIs that they do provide relevant training to the entrepreneurs as part of development support for small businesses: *"…after the application process, we were given some training…no, that was before I received the actual financing…I think the first round took about some few days to a week…then another guy took us through another workshop…* [she opens her eyes wide and looks up], *"…yes, it was another training… it was not as long as the first one*… *all in all, there were three parts of separate times…"*

Another revelation related to improved business skills was that the entrepreneurs are able to separate personal matters from the business, for example, one of the respondent reported: "…*I am taught that I need to earn a salary from the business and only utilise that for personal use…you cannot just take money from the business whenever a need arises… during the workshop we were strongly advised on this and we have realised how this affect the business*…*Yes, I used to think all the profit I make is for my own personal use and when money run short at the business I would struggle to fix that …I did not know that the money still belonged to the business*…''

ii) Employment, increased sales and revenue

There was a consensus between the respondents that the creation of employment was one of the results of development financing by the DFIs. The respondents believe that the development support by the DFIs has enabled them to create some employment: "*…I now have a shop assistant employed on a permanent basis… initially, I was forced to close the shop whenever I went for stock… yes, the financing has enabled me to make more money and am able to pay her a wage…"*

Another respondent mentioned that he received a bricklaying machine and employed two people: *"…I have received the machine from the DFI and the production has increased and sales also increased that I had to employ two more people to help me…I am paying for the second machine myself and hopefully I will get at least an additional guy…I do not know at the moment…but I think one more will be needed…"*

"I have employed one lady permanently and three other ladies are temporary employees that I used during busy periods…the saloon is working well but we are many doing similar business…competition is a little difficult at the moment…but during busy periods, everyone makes lots of money…"

iii) Marketing and recognition

The respondents believe that through the support of the DFIs, their businesses are recognised. For example, the respondents reported that they were helped to register their businesses and to open bank accounts: "…*My business now is legal, it is a registered cc (meaning a close corporation) and it is registered with SARS (revenue service) and has a bank account. These documents are required when you want to be a service provider*…*I am now in the data base for a number of departments…they call us if there is business for us…"*

The DFIs assist with marketing support systems for small businesses:

"…With the help from the NYDA, my business has a website and I am also registered under some other websites…you can also tell your friends from outside Pretoria that this B&B is just a click away [joking]. Most people that come to the B&B make online reservation…I am quite happy with the support …"

6.5.1.2 Indirect performance

i) Livelihoods

The second sub-theme categorised under performance was related to the entrepreneurs' personally. The entrepreneurs believe that the DFIs' support has increased their livelihoods: "…*I am able to pay for my children's schooling and institutions of higher learning…you know how difficult it is to get bursaries these day*… "

"…things have changed in the house; I also contribute to the household expenses with the salary I get from the business. I used to depend on my husband for everything, it was not easy because we have a big extended family and he was the only one working… I work with my sister-in-law and another lady who is full-time at my kitchen …she also cooks well [she smiles]…no my sister-in-law only helps when I have to cater for many people…"

ii) Empowerment

The entrepreneurs believe that financing by the DFIs has empowered them. For example, one entrepreneur stated that she does not have to depend on others for basic needs: "…*I buy my own food, clothes and paying…I school my children*…"

6.5.2 Challenges and solutions

The results also revealed that there are challenges (the second theme) identified by the entrepreneurs which can limit the successful implementation of development financing by the DFIs. Along with the challenges, the entrepreneurs made some suggestions of how these challenges can be resolved (third theme).

i) Development loan pricing

The study discovered that while development financing by the DFIs increases business performance and reduces some of the challenges of access to finance by small businesses, the entrepreneurs believe more can still be done. The entrepreneurs believe that the prices of development loans must be reflective of the development agendas such as employment, poverty and inequality (black, female and youth) that the government entrusts small businesses with: "…*interest they charge is too high, it affects the cash flow of the business…how are they developmental if the charge us so much…?"* Although the RFIs are believed to be very convenient and supportive, they are said to charge even higher rates.

ii) Repossessions and evictions

The entrepreneurs believe that repossessions of property and evictions from residential homes as ways of recovering bad loans are both not developmental: "…*people are repossessed of their properties if they fail to pay back the money…how is that developmental…? Sometimes the situation is beyond our control and the business may not generate enough cash flow as anticipated…look at the situation of drought in the past two years, how are we supposed to make money when there is no production due to natural conditions*..."

One of the entrepreneurs stated: *"We were told that our houses will be used for recovery of debt if we fail to meet our financial obligations…fortunately this has never* *been the case because the business is still performing well...but this was discussed we got the loan from XXX …" [she mentioned the name of the DFI].*

iii) Industry structural repayment

The entrepreneurs believe the DFIs are not being developmental by attaching the residential properties of applicants as indemnity for non-repayment. The entrepreneurs instead suggest that structural repayments be considered as options: *"…due to industry structural fluctuations some people may default, these should be considered in dealing with handling development finance matters…"*

Another respondent suggested: *"…monthly repayments are not applicable to every industry, my bed and breakfast works very well during the festive periods, I used to experience problems when I was paying the bank loan, the DFIs must consider industry's performance when structuring the repayment plans, otherwise people are caught between the rock and a hard place…"* The respondents agree that industries have different structural performance, and therefore, repayments to the DFIs' should be linked to the individual industry's performance basis and not on a monthly basis as in the case of financial markets' practices.

iii) Increased accessibility and marketing

The entrepreneurs believe that the DFIs are not accessible enough, stating that the DFIs are based in the cities and it is costly for the entrepreneurs to reach the DFIs offices, citing costs such as transport and time. Other entrepreneurs stated furthermore that they did not have the information about different financing options available from different DFIs: "… *they need to be accessible enough for everyone to know about their offerings…they need to advertise about their programmes…many people do not know that they can get assistance from the government…"* Another concern regarding accessibility identified was unsuccessful telephone calls: *"…calling the DFIs is always a problem, either no one answers the call or you are transferred from one officer to the other and never get to the right person…"*

iv) Legalisation or official recognition of stokvels

When asked to explain their choice of stokvels as the preferred method of saving and lending for small businesses, the findings revealed that the entrepreneurs believe that with stokvels: *"…members develop a saving culture and build investment empires* *together…unlike banks which use our savings to grow their own businesses and yet we struggle to get loans when we need…"* The other finding from this aspect was that the entrepreneurs believe that for the purposes of development, stokvels can be used in place of current retail financial intermediaries: "…*the DFIs can use stokvels to channel development funds instead of utilising the retail intermediaries (RFIs) which make the DFIs' loan even more expensive*…" The respondents stated that stokvels are more **developmental** and **structural payments** were cited as the main reasons for the choice: *"…members are not confined to monthly repayments, they are allowed to pay back the money according to the performance of their businesses (structural payment), as long as it is within the agreed term and making membership contribution successfully*…". Other respondents stated that there is an opportunity for their money to grow when saved with stokvels: *"…saved money is loaned out to other people and earns the owners some interest which helps the money to grow and made available for other members…*" The entrepreneurs have a sense of ownership of their invested money as opposed to be benefiting the financial institution: *"…when one saves with stokvels, one gets all their money plus interest accumulated*…"

v) Establishment of an SMME development bank

The establishment of an SMME development bank proved to be highly desired by the entrepreneurs: "…*small business development bank is required because other banks do not provide services to small businesses*…" Other reasons cited for the suggestion of development bank include housing all the development finance products under one roof: "…*instead of having the DFIs at different places, having them under one roof can be more convenient* …" The establishment of a small business development bank was also found to be a more applicable and appropriate bank where stokvels can be accommodated: "…*stokvels can work better if they work through the development bank…large used amounts of money are often at risk but keeping it at banks is not favourable also…"*

6.6 CONCLUSION

This chapter was based on the presentation, analysis and interpretation of the findings of the empirical study by the researcher. The first part covered the data analysis of

Phase 1 of the study which is based on the qualitative paradigm. Data was transcribed verbatim from the open-ended in-depth interviews with the research participants. The transcriptions were coded and grouped into the categories. The categories were matched to the six themes which were predetermined together with four additional new themes that emerged. The themes were discussed in detail to give meaning with regard to what they imply to this research relative to the theoretical chapters. The second part of the chapter discussed the findings in relation to the objectives of the second part of the analysis based on quantitative paradigm, consisting of a survey study. The purpose of this second part was to present the Phase 2 data that was gathered from the entrepreneurs from Tshwane Metropolitan Municipality in the province of Gauteng. The data collected from the structured questionnaire as well as open-ended questions were analysed with the aid of the computer program SPSS version 24. The analytic tools that were used include, frequencies, factor analysis, t-test, ANOVA, Pearson's product correlation coefficient and thematic analysis for the open-ended questions, which were presented in five sections. The next chapter discusses the main findings of the study.

CHAPTER 7: DISCUSSION OF FINDINGS

7.1 INTRODUCTION

In the context of small business growth and development in South Africa, it was apparent that development finance is a critical issue that needs to be given attention, particularly in line with economic growth; unemployment reduction; and the eradication of poverty and inequality. Although much research and debates have been documented around the issue of financing for small businesses, the continuing high failures rates in the sector on account financing indicate that much still needs to be done for the development of this sector. Given the number of contributing factors that make financing a much bigger problem than small businesses can handle, all stakeholders need to have a common ground in order to come up with workable solutions against these challenges. While financing of small businesses is a global challenge that also affects developed countries, the dilemma is even worse for developing economies.

After the data analysis and presentation of the empirical results of this study in the previous chapter, the current chapter focuses on a discussion of the results presented in the last chapter.

The main objective of this study was to explore the role of the DFIs in financing small businesses in South Africa since the policy for small business development was enacted in 1996. The chapter attempts to establish the extent to which the researcher has been able to achieve this objective as stated in Chapter 1, along with the research aim:

> *Participation of the DFIs in financing small businesses leads to sustainable development of the SMME sector.*

In attempting to address the main aim, the researcher will evaluate the findings of each of the objectives identified in the study, which in turn forms the basis for the conclusions and recommendations. The extent to which the empirical findings address the objectives, defines the extent to which the study has achieved the research aim.

7.2 THE MAIN FINDINGS OF THE STUDY & RECOMMENDATIONS

This section discusses the main findings of the study with the most relevant recommendations. The participation of the DFIs in financing small businesses can contribute to the growth and development of small businesses in South Africa. The main intention of this study was to explore the role of the DFIs in financing small businesses in South Africa. In order to achieve this aim, the study investigated how participation of the DFIs in the financing of small businesses impacts on the growth and sustainable development of their businesses.

7.2.1 Financial and non-financial programmes

In addressing the following objective:

> *To explore the programmes the DFIs have to finance small businesses in South Africa to ensure the growth and development of the sector.*

The results in Phase 1 revealed that the DFIs have both financial and non-financial programmes that are tailored to address the financing needs of small businesses in South Africa (Table 6.4).These findings were supported by the results of Phase 2 where the respondents (Tables 6.31 - 6.34) confirmed that they were the beneficiaries of different development programmes (both financial and non-financial) offered by the DFIs. The results confirmed the literature views of Masuke *et al*. (2004); and Mazanai and Fatoki (2011) that the DFIs have been established to provide development funding to small businesses, mainly to help address some of the challenges facing small businesses, including access to finance, and high failure rates (Fatoki, 2014)

The results revealed that the DFIs work in partnership with other institutions wherever is possible in their pursuit to provide developmental support to the DFIs. In Section 6.2.11 the DFIs have stated that they do make referrals to other institutions that can offer relevant support in cases where the required support is outside the parameters of the DFI. The results of the survey also confirmed that 36.1% of entrepreneurs were referred to another DFI for support (Table 6. 27)

7.2.2 Bridging the financing gap for small business

This sub-section incorporates the finding of the two objectives:

Objective 2: *To explore the extent to which the DFIs bridge the financing gap that exists in the financial markets for small businesses; and*

Objective 7: *To investigate the perceptions of the entrepreneurs on the role of the DFIs' financing support to small business development in terms of bridging the financing gap.*

This section provides the findings that show what the DFIs have done with regards to bridging the financing gap and the perceptions of the entrepreneurs thereof.

a) Elimination of financing obstacles

The literature review highlights that small businesses fail to access finance from financial markets due to among other things, information asymmetry, a lack of tangible assets and lack of a track record (Abor, 2010; Dayal *et al*. 2008; Beck, 2007; Claessens, 2006; OECD, 2006; Mensah 2004; Hashi 2001). However, the results reveal that through financing by the DFIs, some of the identified challenges are eliminated, asserting the view of structuralist paradigm (Mahalabinos, 1953). Small businesses are able to be provided with asset financing, credit guarantee facilities, grants and procurement financing by the DFIs (Figure 6.4.).

- Asset finance and grants eliminate the problem of lack of assets.
- Loans eliminate the problem of creditworthiness and lack of a track record;
- Credit guarantee scheme reduces default risk;
- Procurement finance increases cash flow.

The DFIs also stated that through their support programmes, they assist small businesses to develop relationships with banks, which eliminates the problem of a lack of a track record.

The subsequent findings of the survey reveal that:

- 76.4% of the respondents believe that the DFIs lead to a bank relationship (Table 6.40);
- 61.8% of the entrepreneurs believe that the DFIs' financing increases credit-worthiness (Table 6.42);

- 75.7% of the financed SMMEs believe that development support by the DFIs increases information asymmetry (Table 6.43).
- 73.4% of the entrepreneurs believe that financing by the DFIs reduces the problem of lack of collateral (Table 6.44)
- However, 51.8% of the respondents disagree and strongly disagree that financing by the DFIs through the facility of credit guarantee reduces the risk premium associated with small businesses (Table 6.41).

Establishing bank relationship waives the shortcoming of lack of a track record that Beck and Frame (2005) identify as one of the challenges facing SMMEs.

On assessing whether there is any statistically significant difference in the perceptions of the entrepreneurs across biographical variables, it was found that there are no significant differences between the perceptions of the entrepreneurs across biographical variables with regard to the finance gap reduction, and the results in Table 6.68 revealed that;

- The p-values were greater than 0.05 implying that the groups do not differ significantly.

b) Different DFIs have different target markets

The findings of the study have revealed that different DFIs have been established to exclusively serve a specific target market of small businesses which is considered to be excluded in the financial markets (Section 6.2.3). There is a very minimal duplication (if any) of programmes aimed at similar markets. However on a large scale, every individual DFI is designed in a way that only a specific target market is served specifically by a distinctive DFI. The literature review stated that gender, race and age are some of the distinguishing features of the market excluded by commercial lending. For example (Kon & Storey, 2003; Kim, 2006; Niethammer *et al*. 2007), in Section 2.6 (a) show that women, minority communities and young people are mostly the victims of commercial lending exclusion (Herrington *et al.*, 2017). The empirical study from the survey shows that, blacks, women and youth entrepreneurs are the targeted groups for financing by the DFIs. For example:

- 57% of financed entrepreneurs were women (Table 6.3);
- 27% of young entrepreneurs received financing from the DFIs (Table 6.4); and

- 61% of the funded entrepreneurs were blacks (Table 6.5).

The results provide the proof that the DFIs are not only bridging the financing gap for the financially excluded, but also reducing incidents of inequality (Claessens, 2006; Herrington *et al*., 2017).

- 82% of businesses that were financed were established less than ten years (Table 6.8),

Theory shows that businesses in their growth stages of business life cycle are mostly faced with the challenges of access to finance (Herrington, et al., 2017), and hence they need more development finance. Furthermore, as they are in the development phase of their life cycle, development finance, and not commercial finance, is the most appropriate finance required for business growth.

7.2.3 DFIs' challenges related to financing small businesses

Objective 3: *To examine the limiting factors for the DFIs in financing small businesses.*

Operations of the DFIs are not without challenges. The findings reveal that the main problems associated with the DFIs in achieving the objective of the government are:

- Credit guarantee schemes;
- Financial regulations;
- The prices of the DFIs' loans;
- Marketing.

a) Credit guarantee schemes and RFIs

The DFIs make use of credit guarantee schemes (Section 6.2.7b) to help reduce lending risk challenges that makes loan prices very high for small businesses (Beck *et al.*, 2010; Cowling, 2010; Abor & Biekpe, 2006). However, the findings of the study reveal that the facility does not eliminate the expected problem due to regulations of the banks that the DFIs partner with for facilitating credit guarantee schemes (6.2.7 h) and also the unethical behaviour of some partners (Section 6.2.7 b).

Credit guarantee schemes, as a form of security, are supposed to reduce the risk factor of the loan, but this has not been the case with the use of the instrument in

South Africa. The lender only uses the security on condition that the borrower defaults, which implies that the applicant goes through the normal assessment process and the loan is still priced according to the risk profile of the borrower, which in the case of small businesses, (risk-based pricing) is very high (see Table 2.3). Likewise, as Table 6.3 shows there are entrepreneurs (though very small at 0.7% but worth noting) who do not believe that funding by the DFIs will improve business growth. This might be the group of entrepreneurs that received the DFIs loans through RFIs, given that the DFIs' loan prices through RFIs are very high loan and hence, this group of the entrepreneurs disagreed that the DFIs' funding improves business growth (Section 6.5.2 (ii)).

The DFI has stated that it (the DFI) does not have the complete profile of the recipients of the facility, and only one variable (race) is used in profiling which exposes the funding decision to bias (see Section 6.2.7b) .

The DFI also indicated that the lender (the bank) is solely the decision-maker on who gets the loan and who gets the credit guarantee facility. The findings imply that there is a possibility that the lender misuses the facility by making money out of potentially risky clients.

c) Loan prices and financing regulation

A finance institution that issues loans stated that they are bound by financing regulations operating in the country. SEFA is bound by the pillars of Basel 111 which expects 100% capital requirements. To comply with the regulations, the DFIs are expected to price their loans accordingly (NCR, 2009). The DFIs that issue loans stated that risk-based and cost-based pricing of the loans are used in determining the interest rates charged in the loans. Subsequently, a significant 85.4% of entrepreneurs (Table 6. 38) believe that the interest rates charged by the DFIs are very high (Section 6.5.2. (i)) that they negatively affect the working capital of the businesses and ultimately reduce the performance of the businesses. These results confirm the theory (Section 2.7.2) that both risk- and cost-based models increase the loan prices, especially for the risky small businesses.

The DFIs that issue loans to small businesses stated that the interest charged are based on risk and cost of the loans. Both risk- and cost-based pricing of loans make loans very expensive (Table 2.3) and entrepreneurs strongly agree that DFIs loans are too expensive (see Table 6.35). While the decision is in line with the National Credit Regulation, the former is no different from commercial lending (see Section 2.7.1) as it is more on hedging against default risk and costs, as opposed to the development agenda (Section 2.2.6). The findings imply that the high prices pose a challenge of the reluctance by potential clients (Category C) to approach the DFIs, as has been identified in (Section 2.2.5).

SEFA further stated that they channel their financing through the RFIs, who charge additional interest on the loans offered to the entrepreneurs, implying that the prices of the loans offered by the DFIs are high. This confirms the views of Diette (2000) and Njuguna (2008), who argue that cost-based lending is a function of various elements and all add to the increase of the loan price. The results imply that the high loan prices discourage small businesses from seeking finance from the DFIs, and therefore contradicts the purpose of development finance (Seers, 1969; Hoffmann, 2008) of serving the market that is excluded by the financial markets (Section 2.2.5).

d) Non-performing programmes and low number of applicants

The DFIs have stated that some programmes are not performing as expected, for example, entrepreneurs are not utilising programmes, like franchising by LEDA that is not being utilised (Section 6.2.7d).

This implies that even though the products are available to support small businesses, there are limiting factors that render the latter ineffective, especially in the case of loans which are expected to earn some returns to the DFIs.

DSMD also mentioned the low turnout of applicants for the financial support the department has in place for small businesses. This might be the result of a lack of awareness due to poor marketing.

7.2.4 DFIs’ financing increases business performance

Objective 4: *To explore the perceptions of the entrepreneurs on how financing by the DFIs impacts on the growth of their businesses across demographic variables.*

- The results from the survey prove that financing by the DFIs increases business growth. When asked if DFIs' financing increases business growth, 71.4% of the respondents either agreed or strongly agreed (Table 6.31).

- 64.8% of the respondents either agreed or strongly agreed that financing by the DFIs helped their businesses to create employment (Table 6.32)
- 82.2% of the entrepreneurs either agreed or strongly agreed that DFIs' financing lead to increased sales (Table 6.33).
- Interestingly, with regards to turnover, only 39.2% either agreed or strongly agreed that DFIs' financing increased turnover, while 46.5% were neutral (Table 6.34). The inference to this finding can be attributed to lack of understanding of financial management (lack of management skills)
- Section 6.5.1.1 shows that there was consensus among the respondents that financing by the DFIs increased performance of the businesses.
- Development of websites for small businesses by NYDA (sec 6.2.2 and Figure 6.14) for example confirms what (Fan, 1993 and DTI, 2008) stated that the DFIs are expected to provide marketing support for the entrepreneurs to make them competitive.

To assess if there was any statistically significant difference amongst the respondents across biographical variables with regard to the DFIs' financing on business growth, the results showed that all the p-values were greater than 0.005 (Table: 6.67), implying that there was no statistical difference between the groups of respondents from biographical variables.

The high Pearson's product correlation coefficient of 0.673 in Table 6.70 shows there is a strong relationship, with entrepreneurs believing that receiving good development finance ensures good business performance.

The results confirm the literature that access to finance affect business growth. For example, Bell (2015) mentioned that the World Bank's expectation of 600 million jobs created by small businesses cannot achieved if the problem of access to finance is addressed, implying that employment area of business growth is related to finance. Similarly, Beck *et al*. (2005) show that lack of financial resources limit the business opportunity to attract employees. Gul *et al*. (2010) asserts that small businesses are instrumental in economic recovery by creating employment after global credit crunch which resulted in massive job losses. The results also confirm the view of Sun (2009) that business growth relate to increased sales volumes, profit, output and asset gross.

The non-financial support programmes offered by the DFIs (Section 6.2.2.2 and Table 6.2) are believed by the entrepreneurs to increase business skills (Table 6.37). The results show that the support by the DFIs eliminates the problem identified by Abor (2010) that lack of management and business skills lead to high business failure rates The entrepreneurs have also confirmed that non-financial support has increased their business skills (Table 6.37 and Figure 6.14) and Section 6.4.1.1 (i). Therefore by offering management and business skills to entrepreneurs, the DFIs increase the prospects of success and reduction of failure rates, a potential solution to the identified challenge of skills shortage (Section 2.6.3).

However, the high negative Pearson's product correlation coefficient of -0.743 in Table 6.35, between loan prices and business performance indicates that there is a negative relationship between the two variables, such that when loan prices are high business performance will decline and the opposite holds. The results also confirm the existing debate in the literature that higher loan prices are not favourable for small businesses as they increase the financial costs (Table 2.3) (Beck *et al.*, 2005; Abor & Biekpe, 2006; Beck *et al.,* 2008)

7.2.5 Propositions for development finance

Objective 5: *To investigate the propositions entrepreneurs have for small business development finance*

The DFIs have indicated that that development financing is meant to positively affect the growth of small businesses. The results showed that employment and development sustainability (continuity) are the main growth agendas for the financing of the business by the DFIs (Section 6.2.8) to target mainly employment.

The findings of phase two reveal that:

- 77.1% of the respondents believe that development loans need to be developmental (Table 6.49);
- 53.8% of the entrepreneurs are of the opinion that development finance must be linked to employment creation (Table 6.50);
- According to 74% and 74.4% of the entrepreneurs, development finance loan prices must factor-in gender disparity which is skewed towards women and business growth prospects (Tables 6.51 and 6.52 respectively).

- 73% believe that credit guarantee schemes need to reduce loan prices (Table 6.54);
- 74% of the respondents believe that stokvels are developmental and not the RFIs (Table 6.57)
- 92% are of the opinion that the RFIs' prices make the DFIs' loans even more expensive (Table 6.58)
- 100% of the entrepreneurs agree that establishment of an SMME development bank is necessary (Table 6.59)

The DFIs have agreed that they still use cost-based pricing, their loan prices are higher than those charged by the financial markets. Therefore the DFIs; loan prices, unlike bank loan prices which are targeting profits, must subsequently reflect the former's target. Unlike commercial lending which uses monthly loan repayments in pursuit to secure members' funds as well as to make profits, development finance must use structural payments depending on the individual industry in which the business operates.

a) Stokvels

The literature review chapter (Section 2.5) shows that start-up businesses depend on a number of sources for start-up capital. However, this study reveals that stokvels are also considered as one of the main sources of start-up capital for small businesses in South Africa. Although the findings of the current study confirmed literature to be true that family and/ or personal savings are traditionally primary sources of finance, however, in the case of small businesses in Tshwane, the entrepreneurs rely mostly on the DFIs and stokvels as the major sources of start-up finances. Interestingly, although banks are believed to be the main sources of finance (Section 2.5), this study reveals that in South Africa, banks are the least likely to be considered for financing by the entrepreneurs. This discovery may be evidence that a gap does exist in the financial markets for small businesses

b) Relationship-based lending and stokvels

One of the prerequisites to access development finance from the DFIs is for the business to have a bank account (Table 6.40). While this is a strategy to help small businesses establish relationship with the banks (relationship banking) (Njuguna, 2008; King, 2007; Diette, 2000; Basu & Rolfes, 1996).), the entrepreneurs believe doing business with the banks during the developmental stages of the business (within first five years of establishment) does not benefit small business and therefore they are not willing to save with the banks. The entrepreneurs rather believe that stokvels are more developmental (Table 6.57) for small business than highly regulated banks (Table 6.56). Although the DFIs strongly recommend (a requirement for lending) that small businesses establish relationship with banks, which has the potential to be translated into the relationship-based pricing (Table 2.3) of business loans in future, small businesses opt to save money within stokvels instead. The benefit of relationship lending (Udell, 2008) is therefore, potentially forfeited.

c) Establishment of a SMME development bank

Literature shows that small businesses are mostly susceptible to failure, especially during the first year of existence, however, those that survive beyond the age of one year, face a growth challenge due to a lack of access to finance during the first five years of existence. The establishment of a development bank can best serve this market of small businesses for at least the first five years until they graduate into bigger business and become the market for financial markets. Literature reveals that small businesses are by virtue of their being in the developmental phase (Section 2.2.7) as such not viable market for financial markets (banks). Despite of all efforts to make the former bankable, small businesses will never be a market for banks Section 2.6). Therefore, persistence to bridge the financing gap while the former is still in the development stage, the support will continue to benefit the latter (banks) while the former (small businesses) remain worse off.

7.2.6 Aligning development finance to business growth strategies

Objective 6: *To determine the extent to which availability of development finance aligns to growth strategies for small businesses.*

In exploring the alignment of development finance to business growth strategies, the review of theoretical study was assessed. Gupta *et al*., 2013 show that finance as one the main resources of the business along with competencies have ability to assist the business in achieving its competitive advantage. The competencies of the entrepreneur along with availability of development finance are very important in articulating business growth plans. As shown in Table 6.36, entrepreneurs align development finance to cash flow, and Table 6.34 where financing is aligned to turnover, converging with the view of Caselli (2009) that during the growth stages of the business, profitability and cash flow are bound to be negative as investment in the business is more operational and therefore more of development finance is required, as opposed to commercial finance that can potentially increase the liabilities of the business. Weinzimmer (2000) asserts that the business that has financial strength can influence business growth strategies through market development (target market); improving distribution channels to deliver the product to the target market.

However, the results showed that there was no shared understanding between the DFIs financing and business growth strategies, for example Table 6.47 indicates that the majority of the entrepreneurs had no idea if long-term business growth plans were shared with the DFIs. This finding is very important given that there is evidence that the availability of development finance is positively correlated to business performance. In the absence of a common understanding between the DFIs and the entrepreneurs regarding long-term growth plans, which translate to sustainability, the latter cannot be guaranteed, as confirmed by Biederman (2015) that businesses that do not have clear growth strategies cannot achieve sustainable growth since they are potentially heading towards failure. Ultimately, the goal to support growth small businesses in order to affect the development agenda may not be achieved. It is important that both the DFIs and entrepreneurs share a common understanding of business growth plans when development finance is provided, as Badulescu (2011) and Robin and Robinson (2014) both agree that finance is an important resource that helps the business to take advantage of opportunities available during each stage of the business cycle.

7.2.7 Development financing towards a sustainable development of small businesses

Objective 8: *To recommend a development financing framework guiding the DFIs to assist small businesses to achieve sustainable growth.*

Against the view that development finance is funding that is aimed at activities that help in reducing unemployment, poverty and inequality, such as investing in small businesses, the researcher recommends that the pricing of development would be more developmental if the three dimensions of development (employment, poverty and inequality) were factored in the determination of loan prices (interest rates).

The study reveals that while the DFIs are inarguably contributing to the development of small businesses, the study reveals that the financing gap will remain a challenge as long as the DFIs work in partnership with the banks during the development phases of the business life cycles of the SMME sector. This finding has its background from the fact that there is a mismatch between what the financial markets can offer and what the SMME sector in the development phase requires. The study, therefore proposes a framework in which the participation by the DFIs in financing small businesses, can lead to a sustainable growth and development of the SMME sector.

The proposed financing framework for small businesses by the DFIs resides around the following:

- The institution to which to channel the funding;
- The period for the incubation in the proposed institution; and
- The exit point of incubation.

The study recommends the framework to which financing of small businesses by the DFIs be carried out through the development bank for the period of at least ten years, the time during which this study has established as the development phase of growth of small businesses. During the ten years of establishment, small businesses are in the development phase which are characterised by many factors, including risks of failure caused, by among others, lack of working capital. Therefore, during the early stages of the business, development financing can be channelled through the use of stokvels which will be operating under the umbrella of the development bank, instead of RFIs which operate under financial markets.

7.3 CONCLUSION

This chapter focused on discussing the main findings of the study against the objectives as identified in the first chapter. The synthesis was done by combining both theoretical and empirical studies in order to address each of the research objectives. Although the study was mostly exploratory and not intended to confirm any particular theory, the theory study was used as the basis or the framework within which the empirical study was to be shaped, therefore it was not the intention of the study to accept or reject any hypothesis predicted by previous studies. All eight of the objectives have been achieved by the study as have been outlined in this chapter.

CHAPTER 8: OVERVIEW, CONCLUSIONS AND RECOMMENDATIONS

8.1 INTRODUCTION

The first part of this chapter provides a summary of the study, and thereafter the conclusions follow in the second part of the chapter. The third part of the chapter focuses on the implications of the study, while the fourth part, the final section, dwells on the recommendations for further research and the conclusion.

8.2 SUMMARY OF CHAPTERS

In Chapter 1 it was established that small businesses are entrusted to make a remarkable contribution towards the eradication of poverty, inequality, the reduction of unemployment, as well as making a meaningful contribution towards economic growth. However, due to high failure rates facing the sector, on account of among other things, lack of access to finance, the government of South Africa established the DFIs in order to help develop small businesses and bridge the financing gap facing the SMMEs.

In an attempt to find answers to the burning issues mentioned in the previous paragraph, the researcher found it necessary to perform a literature review (Chapter 2 – 4) related to the study under investigation.

Chapter 2 focused on the underlying perspectives of the main the concepts, as articulated in the study. The chapter reviewed the importance of small businesses and the challenges thereof with specific focus on the problem of access to finance as one of the leading challenges towards the growth of the sector. The literature review revealed that the problem of access arises from the fact that financing is expected from commercial lending. Commercial lending is highly regulated to minimise risks for the shareholders, and therefore excludes all risky markets, including small businesses. The chapter also revealed that there is limited research that has been done with regards to the role of development financing as an alternative towards the growth and development of small businesses.

Chapter 3 covered the theoretical framework of business growth. After exploring the different perspectives of business growth, the chapter highlighted the position of the current study indicating that business growth is a development process that continues throughout the business life cycle. The position of the study further points out that the competencies of the entrepreneur along with the appropriateness of the growth strategies for each stage of the life cycle which are the key to sustainable business growth.

Chapter 4 documented the South African small businesses and the DFIs. In particular, the chapter unpacked the profiling of the SMME sector in the country, including the milestones and challenges in the first part of the chapter. The second part presented the interventions by the government, through its DFIs, in supporting the growth and development of small businesses to ultimately assist in reducing unemployment, poverty, inequality and most importantly to contribute to economic growth. This part of the chapter provided the details of the distinctive operations of each of the DFIs.

The research methodology employed in this investigation was presented in Chapter 5. The chapter explained the choice of research methods applicable to this study. Reasons were provided for the choice of utilising an exploratory sequential mixed-methods approach to the research which consisted of two phases, I and 2, qualitative and quantitative approaches respectively. Data sources play a very crucial part of research; therefore, the population and data samples were detailed in this chapter along with the research instruments (interviews and questionnaires) as they were used to gather the desired information for this study. Attention was also given to details of how the collected data was presented, analysed and interpreted.

Chapter 6 presented the data that was gathered from the two phases: Phase 1 presented qualitative data from the in-depth interviews conducted with the DFIs which was thematically analysed with the help of Atlas Ti computer package; and Phase 2 presented both survey questionnaires and interviews with the entrepreneurs from Tshwane Metropolitan Municipality in the province of Gauteng. The data collected from structured questionnaire as well as open-ended questions were analysed with the aid of the computer program SPSS version 24 and thematic analysis of open-ended questions part of the question. The analytic tools that were used include, frequencies, factor analysis, t-test, ANOVA, Pearson’s product correlation coefficient and thematic analysis for the open-ended questions, which were presented in five sections.

Chapter 7 presented the discussion of research main findings against the research objectives. And the last chapter 8, the current chapter presents summary of chapters, conclusions, recommendations and implications of the study.

8.3 CONCLUSIONS AND RECOMMENDATIONS

In terms of source and purpose, development finance is different from commercial lending, the former is sourced from donors' funds, subsidies, and public finance to address development agendas such as poverty, unemployment and inequality; while the latter is sourced from members' deposits and savings in order to make profits and receive returns on investment. In order to achieve the individual objectives, the two target different markets. The latter is aimed at those which research considers as Category A customers (financially included), while the former (development finance) is aimed at financially excluded customers of the latter (Category C), from where the participants of the second phase were sampled.

The literature study also reveals that banking supervision and regulation oversees the operations of the banks in order to protect the members' funds and look after their interest of making profit through the regulation of lending criteria: assessments on affordability and creditworthiness, both which are used as the basis for determining the interest rates (loan prices) to be charged on the various pricing models available. The literature study further states that development finance is aimed at small businesses (financially excluded) in order to reduce the high levels of unemployment, poverty and inequality and to ultimately contribute to economic growth. Therefore, the literature review shows that development financing criteria are linked to the development objective however; there is no information with regard to the determination of the pricing of development finance loans (the main element of exclusion).

While DFIs have development programmes in support of the development of small businesses in South Africa, as well as making concerted efforts to reduce the financing gap, a common ground needs to be established between the two parties (the DFIS and small businesses) with regards to the expectations of each individual party. Unlike financial markets which are profit-driven, development institutions are development-driven and do not to accumulate profit; therefore the latter must operate differently from the former. While DFIs need to be sustainable, the pricing of development finance needs to be more biased towards the development factors, as opposed to commercial gains (high interest rates) which are identified as one of the obstacles behind access to finance. The framework that surfaced from both the literature and empirical research in this study delineates an alignment of development finance to the business performance with growth strategies (during the growth stages of the business) in support of development agendas.

The empirical study has revealed that development financing can only be effective for the growth and development of small businesses through the establishment of a development finance bank that is consistent with the development agenda. The DFIs, therefore should not partner with financial markets in financing small businesses for growth and development. Financial markets are regulated and structured for commercial lending and not for development purposes. This approach ensures growth of small businesses throughout the development phases of the business (within first ten years of establishment) until the businesses is well established to become financial market clients (financial inclusion).

Of the lending programmes provided by SEFA, wholesale lending through RFIs has proven more successful than direct lending. Intermediaries reach out to a broader market than direct lending because RFIs are spread across the country. They are well placed, capacitated and have an established market. However, although the entrepreneurs agree that financing is readily accessible from the RFIs, the entrepreneurs believe that loans prices of the RFIs are very high, as opposed to stokvels which function similarly to the RFIs, except that stokvels are considered more developmental than RFIs.

The developmental mandate includes not only employment creation but to alleviate poverty and reduce inequality. Although wholesale lending does not directly impact on employment, people's livelihoods are positively affected thereby.

The study focused on entrepreneurs, academics and policy makers in contemporary access to finance for the small business sector in South Africa, with specific reference to the development financing institutions towards the support of the sector as growth and development instruments. The study is unique because it focused on a different angle of access to finance from the DFIs, as opposed to the existing literature which focused mainly on access to finance from the commercial lending (banks) perspective.

The findings indicate that the DFIs have development programmes (both financial and non-financial) that are tailored to focus mainly on the small business sector, which is excluded from the conventional financing net, as the existing research asserts. The findings of the study further indicate that although the DFIs have made a remarkable impact towards advancing finance to small businesses, the entrepreneurs are of the view that as long as the banks are still partners in channelling of the funds, the problem of access to finance will not be eliminated.

No study has focused exclusively on the role of the DFIs on financing small business as the fundamental and strategic tool for the growth and development of small businesses in South Africa. The study has also adopted the rare approach of using a mixed-methods approach by following the exploratory sequential methodology using both the supply-side (the DFIS) and the demand side (the entrepreneurs), and thereby achieving the aim of the study. The findings obtained from the entrepreneurs' survey are consistent with the results gathered from the DFI interviews, however; the findings from the entrepreneurs further suggest a different approach to development finance which must be completely separated from commercial lending. The results will therefore, prove valuable to the policy makers and entrepreneurs that strive towards the growth and development of small businesses in order to make a remarkable contribution towards economic growth, and a reduction in unemployment rates, inequality and poverty in South Africa.

8.4 MANAGERIAL IMPLICATIONS

This section of the implications of the study is divided into four subsections: the DFIs; policy makers; the entrepreneurs and contribution of the study to the body of knowledge.

8.4.1 Implications for the DFIs:

The findings of the study demonstrated the DFIs have no control on who receives the credit guarantee schemes as the decision lies with their strategic partners, the banks. The facility fails to reach and benefit the intended recipients. All the evidence from previous research indicates that small businesses are a risky market, and therefore not a potential market for the financial markets, so even though the credit guarantee facility is available to ease the problem of access to finance, small businesses cannot benefit from the facility. The results also showed that there are some unethical practices by some stakeholders regarding financing decisions. This behaviour has the potential to pose as a threat to the successful achievement of the institutional financing objectives. The limited budget also limits the impact of the DFIs towards the growth and development of small businesses.

The DFIs should be able to reach out far enough to reach the rural areas where most of the development programmes are not well known. This can be achieved by opening satellite offices at local municipalities to ensure that each region is attended to. Organising regional business summits can help disseminate information.

The role of DFIs should be skewed more towards the development agenda of reducing unemployment, poverty, and inequality through the development support of small businesses, which unarguably are believed to be the engine of economic growth and the key source of employment. DFIs must not function like commercial banks which are profit driven.

8.4.2 Implications to the policy makers

In order for the government to achieve its objective of creating 11 million jobs, of which 90% of those jobs are dependent on small businesses, the development financing of small businesses needs to be linked to the objectives. That is, employment creation must be recognised as one of the key performance areas of investment by the DFIs in advancing development finance. Advancing development finance for SMMEs must be a priority for DSBD to remove the problem of access to finance which has been topping the list of prohibiting growth factors for small businesses for more than 20 years.

This study documents that because small businesses are still in the development phase, only development financing, and not commercial lending is the answer to meeting the development financing needs against growth strategies.

A separate body (different from the existing body regulating the financial markets) is suggested to regulate a development bank. The existing banking regulation body is structured to regulate commercial banking and therefore does not present and match any development agenda. A regulator must be more pro-developmental agenda (targeting employment, poverty and inequality and ultimately, economic development) than the commercial agenda (profit maximisation).

The establishment of development banking seems to be the most prominent and potential answer to the problem of access to finance. Regardless of any efforts being made, small businesses are not the market for the regulated financial markets and therefore will always remain outside the financing net. Only through the establishment of a development bank for the sector will it be able to access finance. The establishment of a development bank will not only cater for small businesses but for all other development agendas, including social development projects such as social stokvels. A development banking model that is compatible with the development process of small businesses is revealed by the findings of this study as a potential solution for the problem of access to finance.

Policy prescriptions in the area of development finance should focus towards the implications of the available funding options. The funding options need to address the needs of the start-ups with high growth potential, which are, however, owned by individuals who are financially excluded (who cannot afford high loan fees yet need new risk capital).

8.4.3 The contemporary South African entrepreneurs

This study is unique in that it focuses on the contemporary South African entrepreneurs with regards to role of the DFIs in financing small businesses. Previous research has focused on the financing of small businesses dominated by commercial lending provided by the financial markets, which implicitly demonstrated that small businesses are not the eligible market for banks, and hence the growth prospects of the sector are hindered. The study indicated that entrepreneurs need to clearly understand different growth strategies applicable to the growth stages of the business life cycle when making a request for financing. The entrepreneurs need to clearly discuss their growth plans with the DFIs so that they establish a common understanding during the finance application process.

The entrepreneurs have stated that they prefer industry-based structural repayment which is more desirable than the monthly repayment method which is usually linked to salaried people. The industry-based structural repayment approach will potentially reduce the prevalence of high default rates and also help increase cash flow for entrepreneurs as well as improve the chances of business survival.

8.4.4 Implications for theory and contribution to the body knowledge

The existing theories of BLC, Structuralist and Complexity as closely linked to the business development theory show lose ends with regards to small business development financing. The current inquest and the business life cycle of the growth theory point to the role of the DFIs' impact on the growth of small businesses using different development financing approaches and tools aligned to different business growth strategies, particularly during the early stages of the business life cycle. Although the study adapted to a large extend the BLC theory, the analogy of Complexity and Structuralist theories. The former with its regards to unpredictable and chaotic environment experienced by start-up businesses was incorporated towards the adoption of a new integrated growth of the BLC theory. Incorporating this element of Complexity to the BCL is believed by the researcher to play a pivotal role in deciding on the financing strategy applicable for the enterprise. The latter points to the institutional support particularly on matters of development finance. There is a strong convergence of the views of the DFIs and the perceptions of the entrepreneurs with regards to the impact of development financing towards bridging the financing gap that exists for small businesses in the financial markets. Most importantly, the entrepreneurs strongly suggest the establishment of a development finance bank that will serve as a gateway towards achieving the objective of bridging the financing gap for small businesses during the early stages of the business life cycle.

Small businesses in South Africa make up about 96% of all businesses, and therefore are entrusted with the huge responsibility of contributing towards reducing the country's dilemma of the high unemployment rate that is currently standing at almost 27% by creating about 11 million jobs in order to achieve the government's NDP of reducing unemployment by at least 6% by the year 2030. With the high failure rates experienced by the SMME sector in the country, the DFIs are reaching out to address some of the potential obstacles, such as bridging the financing gap; business (Fatoki, 2014) and skills shortage (Abdulaziz & Worthington, 2013) that trigger growth and sustainable development of small businesses. The results show that unless the funding and DFIs' loan pricing approaches are matched to business growth strategies, the objective to develop small businesses to increase employment will not be achieved. Entrepreneurs opt for institutions (such as stokvels) that are developmental in order to help them grow their businesses.

8.5 RECOMMENDATIONS FOR FURTHER RESEARCH

The nature of this study is exploratory and the discussion has been done with the observance of the extant literature which informed the analytical discussion. Not all aspects of analysis are supported by research, and hence open doors for further research. Research is surrounded by many complexities that cannot be addressed in one study (Rafaeli & Pratt, 1993). Therefore, the researcher makes the following recommendations for further research:

- The study focused on a holistic view of the DFIs, it is therefore suggested that the impact of individual DFIs be investigated. Each DFI caters for a specific market within the small business sector, it would be interesting to measure the performance of each individual DFI.
- A longitutional study on the performance of small businesses financed by the DFIs is also suggested in order to measure the impact of development finance. Perfomance of the business is a function of a number of variables, measuring it over a period of time can help to single out the actual impact of finance.

8.6 CONCLUSION

This final chapter provided a summary of the chapters of the study. The summary of all the chapters was highlighted in the chapter. The main focus of the chapter was to present the highlights of the study, including the main research aim and question; research objectives and questions; the main findings as well as the overall conclusions of the study.

Although the study is highly skewed towards the BLC theory, the aspects of uncertainty and chaoticness of the start-up business environment of the Complexity theory, along with expansion of programmes and systems to accommodate the excluded sectors of the Structural theory to led to the adoption of a new integrated growth theory of BLC. Understanding the stages of the business life cycle is very crucial in providing development finance, in order to appropriately allocate the most needed type of financing for the stage in which the business finds itself, taking into given that the environment is not always linear and certain. As a response to the challenge of access to finance for small businesses, the DFIs have developed both financial and non-financial programmes to address the problem. In the process, although there is still room for improvement, the financing gap facing the sector is being narrowed. However, being in the development stages of life cycle, the approach to financing for small businesses should be channelled through a development bank (structural development) outside the commercial lending practices, and then progressively transit to mainstream banking as they (small businesses) graduate from the growth stages.

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APPENDIX A:
GATEKEEPER CONSENT LETTER

Department of Management and Entrepreneurship
School of Management, IT and Governance,
College of Law and Management,University of KwaZulu-Natal,
Pietermaritzburg Campus, Pietermaritzburg, Scottsville, South Africa

20 June, 2013

To Whom It May Concern:

PERMISSION TO CONDUCT RESEARCH AS PART OF THE REQUIREMENTS FOR THE AWARD OF PhD QUALIFICATION

It is a requirement of our PhD qualification that all students undertake a practical research project. In this way students are given the opportunity to creatively link and discuss the theoretical aspects of the programme to the practical issues facing organisations in real life settings. Typically this project necessitate data gathering by questionnaires and interviews.

Lisebo Ntiso (212556652) has chosen to do a research project entitled:
The role the DFIs in financing small businesses in South Africa (1996 -2012)

Your assistance in permitting access to your organization for purposes of this research is most appreciated. Please be assured that all information gained from the research will be treated with the utmost circumspection. The student will strictly adhere to confidentiality and anonymity.

I am available at any stage to answer any queries and/or to discuss any aspect of this research project.

If permission is granted, please sign the attached form.

Thank you for your assistance in this regard.

Please complete the section below:

I hereby give permission to .... (Name of student) to conduct research in my organization.

The student MAY/MAY NOT (delete whichever is not applicable) use the name of the organisation in the research report.

Name of Manager/Owner: ....

Signature of Manager/Owner: ....

Date: ....

APPENDIX B:
INFORMED CONSENT LETTER

UNIVERSITY OF KWAZULU-NATAL
School of Management

Dear Respondent,

PhD (Management Studies) Research Project
Researcher: Lisebo Ntiso (012-429 4350)
Supervisor: Prof Phiri (033 260 5736)

I, **(LISEBO NTISO)** a **PhD (Management Studies)** student, at the **MANAGEMENT**, of the University of KwaZulu Natal, you are invited to participate in a research project entitled **(The role of the development finance institutions (DFIs) in financing small businesses in South Africa.** The aim of this study is to: (explore the role of the DFIs in financing small businesses as an imperative growth and development instrument of development policy of South Africa during.

Through your participation I hope to understand **the role the DFIs in financing small businesses in South Africa.** The results of the interview are intended to contribute to achievement of the research aims.

Your participation in this project is voluntary. You may refuse to participate or withdraw from the project at any time with no negative consequence. There will be no monetary gain from participating in this study. Confidentiality and anonymity of records identifying you as a participant will be maintained by the **SCHOOL OF MANAGEMENT**, UKZN.

If you have any questions or concerns about completing the interview or about participating in this study, you may contact me or my supervisor at the numbers listed above.

The interview should take you about **one hour** to complete.

Sincerely

Investigator's signature: ____________________ Date__________________

CONSENT

I…………………………………………………………………………… (full names of participant) hereby confirm that I understand the contents of this document and the nature of the research project, and I consent to participating in the research project.

I understand that I am at liberty to withdraw from the project at any time, should I so desire.

Signature of participant ________________________Date________________________

APPENDIX C:
INTERVIEW GUIDE

Interview Guide

1. When was (**name of the DFI**) established? What is the difference between (NAME OF THE DFI) and (the previous name)? How are they related? What has changed and what remained and why?

2. What was the purpose of the establishment of (NAME OF THE DFI) when there are so many financing institutions?

3. One of the main challenges facing growth of SMMEs is access to finance, how does (NAME OF THE DFI) assist? Can you please explain?
4. How does the institution assist small businesses to access finance? Can you elaborate? (how are the funds channelled? Are the clients expected to have a bank account? SMMEs are not a market for bank lending, what is the motive to get them involved?)

5. What is your target market – age, race, gender, education level? Why that particular market?

6. At what stage of business does (NAME OF THE DFI) help – start –ups, existing/ established businesses? Can you please explain?
7. Most businesses are operating informally; does (NAME OF THE DFI) financially help this market? How?

8. Does (NAME OF THE DFI) operate as a bank for the target market? Can you elaborate? How does the institution address the financial gap that exists for small businesses?

9. What instruments/ tools/strategies does the (NAME OF THE DFI) use on assessing loan applications? Can you explain?
10. How does (NAME OF THE DFI) ascertain that the applicant has linked the need for finance to growth plans

11. As a development financing institution, how does (the DFI) determine whether or not that the support provided does help to develop/ grow small business assisted? Any monitoring? Aftercare services?

12. How many small businesses have been assisted by the (NAME OF THE DFI) since its establishment? Over 5 or 3 years? Who are those – target market? Which industries? How many of those are from Tshwane?

13. How do you ascertain that financial support that (NAME OF THE DFI) provides in deed affect growth and development of small business? Can you elaborate?

14. How much employment is created by small businesses after being supported by (NAME OF THE DFI)?

15. Does (NAME OF THE DFI) manage to achieve its financing budget every financial year? Please elaborate?

16. To what extend have financing program been achieved, and what hinders program implementation? Please explain?

17. What methods and tools are considered in processing the application? (e.g. , applicant analysis, value of collateral, credit worthiness, payment periods, Business Plans as well as financial statements of the business)?

18. If the business fails, does the client have to pay back the money? Or what happens?

19. Which the methods and tools mentioned would consider being key elements? Please explain?

20. What make your programs work well/ not well? Please elaborate?

21. Which methods and tools (if any) have been discontinued or redesigned? Why?

22. What are some barriers and challenges you face in your efforts to assist SMMEs? (E.g. legislation? Lack of key support? Target industries? Illiteracy of entrepreneurs and lack of business skills)?

23. How do you overcome these barrier(s)?

24. How does (NAME OF THE DFI) handle non-payment cases?

25. What are the possible reasons for applications to be rejected? Is there any help that is provided for the rejected applications? Can you name them?

26. What is the expected return on the investment that (NAME OF THE DFI) the clients?

27. What would you do differently next time – increase your budget, personnel or add more programs? Please explain why?

28. South Africa has high failure rates in SMME market, what can be done to assist small businesses to grow and develop?

29. Any recommendations for future programs such as the ones (NAME OF THE DFI) is offering to reach out to a greater population? **ALL**

ANNEXURE E

Questionnaire

English	1
Other language	2

How many employees does your business currently employ, excluding the owners or partners?

None	1
1 – 9	2
10-49	3
50 -99	4
100 – 199	5
200 – 250	6
>250	7

If more than 250 employees, do not fill this, thank you

We need to conduct interview with individuals who are owners, partners/directors, or who have day-to-day control of the business. Can you advise if there is another person in the business who might fit this description?

Answer each question by filling an X in the suitable box provided or write your answer in the shaded space provided (for open questions)

1. **What is your gender?**

Male	1
Female	2

2. **What is your age?**

18 – 35	1
36 – 45	2
46 – 55	3
Above 55	4

3. **What is your race?**

Black	1
White	2
Indian	3
Coloured	4

Section B

4. **Which language do you prefer to use as medium for your business?**

English	1
Other	2

5. **What is your highest formal education?**

Below Matric	1
Matric/ Grade 12	2
Post matric	3
Bachelor's and higher	4

6. **How many people work in your business have?**

1- 5	1
6 -20	2
21 – 50	3
51 – 200	4

7. **When was your business established?**

Within past year	1
1-5 years ago	2
More than 5 years ago	3
More than 10 years ago	4

8. **Was your business already registered when you approach the DFI**

Yes	1
No	2

9. **The DFI helped me register my business**

Yes	**1**
No	**2**

10. **Did the business have a bank account before the DFI was approached?**

Yes	1
No	2

11. **In which industry does the business operate?**

Retail, motor trade and repairs	1
Manufacturing	2
Cleaning/catering/accommodation	3
Construction	4
Wholesale trade/commercial and allied services	5
Finance and business services	6
Transport/storage/communication	7
Agriculture	8

Mining/quarrying/electricity/gas/water	9
Community and personal services	10

12. What is the business annual turnover or gross income?

Less than R50,000	1
R50,000 – R 100,000	2
R101,000 – R200,000	3
R201,000 – R500,000	4
More than R500,000	5

13. When the business started, how was it financed?

Personal savings	1
Family	2
Bank	3
DFI	4
Stockvel	5

14. Was the finance 1st application successful?

Yes	1
No	2

15. On 2nd application, which DFI actually funded your business?

Same DFI	**1**
Another DFI referred to	**2**

16. Additional support provided

Offered non-financial support	**1**
Referred to another institution	**2**

17. What type of finance did the business require?

Loan	**1**
Credit guarantee scheme	**2**
Procurement finance	**3**
Grant	**4**

18. What area of the business needed financing for which you approached the DFI?

To improve my product	**1**
Increase production/stock	**2**
Serve more customers	**3**
Employ more people	**4**
Increase sales	**5**
Increase turnover	**6**

19. What was the stage of the business when you approached the DFI?

Introductory/start-up	1

Growth	2

20. **What is your opinion of the main role of development financing on growth of your business?**

Increased employment	**1**
Business expansion	**2**
Sales growth	**3**
Increased turnover	**4**

21. **How would you define business growth?**

Increase in stock	**1**
Increase in turnover	**2**
Increase in number of employees	**3**
Increase in sales volumes	**4**
Increase in production	**5**
Increase in number of customers	**6**

22. **DFI must work independently not through a bank to minimise transaction costs?**

Strongly disagree	**1**
Disagree	**2**
Indifferent	**3**
Agree	**4**
Strongly agree	**5**

23. **Are you participating in any stockvel?**

Yes	**1**
No	**2**

24. **Where do you prefer to save your money for business growth, with a bank or stockvel?**

Stockvel	**1**
Bank	**2**

Please explain your choice

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25. What other area of the business improved after receiving funding?

Revenue	**1**
Sales	**2**
Stock	**3**
Additional product	**4**
Additional personnel	**5**

Pleas indicate whether you (1) strongly disagree, (2) disagree, (3) are undecided, (4) agree, (5) strongly agree with each of the following statements. Choose one answer only for each statement.

Statement	**SD**	**D**	**N**	**A**	**DA**
26 Non-financial support programs improve business skills?					
27 DFIs programs are developmental for SMMEs	1	2	3	4	5
28 I had my business growth plan when I approached the DFI	1	2	3	4	5
29 DFIs provide services that grow small businesses	1	2	3	4	5
30 The DFIs financing address business financial needs	1	2	3	4	5
31 The turnaround was reasonable	1	2	3	4	5
32 Interest charged by the DFIs is too high	1	2	3	4	5
33 The interest rate should reflect business growth premium	1	2	3	4	5
34 Interest rates must have positive effect on the business	1	2	3	4	5
35 Payment terms need to be linked to industry structural performance	1	2	3	4	5
36 Monthly repayments affect cash-flow/working capital negatively	1	2	3	4	5
37 I have shared my business growth plans with the DFI	1	2	3	4	5
38 The DFI understands my business growth plans	1	2	3	4	5
39 Structural payments is better than pre-tailored monthly payments	1	2	3	4	5
40 I prefer that SMMEs have own bank	1	2	3	4	5
41 A dev bank that will serve the market excluded by banks is needed	1	2	3	4	5
42 Funding has helped me to grow my business	1	2	3	4	5
43 the DFI helped me establish/improve a relationship with the bank	1	2	3	4	5
44 Developmental approaches need to be established to recover bad loans	1	2	3	4	5
45 Given a chance, I would re-approach the DFI for finance than a bank	1	2	3	4	5
43 different growth strategies discussed with the DFI	1	2	3	4	5
44 different financing opportunities were discussed	1	2	3	4	5
46 Finance helped me to create additional employment	1	2	3	4	5
47 Short-term growth plans: finance helped increase sales	1	2	3	4	5
48 Finance increased my turnover	1	2	3	4	5
49 Long-term growth plans discussed with the DFI	1	2	3	4	5
50 The finance helped me achieve my growth plans	1	2	3	4	5
51 Different future growth strategies discussed with DFI	1	2	3	4	5
52 Stockvels are a better are a better saving platform for SMMEs than banks	1	2	3	4	5
53 Default rates are minimal with stockvels	1	2	3	4	5
54 Establishment of SMME development bank can reduce financing gap	1	2	3	4	5
55 SMME development bank can better house stockvels	1	2	3	4	5
56 Stockvels are a form of development finance	1	2	3	4	5
57 DFI loan prices must factor-in youth empowerment	1	2	3	4	5
58 DFI loan prices must factor-in women empowerment	1	2	3	4	5

59 DFI use only cost and risk based on loan prices	**1**	**2**	**3**	**4**	**5**
60 DFI interest rates must factor-in employment factor	**1**	**2**	**3**	**4**	**5**
61 DFI interest rates need to reflect business growth factor	**1**	**2**	**3**	**4**	**5**
62 DFI loan prices should consider address development agenda	**1**	**2**	**3**	**4**	**5**
63 DFI interest rates show lack of shared framework of business growth	**1**	**2**	**3**	**4**	**5**
64 partnerships by the DFIs delays turnaround of finance application	**1**	**2**	**3**	**4**	**5**
65 credit guarantee schemes need to reduce loan prices	**1**	**2**	**3**	**4**	**5**
66 information regarding the DFIs is readily available	**1**	**2**	**3**	**4**	**5**
67 the support by the DFIs reduces information asymmetry	**1**	**2**	**3**	**4**	**5**
68 support of the DFIs reduces the problem of lack of assets	**1**	**2**	**3**	**4**	**5**
69 support of the DFIs eliminates the problem associated with lack of credit record	**1**	**2**	**3**	**4**	**5**
70 support of the DFIs reduces the problem of cost of credit – asset finance	**1**	**2**	**3**	**4**	**5**
71 support of the DFIs reduces high risk premium – equity finance	**1**	**2**	**3**	**4**	**5**
72 support of the DFI increases cash flow – working capital	**1**	**2**	**3**	**4**	**5**
73 support of the DFIs increases credit worthiness	**1**	**2**	**3**	**4**	**5**
74 support of the DFIs increases bank-borrower relationship	**1**	**2**	**3**	**4**	**5**
75 bank regulation limits DFI support	**1**	**2**	**3**	**4**	**5**
76 support of the DFI reduces risk associated with small businesses	**1**	**2**	**3**	**4**	**5**
77 support of the DFIs increases saving and credit management culture	**1**	**2**	**3**	**4**	**5**
78 support of the DFIs improves entrepreneurial and management skills	**1**	**2**	**3**	**4**	**5**
79 my money will be safe with development bank	**1**	**2**	**3**	**4**	**5**
80 development finance needs a different regulation	**1**	**2**	**3**	**4**	**5**
81 development finance needs to operate differently from commercial finance	**1**	**2**	**3**	**4**	**5**
82 development finance needs to have own bank	**1**	**2**	**3**	**4**	**5**
83 small businesses needs to have a banking house - development bank	**1**	**2**	**3**	**4**	**5**
84 DFIs must work with development bank for SMME development	**1**	**2**	**3**	**4**	**5**
85 development finance needs to consider development factors in pricing loans	**1**	**2**	**3**	**4**	**5**
86 development finance bank needs to house stockvels	**1**	**2**	**3**	**4**	**5**
87 development finance bank needs to accept development deposits from stockvels	**1**	**2**	**3**	**4**	**5**

88. In your opinion, how has development support of the DFIs helped your business in terms of growth?

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89 Please explain your opinion: Stockvels are a better saving and lending platform for small businesses (Yes/No)

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90. What does development finance mean to you?

91. In your opinion, how can the DFIs resolve some of the challenges identified?

92 In your opinion, why is it necessary to establish SMME development finance bank when banks are available?

<<<<<<<<<<<<<<<<<<<<Thank you>>>>>>>>>>>>>>>>>>>>>

APPENDIX D:
ETHICAL CLEARANCE CERTIFICATE

UNIVERSITY OF KWAZULU-NATAL™
INYUVESI YAKWAZULU-NATALI

28 March 2014

Ms Lisebo A Ntiso (212556652)
School of Management, IT & Governance
Westville Campus

Protocol reference number: HSS/0050/014D
Project title: The role of the DFIs in financing small businesses in South Africa (1996-2012)

Dear Ms Ntiso,

Full Approval – Expedited

In response to your application dated 26 June 2013, the Humanities & Social Sciences Research Ethics Committee has considered the abovementioned application and the protocol have been granted **FULL APPROVAL.**

Any alteration/s to the approved research protocol i.e. Questionnaire/Interview Schedule, Informed Consent Form, Title of the Project, Location of the Study, Research Approach and Methods must be reviewed and approved through the amendment/modification prior to its implementation. In case you have further queries, please quote the above reference number.

PLEASE NOTE: Research data should be securely stored in the discipline/department for a period of 5 years.

The ethical clearance certificate is only valid for a period of 3 years from the date of issue. Thereafter Recertification must be applied for on an annual basis.

I take this opportunity of wishing you everything of the best with your study.

Your[redacted]

.......[redacted]......................................

Dr Sh[redacted]

/ms

cc Su[redacted]nye and Dr M Phiri
cc Academic Leader Research: Professor Brian McArthur
cc School Administrator: Ms Angela Pearce

Humanities & Social Sciences Research Ethics Committee
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