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BUSINESS FINANCING ACCESS AND SMALL AND MEDIUM SCALE ENTERPRISE DEVELOPMENT IN NIGERIA. (A STUDY OF SOME SELECTED SMALL AND MEDIUM SCALE ENTERPRISES IN ODEDA LOCAL GOVERNEMNT AREA IN ABEOKUTA, OGUN STATE)

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Abstract

The study capitalizing on business financing access as it affects small and medium enterprises development in emerging economy: Nigerian perspectives (Odeda Local Government area, Ogun State). Survey research design was employed for the study where 127 respondents (sample size) from the selected total estimated population of 185 SMEs for the study area and were gathered through the use of structured questionnaire. Their responses were tested using appropriate statistical tools of SPSS package using the ANOVA, the correlation and the regression too. Our study capitalizing on business financing access as it affects small and medium enterprises development in emerging economy: Nigerian perspectives positively which has allowed youths to be self-employed and created economic growth and regional development. Therefore, the study recommended that solving the performance of SME development can be single handedly done by the use of business financing access. Hypothesis one shows Venture Capital Financing is independently and positively correlated with SME Profitability and also highly significant at 1% level. As a result, the alternative hypothesis 1 of this study was accepted due to a correlation value (r = 0.408). Hypothesis two shows that Angel Investment is independently and positively correlated with SME Growth and also significant at 1% level. As a result, the alternative hypothesis 2 of this study was accepted due to a correlation value (r = 0.291). The study therefore recommends that Since SMEs are catalyst for economic development, angel investors and business philanthropist should be willing to fund small businesses for the achievement of goals and objectives.

Keywords: Business Financing Access, Venture Capital, Angel Investors, SMEs, Government and Development

Background to the Study

Small and medium-sized enterprises (SMEs) play a pivotal role in the national economies of countries around the world as they are considered to be an engine for growth in both developed and developing countries; the benefits of a vibrant SME sector include: the creation of employment opportunities; the strengthening of industrial linkages; the promotion of flexibility and innovation; and the generation of export revenues (Lerner, 2002; Rangamohanet al*,* 2007). In Nigeria, there is no one single definition that distinguishes a purely small-scale enterprise from a medium-scale enterprise. Financing is necessary to help SMEs set up and expand their operations, develop new products, and invest in new staff or production facilities. Many small businesses start out as an idea from one or two people, who invest their own money and probably turn to family and friends for financial help in return for a share in the business. But if they are successful, there comes a time when they need further funds to expand or innovate further. Hence, SMEs owners need to look beyond credit financing and focus on equity financing as a better option since equity financing requires no collateral and also connotes commitment.

Venture capital is an investment in a start-up or growing SME that is perceived to have excellent growth prospects. Venture capitalists raise and manage funds which are a pool of money raised from both public and private investors. Venture Capitalists are organized providers of financing for winning but risky business proposals by small and medium firms that have a promising but as yet unproven idea. Venture capital assists investors to access equity capital to finance expansion of business while maintaining control. In venture capital financing agreement, the venture capital firm will provide financing to enable a business to undertake a project and in return the venture capital company gets an ownership stake in the business (Boateng, 2010).

Besides financial benefits their motivations rested also in their love for the theatre and the opportunity to meet and socialize with famous actors, screenplay writers and producers. These investors secured high-risk capital and were motivated by something larger than money. However, SMEs in Nigeria and Ogun State, in particular, have continued to remain underfunded. Therefore, there is the need to enhance the development of SMEs since they should contribute meaningfully to economic development. It is on this basis that this study sought to investigate whether business finance improves the development of SMEs in Odeda LGA, Ogun State.

Statement of Research Problem

SMEs are faced with many problems such as dearth of set up capital, lack of funds for expansion, unreliable and inadequate economic infrastructure and lack of management skills and techniques. Among all the pressing limiting factors, accessing finance for set up and working capital for expansion seems to be the most challenging (Oma-William, 2003). Financing early stage business involves special problems and is fundamentally different from investments in matured and well established companies.

Furthermore, venture-backed firms also perform significantly better after they go public than similar non-venture-backed firms (Bratton, 2002). An empirical study on the effect of venture capital financing on the economic value added profile of Nigerian SMEs by (Dagogo and Ollor, 2012) found that venture backed SMEs contributed more to society in terms of taxes to government, provision for corporate social responsibility and staff welfare. Although the reasons to seek venture capital are obvious, the entrepreneur and the venture capitalist must be aware of the conflicts of interest that exist between them. Deal terms structured by the venture capitalist should address these conflicts of interest by minimizing the risk and maximizing the returns for the VC. Structuring deal terms in the venture capital world can be a very complex process.

Angel investors play a key role in financing small and medium sized enterprises, especially those which are innovative and with high growth potential. SMEs in their development pass through several stages. Many companies have problems, not only with the use of financial capital; they are less-known in nonprofessional social circles, because they tend to keep their business activities away from the public and the media, because they do not want to be disturbed with various offers for future investments. This is so because even in developed economies where angels exist not much is known about them. This study wishes to confirm this statement. With the above mentioned issues, it becomes imperative to investigate the effect of business finance on the development of SMEs in Odeda Local Government, Ogun State.

Literature Review

SMEs in Nigeria have not performed creditably well and hence have not played the expected vital and vibrant role in the economic growth and development of Nigeria. However, the role played by SMEs, notwithstanding their development, is everywhere constrained by inadequate funding and poor management. The unfavourable macroeconomic environment has also been identified as one of the major constraints which most times encourage financial institutions to be risk-averse in funding small and medium scale businesses (Ogujiubaet al., 2004).

SMEs play very important roles in developing economies, and assisting them is a task which ranks high in the priorities of the governments. This position is corroborated by other studies which identified financial support as one of the main factors responsible for small business failures in Nigeria (Abereijo & Fayomi, 2005; Okpara & Pamela, 2007).According to Okafor & Onebunne (2012), the terms and conditions for accessing funds of this nature are spelt out against each credit type. Since small businesses are perceived as risky borrowers, fund providers attempt to minimize credit risk exposure when dealing with them by offering small amount of loans rather than full financing, at very high cost.

Venture capital is relatively a new term in transitive countries. Venture capital is one of the most up-to-date forms of investment. Its nature is that private firms are financed through increasing their basic capital for concrete period. This is a cooperation and partnership between investor and entrepreneur resulting from former agreed conditions about both-side advantageousness. Concerning different authors and points of view on venture capital investments, we may define venture capital in several ways. Venture capital is thus the alternative form of obtaining the financial sources for small and medium enterprises. Unfortunately, in transitive countries this form of financing is rarely used.

Venture capital is capital provided by outside investors for financing of new, growing or struggling businesses. Venture capital investments generally are high risk investments but offer the potential for above average returns. A venture capitalist (VC) is a person who makes such investments. A venture capital fund is a pooled investment vehicle (often a partnership) that primarily invests the financial capital of third-party investors in enterprises that are too risky for the standard capital markets or bank loans. For aspiring entrepreneurs looking to locate and secure venture capital they have the option of seeking the support of a mentor capitalist. A mentor capitalist is an expert not only in acquiring capital but he can also provide support and direction to early start-ups and seeds.

The importance of access to early-stage finance for fostering high-growth innovative entrepreneurship has been widely acknowledged in the literature. Business angels serve as gap fillers in start-up financing that provide sources of financial, human and social capital to overcome these gaps (Macht& Robinson, 2009). A business angel is an investor who has passion and enjoys helping early stage businesses with limited or no fund (Preston, 2007). Angels are significant suppliers of equity capital at the early stage of a small business life.

One of the most difficult components in starting and growing a new enterprise is acquiring capital and other resources. The lack of funding can lead to cash flow problems, missed opportunities, and shut down of the fledgling enterprise (Auken, 2002). Globally, angels are responsible for a growing number of investments, even though this is relatively unidentified in both developing and developed economies (Shane, 2008).

The concept of SMEs is dynamic and relative (Ogunleye 2004). Several institutions and agencies defined SMEs differently with parameters such as employee's size, asset base, turnover, financial strength, working capital and size of the business. These definitions include; Nigerian Industrial Policy 1989 defined SMEs as enterprise whose investment in working capital is between N100,000 and N2m excluding cost of land.

The pecking order theory of financing says that firms and individuals will use personal funds before acquiring external debt and equity. POT was originally devised to examine the financing of large corporations, but it has also been applied to small and medium-sized businesses. In the case of the small firm or entrepreneur, personal sources are used first, external debt next, followed by outside equity. Equity is acquired last because the entrepreneur presumably has more information than the investor. The presence of significant information asymmetries causes the investor to charge a higher rate of return on equity than on debt (Frank and Goyal, 2003). This theory is relevant to this study as it critically focused on equity financing last and it can be deduced that equity financing does not really have significant impact on SMEs development unlike the first two; personal savings and credit financing.

Research Method

This study adopted quantitative data analysis for this study; the survey research design was employed. The scope of the study covers Odeda Local Government Area, Ogun State, Nigeria. The respondents who are owners of businesses (SMEs) in the areas were purposively selected in order to accomplish the objective of the study. Primary method of data collection was used for this study through a field survey of businesses with the aid of purposive well-structured questionnaires.

The questionnaires instrument was designed using five (5) likert's scale, as well as through an in-depth personal interview guided by the questions raised in the questionnaire which proved to be most effective due to the fact that most respondents could not fill in their responses or due to time constraints. A sample of 127 respondents was identified from a population of 185 small and medium enterprises within the study area using purposive sampling method of Marcor S.S (2019) Calculator and Raosoft (2019) calculator based on reports of the number of small and medium businesses in the study area and approximately

94.5% of the administered questionnaires were retrieved. Each of the dependent and independent variables of the research construct were measured by three (3) items each validated by different authors found in extant literature. Pre-test was also conducted through a pilot study which was carried out for the research instrument's validity test results is 0.705. Split half method of reliability test results on the split halves 0.84 and 0.91 respectively show that research instrument is reliable (Garson, 2009)

Interpretation of Results

Spearman Rank correlation and Ordinary Least Square (OLS) were used to test the research hypotheses and analyze the dependent and independent variables.

Hypothesis 1: There is no significant relationship between venture capital financing and SME profitability

Table 4.3.1 Correlations of Venture Capital Financing and SME Profitability

			Venture capital financing	SME Profitability
Spearman's rho	Venture capital financing	Correlation Coefficient	1.000	.408**
		Sig. (2-tailed)	.	.000
		N	120	120
	SME Profitability	Correlation Coefficient	.408**	1.000
		Sig. (2-tailed)	.000	.
		N	120	120

**. Correlation is significant at the 0.01 level (2-tailed).

Table 4.3.1 shows that Venture Capital Financing is independently and positively correlated with SME Profitability and also highly significant at 1% level. As a result, the alternative hypothesis 1 of this study was accepted due to a correlation value (r = 0.408).

Decision

The above result implies that there is a significant relationship between venture capital financing and SME profitability i.e. since our r value (0.408) is positive and highly significant. Thus, the decision would be to reject null hypothesis (Ho) and accept alternative hypothesis (H_1), i.e. there is a significant relationship between venture capital financing and SME profitability.

Hypothesis 2: Angel investment has no significant effect on SME growth

Table 4.3.5 Correlations of Angel Investment and SME Growth

			Angel Investment	SME Growth
Spearman's rho	Angel Investment	Correlation Coefficient	1.000	.291**
		Sig. (2-tailed)	.	.001
		N	120	120
	SME Growth	Correlation Coefficient	.291**	1.000

	Sig. (2-tailed)	.001	.
	N	120	120

**. Correlation is significant at the 0.01 level (2-tailed).

Table 4.3.5 shows that Angel Investment is independently and positively correlated with SME Growth and also significant at 1% level. As a result, the alternative hypothesis 2 of this study was accepted due to a correlation value (r = 0.291).

Decision

The above result implies that angel investment has a significant effect on SME growth i.e. since our r value (0.291) is positive and slightly significant. Thus, the decision would be to reject null hypothesis (Ho) and accept alternative hypothesis (H_1), i.e. angel investment has a significant effect on SME growth.

Conclusion

The SME landscape in Nigeria accounts for 90% of businesses; contributes 48% of Gross Domestic Product (GDP); consists of 43% female led enterprises and over 100,000,000 jobs. SMEs are classified as companies with labour force of 11 to 300 and a turnover of less than 100 million naira. Though SMEs have been the engine for growth in various developed and developing economies, they are always faced with problems. Access to finance, financial management skills and support is a major constraint that most SMEs face. Without proper finance, SMEs can neither expand to compete globally nor can they acquire technology or meet their fixed and working capital requirements (Wanjohi and Mugure, 2008).

This study focused on Business Finance and the development of Small and Medium Scale Enterprises in Odeda LGA, Abeokuta, Ogun State. This study was able to identify three equity finance sources (venture capital financing, angel investment and government grants) and their effect on SME development. Venture capital financing had the strongest impact on the development of SMEs followed by government grants and then angel investment.

Recommendations

Following the findings and conclusion, the study made the following recommendations:

(1) SMEs should endeavour to adopt the best financial structure to run their businesses thereby transforming the nation.
(2) SMEs should focus more on personal savings and debt financing first before thinking of equity financing as they are rarely accessible.
(3) Venture capital financing is very paramount in facilitating the profitability of SMEs.
(4) Government should encourage the grants and loans so that SMEs can grow and develop for further economic development
(5) Since SMEs are catalyst for economic development, angel investors and business philanthropist should be willing to fund small businesses for the achievement of goals and objectives.
(6) The business environment is a battle front full of competition; SMEs need to find other means and strategy that will bring about positive performance.

(7) Most small businesses should be able to effectively manage their funds and orientate employees on efficient financial management.

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