

**FINANCIAL MANAGEMENT: An Assessment of access to Financial Management Services by Small,
Medium and Micro Enterprises in Thohoyandou Business Centre
(Thulamela Municipality).**

By

NDOU MUHALI PIET

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Supervisor: Dr L. Beyers

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DECLARATION

I declare that the dissertation hereby submitted to the University of Limpopo, for the degree of Master of Business Administration (MBA) has not previously been submitted by me for a degree at this or any other university; that is my work design and in execution, and that all material contained herein has been duly acknowledged.

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M.P. Ndou (Mr)

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Date

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ABSTRACT

Small, Medium and Micro-Enterprises (SMMEs) as vehicles of growth, innovation and social transformation, are important categories of businesses which must be nurtured and harnessed by the South African authorities. This should enable them to quickly and effectively adapt to the challenges of globalization thereby benefiting the economy. The importance of SMMEs to the South African economy has already been acknowledged by government.

Despite the growth in venture capital funding, access to funding remains a problem for small enterprises, in particular for empowerment groups in South Africa. In most surveys among small enterprises, the provision of concessionary finance comes out as one of the most urgently felt needs. Indeed extensive research reveals that access financing is one of the several important factors that are critical for business survival and growth while other factors are market access and lack of financial management skills. South Africa's financial sectors have always been reluctant to provide comprehensive services for the fragmented, risk-prone and geographically dispersed small enterprises sector.

Evidence of management skills and business knowledge are indications of how well an entrepreneur can perform important tasks and activities related to the eight functions of a business, which are: general management, operations, finance, purchasing, human resources, marketing, administration and external relations.

One of the major hurdles that face entrepreneurial endeavours is the shortage of financial management skills. South Africa shows a grim picture of the skills gap. SMMEs become the hardest hit as the entire commerce sector forages for the scarcest skills. Small enterprises have been victims of instances of developing their employees only to lose them to bigger firms offering more lucrative incentives and currently SMMEs in South Africa's expanding construction sector are losing the fight in the battle for scarce skills.

Although government has tried to put in place policies and institutions with the aim of improving the accessing of finance by small business owners, their success has been minimal. It

is, therefore, imperative that management capability and financial management acumen be regarded as key to accessing funding by the entrepreneurs themselves, and the parties involved in supporting and promoting them.

It is important to bear in mind that training in entrepreneurial skills without training in business skills will not ensure optimal results. A combination of training to develop entrepreneurial skills and business training is most effective in preparing and developing successful entrepreneurs.

Therefore, this study is an assessment on access to financial management services by SMMEs in Thohoyandou Business Centre, as funding has a bearing on the economic development and sustainability of SMMEs. The research wanted to establish if the SMMEs in Thohoyandou Business Centre had access to financial management services support and, if they have, are the SMMEs ready to receive these financial management services?

The study revealed that the SMMEs do not possess financial management skills neither do they have access to financial management services although most of them acknowledged that there is a need for these skills for the success of their businesses. The lack of requisite bookkeeping and financial management skills results in most financial institutions being unwilling to provide funds to this sector, resulting in entrepreneurs relying on their own sources of finance which are limited as shown in the study.

Management capability strengthens the financial capacity of SMMEs. Financial institutions are prone to be favourably biased towards SMMEs who can demonstrate eloquence in areas such as financial management (including basic bookkeeping), marketing and technology upgrading. It is recommended that government and other facilitators incorporate simplified components into their training packages to cover such areas as bookkeeping and compilation of business plans.

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CHAPTER 1

INTRODUCTION AND ORIENTATION TO THE STUDY

1.1 Introduction

Small businesses have a major role to play in the South African economy, in terms of employment creation, income generation and poverty alleviation. According to Statistics SA (2006), small businesses account for more than 60 % of all employment in the economy. In addition, they are the main source of opportunities for income generation for the low income section of the population. The increasing consensus on the importance of small, medium and micro enterprises (SMMEs) in developing economies has led to a wealth of literature on the subject. The contributions range from broad policy-based proposals to specific case studies regarding the need for further business development services.

The development of SMMEs contributes significantly to job creation, social stability and economic welfare across the globe (Ladzani and Van Vuuren, 2002:2). In the United States of America (USA) for example, SMMEs have introduced innovative products and services, created new jobs, opened foreign markets, and in the process ignited the USA's economy into regaining its competitive edge in the global economy (Scarborough and Zimmerer, 1996:10). Japan's SMMEs sector accounts for the bulk of the country's business establishment, providing vital support for employment, for regional economies and, by extension, for the day-to-day life of the Japanese people (Ministry of International Trade and Industry, 1997:11). In Taiwan, the SMMEs sector generates approximately 98 percent of the economy's GDP. Although these businesses are relatively small in scale, have limited funds, and are weak in structure, they make

significant contribution to national economic prosperity, create innumerable jobs and promote social stability (Scarborough and Zimmerer, 1996:12).

In South Africa, SMMEs development was identified by government as a priority in creating jobs to solve the high unemployment condition. There is evidence that the national unemployment level currently estimated at 28.4 percent (Statistics South Africa 2004:1), is increasing at an alarming rate. According to the Ntsika Annual Review (2001:111), SMMEs constitute 97.5 percent of all businesses in South Africa. This sector generates 34.8 percent of the Gross Domestic Product (GDP), contributes 42.7 percent of the total value of salaries and wages paid in South Africa, and employs 54.5 percent of all formal private sector employees (Diederichs, 2001:64). The gap between high and low income groups is increasing fundamentally over time and small businesses and entrepreneurial development may serve as a facilitator in filling economic gaps.

Given South Africa's legacy of big business and constrained competition, the small business sector is seen as an important force to generate employment and more equitable income distribution, activate completion, exploit niche markets, enhance productivity and technical change, and thereby stimulate economic development. The Ministry of Trade and Industry (1994:11) emphasizes the problem of accessing small business finance, mentioning that for many years only 8 percent of total credit in South Africa went to previously disadvantaged individuals while 82 percent went to non-previously disadvantaged individuals. The reason mentioned pertaining to the lack of access to financing is that the requirements of lending institutions made it difficult for Blacks, Indians and Coloureds to get credit.

Despite the growth in venture capital funding, access to funding remains a problem for small enterprises, in particular for empowerment groups in South Africa. In most surveys among small enterprises, the provision of concessionary finance comes out as one of the most urgently felt needs. Yet, extensive research reveals that access financing

is one of the several important factors that are critical for business survival and growth; the other factors are market access and lack of financial management skills (Ministry of Trade and Industry, 1994:24). South Africa's financial sector has always been reluctant to provide comprehensive services for the fragmented, risk-prone and geographically dispersed small enterprises sector (Ministry of Trade and Industry, 1994:25).

SMMEs are a major feature of the economic landscape in all developing countries today (Liedhom and Mead, 1999). The contribution of these enterprises to the creation of jobs and to the alleviation of poverty has been recognised by many developing world governments, including the South African Government. They have been given prominence in many development plans as well as in the strategies of many donors. From 1995 the democratic government of South Africa, through its various departments has initiated some SMMEs development programmes by which it awards certain levels of its construction projects to the historically disadvantaged black SMMEs in order to enable development of competent skills, build viable SMMEs, create jobs and redistribute wealth (Department of Public Works, 1996).

Levinsky (1996:1) indicates that virtually all countries, at whatever stage of economic development, recognise the importance of SMMEs and the need to support their development. SMMEs contribute more than 90% of employment opportunities in many countries, are responsible for revenue creation and poverty alleviation, and are a source for creativity and innovation. The SMMEs sector, when adequately supported, could see many countries realising their dreams of improving their economies.

Following South Africa's democratisation in 1994, the government has increasingly sought to include SMMEs in its strategy for nationwide economic development. Although the initial strategic framework for these policies has undergone several revisions since the early 1990s, the government's perception of the role of SMMEs remains essentially unchanged. They perceive SMMEs to be important role players in

three areas: increasing international economic competitiveness; creating employment; and facilitating wealth redistribution (Rogerson, 2004; White Paper, 1995). Kespers (2000) and Berry *et al.* (2002) have led important efforts to understand the economic contribution of SMMEs in South Africa. These studies have provided illuminating reviews of government policy and overall growth trends. Chandra *et al.* (2001) indicate that despite earnest efforts on the part of the government, SMMEs have struggled to achieve forecasted levels of job growth and profitability. Government efforts to address the non-financial needs of SMMEs in South Africa have had limited effect. It has been noted that the majority of government services provided have offered very little value, from the perspective of entrepreneurs themselves (GEM, 2003).

Chandra *et al.* (2001) observe that SMMEs are financially more constrained than large firms and less likely to have access to formal finance. The study addressed two main issues relating to the growth and development of SMMEs in South Africa: lack of financial management skills and lack of access to finance. The lack of financial management skills is one of the obstacles affecting the growth of SMMEs in South Africa.

This study made an assessment on access to financial management services by SMMEs in Thohoyandou Business Centre, as this has a bearing on the economic development and sustainability of SMMEs. The research wanted to establish if the SMMEs in Thohoyandou Business Centre had access to financial management services support and, if they have, are the SMMEs ready to receive these financial management services?

1.2 Problem Statement

The problem investigated in this study was to do with the inability of SMMEs, in Thohoyandou Business Centre, to access financial management support services that would enable them to effectively and efficiently run their businesses.

1.3 Aim of the Study

The study is aimed at investigating, identifying and describing the challenges impeding the access to financial management support services by SMMEs in the Thohoyandou Business Centre. Given the proven relationship between sound financial management practices and a business's likelihood of obtaining financing, businesses who procure some form of external financial management services are also more likely to obtain loan finance; the study therefore also recommends relevant financial management practices to be implemented by SMMEs in order for them to be able to run their businesses properly.

1.4 Objectives

The study aimed at achieving the following objectives:

- To establish and describe the state of readiness of SMMEs in terms of receiving financial management support services;
- To identify and describe the challenges faced by SMMEs in the Thohoyandou Business Centre in accessing financial management services and
- To recommend relevant financial management services to be accessed by SMMEs.

1.5 Research Questions

The following main research question guided this study: “What are the challenges faced by SMMEs in accessing financial management support services?” In an attempt to provide answers to this question, the following research sub-questions were formulated and used during the investigation:

- Does there appear to be a need for further or better external support in the area of financial management in the SMMEs’ sector?
- What indicators exist, if any, to suggest that existing external financial management service providers help SMMEs to achieve financial health?
- Does the access of such support lead, in turn, to a greater probability of qualifying for loan finance from the formal financial sector?
- What barriers exist which may be impeding access to financial management services by SMMEs in Thohoyandou Business Centre?

1.6 Significance of the Study

The Global Entrepreneurship Monitor (GEM) conducted a study in an effort to shed further light on the difficulties which previously disadvantaged entrepreneurs encounter when applying for finance. The report aimed to better understand the financial management practices of South African entrepreneurs; and, in turn, to identify whether good financial management practices have a positive effect on an entrepreneur’s ability to secure a loan (GEM, 2003:47).

The study concluded that there is a worrying dearth of financial administration skills amongst previously disadvantaged entrepreneurs. Further, the study identified a positive relationship between firms that adopted sound financial management practices, and their ability to procure financing. Banks evidently prefer to channel finance, via term loans, to entrepreneurs that adopt good financial practices. More than

70% of entrepreneurs who had implemented the four essential financial management practices were successful in applications for loan finance. The report calls for further financial management support, which caters specifically to the financial administration needs of SMMEs (GEM, 2003: 48).

There is a need to view and understand the access-to-finance dilemma in a broader context. The reluctance of financial institutions to advance loans or overdrafts to small business is not just based on alleged conservatism of commercial or racially biased financiers. "It is the result of their experience with poorly motivated loan applications, frequent lack of systematic business plans and realistic market assessments, statistically verified high rate of small business failure and irrecoverable collateral, and other complications which make small business finance by banks difficult" (Ntsika Annual Review, 2002:111).

Given this background, it is important to look at the obstacles that small business owners face in terms of access to start-up finance. Conversely it has been noted that one way to address the problem of access to finance is to focus on improving the financial management practices of entrepreneurs (Oxford, Wood, Fischer, Herrington and Segal (2003:47).

Seeking to make finance more easily available, especially in businesses with inadequate administrative and management practices, is unlikely to result in optimal use of the relatively scarce resources. Rather, it is likely to have an added undesirable result of increased numbers of highly indebted and bankrupt entrepreneurs. It is therefore important to assess the current situation of the South African financial sector and come up with possible solutions that will help increase the financial success of small businesses and hence improve income and wealth distribution (Kirby and Watson (2003:100).

The significance of this study lies in its attempt to evaluate access to financial management support services by SMMEs, an investigation which has not received adequate attention in past research. This study, will therefore, be crucial in contributing to the body of knowledge and closing the knowledge gap which has been identified. In an attempt to close this gap, the study will identify and describe the readiness as well as barriers to access to financial management services by SMMEs in Thohoyandou Business Centre. The findings of the study are expected to assist SMMEs in accessing financial management services that are at their disposal for consumption and also encourage SMMEs to apply good financial management practices in their businesses.

1.7 Shortcomings of the study

There has been much research into the primary issues of accessing SMME financial management services in South Africa. The lack of research on a secondary level indicates omissions in available literature. However, access of financial management services has been researched extensively in other countries. As a result, this study endeavoured to create a platform to highlight the current position of entrepreneurs in their effort to access financial management services, especially during such businesses' developmental phase. Also most of the entrepreneurs contacted were from small size firms and very few from the micro and medium firms. Most are survivalist industries and are therefore not formally registered. Further research is therefore suggested as a means of establishing the specific relationship and correlated variables presented by the findings of the entrepreneurs.

1.8 Outline of the Research Report

The findings of the study will be presented as a research report in the following research format:

- **Chapter 1: Introduction and orientation to the study**

The first chapter presents an overview of the study, the background to the study, the problem statement, the motivation for the study, the aims and objectives of the study, and the research questions asked, and also a discussion of the significance of the study.

- **Chapter 2: Literature Review**

The second chapter presents a review of relevant literature with a view to positioning the study within the existing theoretical body of knowledge. In this chapter preliminary findings based on relevant literature are formulated. The chapter also sheds light on the type and nature of questions suitable for the collection of data for the study.

- **Chapter 3: Research Design and Methodology**

The third chapter of the research report presents a detailed outline of the research design and methodology adopted in the study. The choice of a specific research design and specific research methodologies is also justified in terms of the nature of the study conducted.

- **Chapter 4: Data Analysis and Interpretation**

In chapter 4 the data collected by means of various techniques are presented, analysed and interpreted.

- **Chapter 5: Conclusions, Recommendations and Summary**

Chapter 5 is dedicated to the conclusions, the recommendations and a summary based on the findings. The findings from the empirical investigation are compared with the findings of the literature review in order to ascertain whether new knowledge has come to light as a result of the investigation. Possibilities for further investigations which were identified during the study are also highlighted in this chapter.

1.9 Conclusion

The lack of sufficient financing is always a serious constraint during the formation and later stages of new ventures , as business may requires not only initial but additional inflows of capital to support expansion and growth (Nieuwenhuizen and Groenewald, 2004:9). Inadequate bookkeeping is also responsible for deficiencies in several other areas of financial management.

Although support providers are in place, certain small businesses and prospective entrepreneurs, through either ignorance or lack of information could still remain ignorant of the availability and accessibility of these support systems. In an investigation into programmes being used in South Africa to develop the SMME sector, Pretorius and Van Vuuren (2003 :519) found that core focuses of programmes from Khula, IDC and SEDA include finance, growth, expansion and competitiveness (through export) that are more relevant for existing businesses than for start-ups. There is a tendency of Khula, IDC and DTI programmes to focus on the larger and existing ventures as their target audience. Very few programmes are aimed at micro and small enterprises.

CHAPTER 2

LITERATURE REVIEW

2.1 Introduction

This chapter will review appropriate theoretical paradigms on the research topic of access to financial management services by SMMEs. The researcher will review previous literature on access to financial management services by seeking some tentative guidelines and possible solutions to the research problem. The literature review guided the researcher in the design of questionnaire, aiding him to focus his questions on critical aspects of the literature so as to ensure the best results.

Where financial management services have been tackled in the literature, they are typically within the context of a larger context of business development services (BDS). Unfortunately, this pool of work is much smaller. Early work has been performed by the International Labour Office in an effort to assess markets for BDS which are broad in nature; these efforts provide a number of insights into international BDS provision. Miehlbradt tests preconceived notions about developing BDS markets, refuting the idea that clients pick programs solely based on price, or that all BDS markets in developing countries are weak (Miehlbradt, 2006).

One of the major hurdles that face entrepreneurial endeavours involves the shortage of financial management skills. South Africa has a grim picture of the skills gap. SMMEs become the hardest hit as the entire commerce sector forages for the scarcest skills. Small enterprises have been affected by instances of developing their employees only to lose them to bigger firms offering more lucrative incentives. SMMEs in South Africa's expanding construction sector, for example, are losing the fight in the battle for scarce skills (Loveman and Sengenberger 1990:8).

2.2 Entrepreneurship

As a field of study, entrepreneurship has been undergoing expanded and updated definitions that include the need to more precisely explore who creates new business opportunities for the manufacture of goods and services (Alstete, 2002:223). The notion of value creation through new ventures is common to most definitions. However, literature shows that there exists no generally accepted definition of entrepreneurship. The following are some of the definitions which were deemed sufficient for the purposes of this study:

- “Entrepreneurship is the act of forming a new organization of value” (Bateman and Snell 1996:208).
- “Entrepreneurship can also be defined as the process of an innovative economic organization (or network of organizations) for the purpose of gain under conditions of risk and uncertainty” (Dollinger, 1995:7).
- “Entrepreneurship is the process of conceptualizing, organizing, launching and through innovation-nurturing a business opportunity into a potentially high growth ventures in a complex, unstable environment” (Rwigema and Venter; 2004:6).
- “Entrepreneurship is the process that causes changes in the economic system through innovations of individuals who respond to opportunities” (Nieman, *et al.* 2003:9).
- “Any attempt at new business or new venture creation, such as self employment, a new business organization, or the expansion of an existing business, by an individual, teams of individuals or established businesses” (DTI, 1998:1).

Entrepreneurship embraces the emergence and growth of new businesses. It is also the process that causes changes in the economic system through innovations of individuals who respond to opportunities in the market. These definitions, when integrated, provide an opportunity to capture as broadly as possible the critical aspects of entrepreneurship. For instance, self-employment is explicitly recognized as one

manifestation of entrepreneurship. It takes note of the critical aspect of entrepreneurship which has an important bearing on sustainable job creation, in particular-establishing sustainable business (Foxcroft *et al*, 2002:16).

The final point to make with regards to the definition of entrepreneurship for the purposes of this research is that, entrepreneurship extends beyond individuals and groups to organizations, society and culture. Thus in a broad sense entrepreneurship is regarded as a set of qualities and competencies that enable individuals, organizations, societies and cultures to be flexible, creative and adaptable in the face of challenges, and contributes to rapid social and economic change (Bukula, 2002:2).

Thus, entrepreneurs spot an opportunity, marshal resources and organize these into a venture the offers something new or improved to the market. However, an important distinction has to be made between entrepreneurship and small business management. Wickham (1998:24) believes that, although entrepreneurial ventures and small businesses pursue the same objectives, there are some fundamental differences between the two as shown in the table below:

Table 2.1 Distinction between entrepreneur and small business owner

| Entrepreneurs | Small business owners |
|--|---|
| Are innovative and are creators of new products, processes and technology | Operate with established products |
| Ventures have high growth potential | Normally operate in an established market |
| Ventures are concerned with growth targets, market development and positioning | Are concerned with sales and profits |

Source: Wickham (1998:24)

For the purposes of this study, both entrepreneurs and small business owner-managers will be considered, as financial management services are required in both ventures. An

understanding of the definition of entrepreneurship highlights the importance of the processes that entrepreneurs will follow to achieve their goals.

2.3 Small and Medium Sized Enterprises: Definitions

Enterprises are entities that provide existing or new products or services, in the same way as the others or with more efficiency and effectiveness through the use of improved processes and technologies (<http://www.thefreedictionary.com/enterprise>). The definition of small businesses varies from one country to the other. Various definitions have been provided based on varied criteria. Among the common criteria used are the numbers of employees, gross assets, turnover, and investment level.

2.3.1 World Bank Group

According to the World Bank Group, Small and Medium Enterprises (SMEs) are classified as follows:

- Micro-enterprise: up to 10 employees and total assets and turnover of \$ 100
- Small enterprise: up to 50 employees and total assets and turnover of \$ 3 million
- Medium enterprise: up to 300 employees and total assets and turnover base of \$ 15 million

Table 2.2 Categorization of SME

| | Manufacturing | Service | Agriculture |
|--------------|----------------------------|----------------------------|-----------------------------|
| Micro | Less than 5 employees | Less than 5 employees | Less than 5 employees |
| Small | Between 5 and 50 employees | Between 5 and 19 employees | Between 20 and 50 employees |

| | | | |
|---------------|-------------------------------------|------------------------------------|------------------------------------|
| Medium | Between 51 and 150 employees | Between 20 and 50 employees | Between 20 and 50 employees |
|---------------|-------------------------------------|------------------------------------|------------------------------------|

Source: World Bank Group Classification (Small and Medium size Enterprises) 2003

2.3.2 European Commission

The European Commission has adopted a new definition to update the version in place since 1996. The revised definition maintains the different staff thresholds for micro-, small and medium-sized enterprises. However, the criteria provide for substantial increases in the ceilings for company turnover and balanced sheet totals.

The European Commission adopted recommendation 2003/361/EC on 6th May 2003, to take effect from 1st January 2005 (published in OJL 124 of 20.05.2003: 36). The commission has a third category called 'Micro Enterprises'. A micro enterprise has a headcount of less than 10, and a turnover or balance sheet total of not more than €2 million. A small enterprise has a headcount of less than 50, and a turnover or balance sheet total of not more than €10 million. A medium-sized enterprise has a headcount of less than 250 and turnover of not more than 50 €50 million or a balance sheet total of not more than €43 million. The Commission considers the application of this definition by Member States, European Investment bank (EIB) and the European Investment Fund (EIF) as an aid to improving consistency and effectiveness of policies targeting SMEs. Recommendation 2003/361/EC allowed in Article 9 for the application of the definition to be reviewed in March 2006. Depending on the results, the Commission may adapt it, particularly the ceilings for turnover and balance sheet totals. Work has been done on considering the reporting burdens for micro enterprises, and as a result it is proposed that the burden be relieved for those with a balance sheet total of less than €500 or net turnover of less than €1 000. The proposed directive was reported in Com (2009) 83 final/2.

Table 2.3 Summary of SME Definition

| | Now | As from 1/1/2005 |
|--------------------|--|--|
| Micro enterprises | Employees < 10 Annual turnover: not defined or Balance sheet: not defined | Employees < 10 Annual turnover: < 2 Mio Euro or Balance sheet: < 2 Mio Euro |
| Small enterprises | Employees < 50 Annual turnover: < 7 Mio Euro or Balance sheet: < 5 Mio Euro < 25% of its capital or voting rights controlled by a public body | Employees < 50 Annual turnover: < 10 Mio Euro or Balance sheet: < 10 Mio Euro < 25% of its capital or voting rights controlled by a public body |
| Medium enterprises | Employees < 250 Annual turnover: < 40 Mio Euro or Balance sheet: < 27 Mio Euro < 25% of its capital or voting rights controlled by a public body | Employees < 250 Annual turnover: < 50 Mio Euro or Balance sheet: < 43 Mio Euro < 25% of its capital or voting rights controlled by a public body |

Source: European Commission 2003/361/EC

2.3.3 UK

In the UK, sections 382 and 465 of the Companies Act 2006 define a SME for the purpose of accounting requirements. According to this, a small company is one that has a turnover of not more than £6.5 million, a balance sheet total of not more than £3.26 million and not more than 50 employees. A medium-sized company has a turnover of

not more than £25.9 million, a balance sheet total of not more than £12.9 million and not more than 250 employees. It is worth noting that even within UK; this definition is not universally applied.

The British Bankers Association (BBA) embeds its own definition within the introduction of its voluntary code, The Business Banking Code (March 2008). Here, small business customers are defined as sole traders, partnerships, limited liability partnerships and limited companies with an annual turnover of under £1 million, as well as associations, charities and clubs with an annual income of under £1 million. If the concern applying for the business account is a group of business, the turnover threshold applies to the combined turnover of a group of limited companies within the group (<http://www.ec.eu/enterprise/enterprise>).

2.3.4 USA

In the USA, the definition of 'small business' is set by a government department called the Small Business Administration (SBA) Size Standards Office. The SBA uses the term "size standards" to indicate the largest a concern can be in order to still be considered a small business, and therefore able to benefit from small business targeted funding. The concern cannot be dominant in its field, on a national basis; it must also be independently owned and operated. Unlike the UK and European Union which have simple definitions applied to all industries, the US has chosen to set size standards for each individual NAICS coded industry. This variation is intended to better reflect industry differences. The most common size standards are:

- 500 employees for most manufacturing and mining industries;
- 100 employees for wholesale trade industries;
- \$7 million of annual receipts for most retail and service industries;
- \$33.5 million of annual receipts for most general & heavy construction industries and

- \$0.75 million of receipts of most agricultural industries.

Approximately one quarter of industries have a size standard that is different to those listed above. The most recent scheme was originally produced in 2002, but has had amendments integrated on a rolling basis. Both the US and EU generally use the same threshold of fewer than 10 employees for small offices (<http://www.census.gov/epcd/www/smallbus.html>).

2.3.5 India

In India, the Micro and Small Enterprises (MSEs) sector plays a pivotal role in the overall industrial economy of the country. It is estimated that in terms of value, the sector accounts for about 39% of the manufacturing output and around 33% of the total export of the country. Further, in recent years the MSE sector has consistently registered higher growth rate compared to the overall industrial sector. The major advantage of the sector is its employment potential at low capital cost. As per available statistics, this sector employs an estimated 31 million persons spread over 12.8 million enterprises and the labour intensity in the MSE sector is estimated to be almost 4 times higher than the large enterprises (http://msme.gov.in/msme_aboutus.htm).

2.3.6 South Africa

In South Africa the term 'SMME', for Small, Medium and Micro Enterprises, is used. Elsewhere in Africa, 'MSME' is used, for Micro, Small and Medium Enterprises. Definition for SMEs is often considered an obstacle for business studies and market research. Definitions used today define thresholds in terms of employment, turnover and assets. These definitions also incorporate a reasonable amount of flexibility around year-to-year changes in these measures so that a business qualifying as an SME in one year can have a reasonable expectation of remaining an SME in the next.

Writing in *African Insight*, Prof Chris Rogerson categorised businesses into three sets of enterprises:

- **Survival Enterprises of the Informal Economy**

“These are the sets of activities undertaken primarily by unemployed black people unable to find regular employment,” he wrote. According to Prof Rogerson, here incomes usually fall short of minimum standards, little capital is invested, skills training are minimal and there are scant opportunities for upward growth into a viable small business enterprise.”

- **Micro-Enterprises**

“These are very small enterprises, often involving the owner, some family members and at most, one to four employees,” Prof Rogerson explained. “Although such businesses frequently lack the trappings of ‘formality’ in terms of licences or formal premises, and entrepreneurs sometimes have only rudimentary business skills or training, many (though not all) micro-enterprises will make a transition into viable formal small businesses,” he added.

- **Small and Medium Enterprises (SME)**

These entities constitute the basis of the formal SME economy, according to Prof Rogerson. Their employment levels, he wrote, range between five and 100 workers for small ones and up to 200 to medium-sized ones. “Such enterprises are usually owner-managed, operate from fixed premises and fulfil all the trappings associated with formality,” Prof Rogerson concluded.

According to the National Small Business Act 102 of 1996, a small business means a separate and distinct business entity, including co-operative enterprises and non-governmental organizations managed by one owner or more which includes its branches or subsidiaries, if any, and is predominately carried on in any sector or sub-sector of the economy, which can be classified as a micro, a very, small or medium enterprise.

This study uses the definition of small business provided by the National Small Business Act 102 (1996):

“a separate and distinct business entity, including cooperative enterprises and non-governmental organisations, managed by one owner or more which, including its branches or subsidiaries, if any, is predominantly carried on in any sector or sub-sector of the economy”.

In addition to the above definition, the study includes survivalist businesses (informal businesses), as they play a vital role in rural economies (SEDA, 2006). The survivalist businesses have been defined as “enterprises generating income that is less than the minimum income standards or poverty line”. These one-person businesses operate with minimal asset value and have no paid employees. This category comprises subsistence farmers, street hawkers, and corner shops, among others. The main economic activity of these is for survival of the owner and the family. In this study the term “small business” is used synonymously with SMMEs. The National Small Business Act 102 (1996) also classifies small businesses into four main categories using three parameters: full-time employees, turnover, and asset value. Table 2.4 shows this classification per industry sector.

Table 2.4 Thresholds for the classification: micro, very small, small or medium enterprise.

| Sector or sub sector in accordance with the Standard Industrial Classification | Size of classes | The total number of full-time equivalent of paid employees Less than: | Total turnover (Rm) Less than: | Total gross asset value (fixed property excluded) (Rm) Less than: |
|---|------------------------|--|---|--|
| Agriculture | Medium | 100 | 5.00 | 5.00 |

| | | | | |
|--|------------|-----|-------|-------|
| | Small | 50 | 3.00 | 3.00 |
| | Very small | 10 | 0.50 | 0.50 |
| | Micro | 5 | 0.20 | 0.10 |
| Mining and Quarrying | Medium | 200 | 39.00 | 23.00 |
| | Small | 50 | 10.00 | 6.00 |
| | Very small | 20 | 4.00 | 2.00 |
| | Micro | 5 | 0.20 | 0.10 |
| Manufacturing | Medium | 200 | 51.00 | 19.00 |
| | Small | 50 | 13.00 | 5.00 |
| | Very small | 20 | 5.00 | 2.00 |
| | Micro | 5 | 0.20 | 0.10 |
| Electricity, Gas and Water | Medium | 200 | 51.00 | 19.00 |
| | Small | 50 | 13.00 | 5.00 |
| | Very small | 20 | 5.00 | 1.90 |
| | Micro | 5 | 0.20 | 0.10 |
| Construction | Medium | 200 | 26.00 | 5.00 |
| | Small | 50 | 6.00 | 1.00 |
| | Very small | 20 | 3.00 | 0.50 |
| | Micro | 5 | 0.20 | 0.10 |
| Retail and Motor Trade and Repair Services | Medium | 200 | 39.00 | 6.00 |
| | Small | 50 | 19.00 | 3.00 |
| | Very small | 20 | 4.00 | 0.60 |
| | Micro | 5 | 0.20 | 0.10 |
| Wholesale Trade, Commercial Agents and Allied Services | Medium | 200 | 64.00 | 10.00 |
| | Small | 50 | 32.00 | 5.00 |
| | Very small | 20 | 6.00 | 0.60 |
| | Micro | 5 | 0.20 | 0.10 |
| Catering, | Medium | 200 | 13.00 | 3.00 |

| | | | | |
|---|------------|-----|-------|------|
| Accommodation and other Trade | Small | 50 | 6.00 | 1.00 |
| | Very small | 20 | 5.10 | 1.90 |
| | Micro | 5 | 0.20 | 0.10 |
| Transport, Storage and Communication | Medium | 200 | 26.00 | 6.00 |
| | Small | 50 | 13.00 | 3.00 |
| | Very small | 20 | 3.00 | 0.60 |
| | Micro | 5 | 0.20 | 0.10 |
| Finance and Business Services | Medium | 200 | 26.00 | 5.00 |
| | Small | 50 | 13.00 | 3.00 |
| | Very small | 20 | 3.00 | 0.50 |
| | Micro | 5 | 0.20 | 0.10 |
| Community, Social and Personal Services | Medium | 200 | 13.00 | 6.00 |
| | Small | 50 | 6.00 | 3.00 |
| | Very small | 20 | 1.00 | 0.60 |
| | Micro | 5 | 0.20 | 0.10 |

Source: Schedule 1 to the National Small Business Act, 1996, as revised by the National Small Business Amendment Bill, March 2003.

Definitions of SMMEs are difficult to discern since the labour and capital intensity of enterprises vary so widely. Some credit lines also differentiate SMMEs by net asset size or turnover; each of these has their unique limitations.

Another enlightening definition in (South African Parliament's White Paper on National Strategy for the Development and Promotion of Small Businesses in South Africa, 1995) is that:

“Micro-enterprises are very small businesses, often involving the owner, some family member/(s) and at the most one or two paid employees. They usually lack formality in terms of business premises, operating permits and accounting procedures. Most of them have a limited capital base and rudimentary technical or business skills amongst their operators. However, many micro-enterprises advance into viable small businesses.

Earning levels of micro-enterprises differ widely, depending on the particular sector, the growth phase of the business and access to relevant support.

Small enterprises constitute the bulk of the established businesses, with employment ranging between five and about fifty. The enterprises will usually be owner-managed or directly controlled by the owner-community. They are likely to operate from business or industrial premises, be tax-registered and meet other formal registration requirements. Classification in terms of assets and turnover is difficult, given the wide differences in various business sectors like retailing, manufacturing, professional services and construction.

Medium enterprises constitute a category difficult to demarcate vis-a-vis the “small” and “big” business categories. It is still viewed as basically owner/manager-controlled, though the shareholding or community control base could be more complex. The employment of 200 and capital assets (excluding property) of about R5 million are often seen as the upper limit.

For the purposes of this study and resulting from information gathered, the following categorization can be taken to be representative of the majority of the respondents’ definition of SMMEs:

Table 2.5 Categorization of SMMEs

| Type of business | Number of people employed |
|-----------------------------|-----------------------------|
| Micro-enterprises | A staff of less than 5 |
| Very Small-scale enterprise | Staffing between 6 and 10 |
| Small | Staffing between 11 and 50 |
| Medium - enterprise | Staffing between 51 and 200 |

The above stated figures are inclusive of the proprietor(s).

2.4 SMMEs as Major Employment Creators – evidence from Industrialized Countries

In many industrialized countries, 1970s and 1980s witnessed the re-emergence of the small business sector due to two major events. First, spectacular cases of large enterprises running into economic difficulties and shedding employment arose in nearly all industrialized countries, while the latter's small business sectors (or parts of it) went relatively well through the period of economic turbulences that started in the early 1970s. Second, Birch's (1987) finding that small businesses created the majority of new jobs in the United States, spread quickly around the world and provoked an upsurge in research on employment shifts towards smaller businesses.

The Organization of Economic Co-operation and Development (OECD) countries which accounts for over 75% of the world output, concluded in 1985 that, in several of its member states, a tendency towards the concentration of workers in small businesses could be found, even after accounting for shifts in industrial structure or sectoral composition (OECD, 1985). Reviewing data on employment shares by enterprises size for nine industrialized countries, Loveman and Sengenberger (1990:8) confirm that,

“Despite significant cross-national differences in the size distribution and despite methodological caveats, the employment share of small enterprises has reversed a downward trend that had prevailed for many decades and risen significantly. Taken together, the case studies present a convincing case for shift in employment to smaller units of production”.

According to Harrison (1994), it is important to guard against rushing into premature and overly general conclusions as to the economic implication of the shift toward smaller units. Job generation studies show that the employment dynamics accompanying new business formations and business closures is very important to net employment contribution of smaller businesses. Many of the recent firm births in industrialized countries may have been induced by poor economic conditions in general and by high unemployment in particular. Those undertaken as “last-ditch” attempts to provide livelihood for the founder may rest on

especially shaky ground and their rate might therefore be expected to be dependent employment or that bad times will topple the weak businesses (Sengenberger *et al.*, 1990).

Nevertheless, it has been acknowledged that a large majority of business units in industrialized countries are small, and even a conservative review of job generation literature suggests that small businesses account for at least a proportional share of employment creation. The net new jobs created in small businesses, however, result from a very dynamic process of expansion and contraction within the small business sector. While some small businesses start and remain small throughout their existence, others experience stages of growth, and senescent businesses even decline (Timmons, 1994). Large employment gains occur seemingly only in a few small businesses (Sengenberger *et al.*, 1990).

2.5 SMMEs as Major Employment Creators – the Experience in African Countries

In Africa, as well as in other less developed countries, SMMEs (and micro enterprises in particular which constitute their majority) have received mounting attention because of their labour absorptive capacity in times of both shrinking public sector and private formal economy, and increasing numbers of new labour entrants. With the shift of industrial policy away from import substations and of trade policy towards liberalization, SMMEs are moreover expected to respond flexibly and thus withstand global competition (Sengenberger *et al.*, 1990).

Virtually all SMMEs operate in conditions of excess supply of relatively unskilled and unorganized labour, which allows them to transfer burden of unstable markets on their employees and to base competition on squeezing labour costs rather than innovation or technological upgrading (Storper, 1991; Schmitz, 1995; McCormick, 1999). Unlike in South Korea, where large businesses function as catalysts of growth to their subcontractors, corporate subcontracting to small and mostly “informal” businesses, in Africa such situations are more than often a means to reduce costs by exploiting labour-surplus conditions and circumventing regulations and trade union organizations (McCormick, 1999).

Clusters of sector-specific businesses exist in Africa, but their growth experiences vary and differ markedly from other developing countries' cases, like the successful Sinos Valley shoe cluster in Brazil and the surgical instruments cluster in Saikot, Pakistan, or from the "model" industrial districts of Italy (Dawson, 1992).

Indeed, strong social ties and networking, reported to be essential for the success of industrial districts in Europe, have ambiguous effects on firm growth in Africa; while being supportive amongst the Igbo in Nigeria, research in Kenya suggest that the successful African entrepreneur has loosened his networks based on kingship and social ties in general (McCormick *et al.*, 1997). Furthermore, formal institutions in Africa face crises of legitimacy and enforcement by not being rooted in local culture and therefore are far from being conducive to enterprise growth (Dia, 1996).

The above suggest that models of competitions and growth trajectories of SMMEs vary across continents and countries (McCormick, 1999). Research findings on SMMEs throughout Africa are diverse, albeit they show widely that it cannot be enterprise size as such which determines the potential for success and failure of SMMEs to co-exist but instead point to the role of the entrepreneur (Sengenberger et al, 1990). The predominance of SMMEs in the industrial tissue, both in terms of numbers and employment opportunities generated, demonstrates that SMMEs form important economies and has found their own ways to deal with market instability and uncertainty. Nevertheless, the critical underlying issues of the viability of these small firms, and the sustainability and quality of the employment generated by them remain still unclear (McCormick *et al.*, 1997).

2.6 SMMEs as a Vehicle to Tackle the Problem of Unemployment-South Africa

Since the elections of April 1994, the issue of black economic empowerment and a more equal income distribution have been placed high on the agenda of the government of South Africa (Rogerson: 2004). Nevertheless, the need to take the South African economy onto "a

higher road”, i.e. a diversified economy in which productivity and international competitiveness are enhanced, wage-levels are raised, investment is stimulated and entrepreneurship flourishes, is recognised as a condition to address these issues successfully (RSA, 1994; 1995). In the 1995 White Paper on National Strategy for the Development and Promotion of Small Business in South Africa, the government assigns the SMME sector a key role in South Africa’s socio-economic transition (RSA, 1995:10). In particular, SMMEs are seen as vehicles to:

- Address the problem of high unemployment levels in South Africa as they have high labour-absorptive capacity;
- Activate domestic competition by creating market niches in which they grow until they identify a new niche as a response to demand changes and to be internationally competitive because of their flexibility;
- Redress the inequalities from the apartheid period, in terms of patterns of economic ownership and restricted career opportunities for black employees;
- Contribute to black economic empowerment in that the majority of SMMEs is reported to be initiated, owned or controlled by those members of society who were discriminated against in South Africa’s past and
- Play a crucial role in peoples’ efforts to meet basic needs in the absence of social support systems during restructuring processes, which refers in particular to South Africa’s micro-enterprise segment and especially survivalist activities characterized by low entry barriers for inexperienced job seekers.

2.7 Entrepreneurship in South Africa

The promotion and development of entrepreneurship in South Africa is currently the focus of much attention in a wide variety of fields because it is regarded as a major key to economic development and wealth creation, thereby contributing towards social prosperity and upward mobility. The demand for an entrepreneurial-driven economy in South Africa is

increasing, particularly because of the employment creation benefits it offers. The SMMEs sector is globally regarded as the driving force in economic growth and job creation (Nieman *et al.*, 2003:3).

The South African economy has declined over the past twenty years. The year on-year change in the value of real gross domestic product (GDP) determines the real growth rate of a country (Nieman *et al.*, 2003:4). In the 1960s South Africa's GDP averaged six percent per year. During the 1980s, the GDP decreased to 2.2 percent, with no growth in the 1990s. Lack of growth in the economy has led to fewer employment opportunities being available. This has given rise to high unemployment rate of about 30 percent. In creating wealth, small businesses in South Africa contribute approximately forty-two percent to the country's GDP (Nieman *et al.*, 2003:10).

According to the 1995 White Paper on Small Business Development, the goals of the South African SMME promotion strategy are:

- Economic growth and development;
- Poverty alleviation;
- Income distribution;
- Employment creation;
- Economic empowerment of previously disadvantaged population groups;
- Democratization of economic participation;
- Replacement of the present rather oligopolistic structure of the economy with one that allows a much higher degree of competition.

Through the National Small Business Act (1996) the South African government acknowledges the economic potential of a strong SMME sector and is committed to its promotion and growth. The government aims not only to increase the number of new ventures, but also to create an enabling environment to ensure the survival and growth of small businesses. According to Van Eeden, Viviers and Venter, (2003:13) the National Small Business Act (1996) has been instrumental in the creation of an enabling

environment by means of the provision made for financial and non-financial governmental assistance to all South African entrepreneurs.

The South African government support structures for SMMEs include the following:

- The centre for Small Business Promotion, established by the Department of Trade and Industry (DTI) at national level is responsible for SMMEs policy-related matters and support programmes.
- Small Enterprise Development Agency (SEDA) is responsible for non-financial services like marketing, training programmes, procurement advice, technology assistance, and mentoring of businesses. Most of these services are rendered to SMMEs through service providers, such as Tender Advice Centres (TACs) Manufacturing Advisory Centres (MACs), Local Business Services Centres (LBSCs), Non Governmental organization (NGOs) and Community Based Organizations (CBOs).

2.8 Access to Finance in South Africa

In 2006, the World Bank issued an assessment of the overall investment climate in South Africa. The report covers some of the largest obstacles facing the nation's business, and documents on the accessibility of finance for black businesses. As previously mentioned, "black owned businesses report significantly higher difficulty in accessing finance. African owned firms were far more concerned about access to credit and the cost of financing than European owned firms. This remains true even after controlling for other observable differences that might affect perceptions about access to financing such as enterprise size, sector of operation, and age". This finding buttresses the work of Chris Rogerson, who, in 1999, reported that as many as 85 % of emerging SMEs complained about lack of access to credit. This finding, however, was questioned by Oxford in 2004, which showed that by international standards, a

relatively high proportion of entrepreneurs in SA expect to obtain bank finance (GEM, 2004).

Berry *et al.* elaborate on these conclusions. Despite earlier work indicating that small and new firms have relatively good access to South African banks, Berry *et al.* report that these findings tend to “conceal a much more gloomy picture among African businesses, which represent only 7% of Levy’s sample and all complained about prejudices of banks against them (Berry *et al.* 2002). The piece goes on to describe the difficult dichotomy involved in assessing the financial predicament of South African entrepreneurs. “There is still lack of evidence,” they explain, “on whether this higher mortality is a cause or a consequence of the higher credit rejections, and whether the higher risks of these segments can be made up for on an accordingly higher return” as cited in (GEM, 2003:70). This is an important clarification since judging from the failure rates alone, it is difficult to know why previously disadvantaged SMEs struggle to access finance. The literature suggests that it could be the result of several phenomena, including: unreasonably high standards on the part of banks; lack of skills on the part of the entrepreneur; prejudice; or a combination of all of the above.

The lack of financial assistance to small business is the largest constraint on the growth of those small businesses. Numerous studies have shown that small and medium enterprises (SMMEs) are financially more constrained than large firms and are unlikely to have access to formal finance. But recently however, there was some evidence on the extent to which business size is a decisive factor in determining growth obstacles or access to finance (GEM, 2003:71).

Previous researchers divided the constraints into different sub-topics. Sievers and Van den Berg (2004) classified the problem into two parts, that is (1) financial constraint, access to finance, and growth, and (2) the importance of size of the business and the importance of the institutions. Many Indian entrepreneurs in East Africa and European enterprises in Southern Africa were asked to rate financial and other problems such as

infrastructure, crime, macroeconomic instability and corruption in terms of their impact on the operation and growth of their firms.

Small firms consistently report higher growth obstacles than medium-sized firms (Sievers and Van den Berg, 2004). The researchers show that size, age and ownership are the most reliable predictors of firms financing obstacles. They find that older, larger and foreign owned firms report lower financing obstacles. The relationship is not only statistically but also economically significant. Sievers and Van den Berg (2004) show that the probability that a small firm will list financing as a major problem is 39 % compared to 36% for medium size firms and 30% for large firms. The high financing problems that small firms report match evidence from developed and developing countries and this confirms the theory's prediction.

Even though access to finance and financial management skills are the major constraints on the growth of SMMEs, there are other constraints, which are a threat to the growth of SMMEs in South Africa (Ladzani, 2001; White Paper, 1995). As noted before, among others, these include:

- Poor quality education to previously disadvantaged South Africans;
- Unfavourable legal environment for example, tax burden and policy and regulations which are sometimes unfavourable for informal traders because existing stakeholders have not been fully engaged in the strategy behind the promotion of informal traders and benefits of regulating informal trade;
- Poor credit rating;
- Lack of access to information;
- Lack of innovation as most of them operate in the homogenous sector of businesses;
- Lack of access of markets and procurement;
- Lack of management skills;
- Lack of understanding of some business information and
- Lack of infrastructure especially in rural areas.

A study conducted by Thorsten and Alsi (2006) on the constraints of access to finance by SMMEs indicate that SMMEs face larger growth constraints and have less access to formal sources of external finance. They concluded that this situation is a hindrance to their growth and development more than larger enterprises. The study suggests the establishment of specialised financial institutions to assist SMMEs financially to alleviate some of the constraints, which in the end would enable them to compete with larger enterprises.

The primary challenge facing SMMEs is the access to finances. South Africa is full of people willing to start their small business, but they face a stiff challenge in terms of answering questions such as: where is the money going to come from? Some do have small portion of finance which they feel is not enough to cover all the business's operating expenses, which include rental of premises, personnel's wages, transport and so on.

Existing small enterprises face the same challenge; they complain of lack of financial opportunities to develop and grow their businesses. During 2007's SMMES Annual Summit, Technonet Africa urged South Africa to adopt the following experiences drawn from the Africa-Asia SME Network:

- Increase access to SMMEs' financing as they contribute at least 30 to GDP and provide more than 60% of employment opportunities;
- Mainstream financial institutions are beginning to open windows for SMME financing but not enough to meet the demand;
- Explore the Alternative Financing systems like the Guarantee Financing schemes, Trade Finance, Debt Finance, Venture capital, Equity Finance, raise funds from Capital Markets and
- Special funds with a complete package which includes training, business clinics, mentorship, business monitoring, walk in business information centres with "how to" kits.

Financing SMMEs in Africa has proved a mammoth task and sometimes a delayed, futile, and unproductive exercise because of lack of proper models of funding. Besides, rampant corruption, chaotic administration, economic and financial mismanagement, red tape and nepotism have made matters worse and complicated the whole process, delaying the development and growth of the small business. The 2010 FIFA World Cup might bring countless opportunities when it comes to funding SMMEs, proper and conventional procedures must be followed and right mechanisms must be put in place to ensure that benefits are maximised from this venture.

Efforts to promote SMME access to finance might have more impact on development and growth but access is limited and the cost of capital is high. While government has made some efforts to increase accessibility to finances, the targeted programmes have had limited success because awareness and usage of existing promotional programmes are very low. In addition to insufficient access, high interest rates also pose a constraint to micro enterprise growth. Moreover, there are reports that core difficulties are seen in terms of discrimination by financial institutions against micro enterprises with little collateral, difficulties in accessing information and lack of market exposure. The inadequacy of external finance at the critical growth/transformation stages of micro enterprises deters the enterprises with growth potential, from expanding (Thorsten and Alsi, 2006).

2.9 Financial Management

Financial management is about planning income and expenditure, and making decisions that will enable the enterprises to survive financially (<http://www.businessdictionary.com>).

Financial management includes:

- Financial planning;
- Financial accounting;

- Financial analysis;
- Financial decision-making and
- Action.

Financial planning is about:

- Making sure that the enterprise can survive;
- Making sure the money is being spent in the most efficient way;
- Making sure that the money is being spent to fulfil the objectives of the organisation and
- Being able to plan for the future of the organisation in a realistic way (<http://www.businessdictionary.com>).

Financial Accountability

In non-profit organizations, the money that the organization is using is held in trust - on behalf of the community that it serves. The money is not the personal possession of the individual staff members. They have to account for how they used the money, to show that it was used to benefit the community.

In a profit-making organization, it is easy to hold management accountable. We simply ask: Did they make a profit?

In a non-profit making organization we ask: Did they use the money to benefit the community in the best possible way?

Financial accountability can be broken down into two components:

Financial Accountability

Being able to account for the way the money is spent to:

- Donors,
- Boards and committees,

- Members, and
- The people whom the money is meant to benefit.

Financial Responsibility

- Not taking on obligations so that the enterprise cannot meet its intended objective,
- Paying staff and accounts on time and
- Keeping proper records of the money that comes into the enterprise and goes out (<http://www.businessdictionary.com>).

2.10 Financial Management Services

A 2003 study concluded by the GEM explored this idea further. In an effort to better understand the effect that financial administration skills have on access to finance, GEM put forth a study of the financial management practices of 224 black owned SMMEs in South Africa. The study sought to answer the following questions regarding SMME: What aspects of financial administration, if any, are deficient? How widespread are these deficiencies? What impact do these deficiencies have on the financial health of a business? Do these deficiencies influence an entrepreneur's ability to secure external finance?

The report suggests a worrying trend amongst the previously disadvantaged SMME community. "Overall, the financial state of a significant majority of businesses in this sample shows signs of being precarious. 45% of those businesses that have an overdraft facility had exhausted this facility in the last six months." In an effort to understand the effect of good financial management practices, the study surveyed entrepreneurs' financial procedures across a range of business activities. It determined that by implanting four procedures into their financial operating models, entrepreneurs could significantly enhance their financial health. The procedures included: keeping a cash book; keeping receivable record; keeping a record of inventory and performing proactive debtor management (GEM 2003).

The report concludes, that “a few relatively simple changes to the administration practices of owner-managed firms have the potential to improve significantly their cash position and reduce the probability of their overdraft being exhausted. Over 60% of these entrepreneurs could potentially benefit from training in these practices.” Most importantly, “The results demonstrate that nearly three quarters of entrepreneurs who proactively manage cash flows are successful in applications for bank loan finance. This implies that banks channel finance to the majority of firms that adopt good management practices”. This infers that increased understanding of financial support for previously disadvantaged entrepreneurs is of critical importance (GEM, 2003:43).

Sound financial management is an incontrovertible trait in business as it caters for the administering of the cash-flow, the balancing of costs and turnover versus business growth. This filter down to how much money should be spent on what; how much money should be spent on development, on the South African Reserve Bank Repo Rate is currently pegged at 7%.

In the SMMEs Survey barometer in South Africa sponsored by Standard Bank and Oracle Corporation in South Africa, which tracks the needs of the SMME market, researchers examined factors behind the competitiveness of SMMEs by polling 6 000 companies across vertical markets countrywide. Nikki Kearns, director of business banking at Standard Bank, warns that with rising interest rates, businesses across the board may find themselves targeting consumers who are no longer able to fully service their debt. “There has been an upturn in the prolonged low interest rates; Tito Mboweni has publicly stated that it is necessary to curb consumer spending. This can potentially leave SMMEs exposed to the possibility of bad debt,” she explains. “There is no getting away from the key success factors for starting a small business: passion for the business, knowing the market, a sound business plan, the ability to turn ideas into actions, planning for good times and bad and the ability to overcome adversity,” she says (GEM 2003:48).

Various programmes have been set up to empower business owners to combat the ills of poor financial management. Programmes like the Micro-MBA business training programme

come to mind. The programme equips business people with skills of business management with emphasis on financial management based on the perspective that all successful business owners should have good cash-flow management disciplines. The programme does not necessarily teach business owners about traditional bookkeeping and accounting methods, instead it teaches an easy-to-use cash flow management system that allows micro entrepreneurs to work out the correct allocations for all expenses and income and more importantly, how much they have to spend at each month end. SMMEs often operate without any visionary financial policies modelled to foster enterprises' sustainability, growth and diversification. This has often resulted in the proliferation of stagnant businesses with no indices of remarkable growth (GEM 2004).

Despite the general consensus on the importance of the private sector in delivering financial administration services, little research has been done on the effects of external service provision. Given the critical importance of SMMEs to national growth; the need for further and better financial management support amongst the previously disadvantaged entrepreneurial community; the significant effect which sound financial management practices have on the operating effectiveness of SMMEs and their ability to procure finance, further research is needed (GEM 2004).

2.11 Obstacles faced by the SMMEs sector

Sixteen years after the attainment of democracy, some of the SMMEs in South Africa appear not to have shaken off the legacy of apartheid, which had confined their access and spheres of activity to a very narrow segment of the economy. Within the formal sector SMMEs suffer from the structural weaknesses of the economy that wealth generation is concentrated in a limited number of sectors which do not have strong linkages with the rest of the economy. Also, these sectors contend with competition from established global competitors, whose greater size enables them to use predatory business practices to ward off competition. As a result the SMME sector is characterised by the incidence of a high

failure rate. It is estimated that the failure rate of SMMEs in South Africa is between 70% and 80% (Van Eeden *et al.* 2003:20). Both establishment and operational aspects of SMMEs are hampered by insufficiency of technology and managerial knowledge, the scarcity of financial resources, inadequate skill of the labour force, lack of information on markets and lack of basic education (Wickham 2004:50).

2.11.1 Training for SMMEs

Though the majority of SMME operations are not complex, it should be noted that a basic level of education is re-requisite for the successful management of the small business unit. This basic educational level is not usually the norm amongst, especially the micro and medium entrepreneurs, but is a factor found militating against them. On the part of the entrepreneur or small businessperson, there seems to be not enough practical or vocational training readily available for skills training and enhancement. Experts in South Africa isolate lack of education and training as South Africa's main weakness with regard to the enabling environment for entrepreneurship (Oxford *et al.* 2003:15).

2.11.2 Financial Constraints

In South Africa, not even short-term funds are easily available to the small entrepreneur. The social, economic, financial, legislative, political and banking systems, characteristic of the previous dispensation, have all combined to make financial problem in the SMME sector particularly difficult.

The government needs to assist in stimulating a greater diversity of alternative financial institutions that serve as vehicles for savings and loans to low and middle income individuals, as well as the self-employed.

Other obstacles that small firms frequently face include:

- **Marketing from a limited product range:** The small firms produce just one type of good or service – or at least a very limited range of them. This exposes them to problems should consumer taste and demand conditions change.
- **Difficulty in finding suitable and reasonably priced premises:** The best locations tend to be the expensive and often only affordable by large firms.
- **Lack of education:** In general terms, owners of SMMEs do not have the ability to present a proper budget case to potential financiers. They do not have the basic understanding of organisational strategy and financing needs that are essential for sustainable growth.
- **Problems in raising both short- and long-term finance:** Small firms have little security to offer banks in exchange for loans and this makes obtaining finance much more difficult than for larger firms. In addition, suppliers may be reluctant to sell goods on credit if the business has only been operating for a short time.
- **Inefficiencies:** Poor financial systems, lack of regulations and anti-competitive policies produce inefficiencies. Also, poor business processes and procedures and the existence of a “business as usual” attitude worsen the situation.
- Inadequate information regarding support structures which are available to SMMEs.
- Lack of timely access to up-to date and appropriate technology (Naude and Havenga, 2004:112).

2.12 SMME Support in South Africa

There are many constraints that hinder SMMEs from growing and developing in many countries. One of the many factors that have been identified as constraining small business development is access to business support and advice. Lack of awareness of the value of business support amongst entrepreneurs, or problems arising from the accessibility of

providers, with many located in urban areas, may be attributed to lower SMMEs support in rural areas (Nieuwenhuizen and Groenewald, 2004:13).

SMMEs support encompasses a wide range of assistance including business advice and information, training, financial assistance; and business networks and mentoring schemes. Business advice and information incorporate generic business start-up advice and support, business planning advice, development support, and consultancy and advice on business plans and business promotion (Smallbone, Baldock & Burgess, 2000). Training ranges from generic training to business planning courses and financial management training, whereas financial assistance can consist of advice on raising finance, provision of grants and funding, financial planning and management (Smallbone et al., 2000).

Training provides the opportunity for owner-managers to develop their management skills. Harrison (1994) state that with training facilities predominantly located in urban areas, many rural businesses are significantly disadvantaged in term of access, and many have little opportunity or funds to utilize formal training.

Levistky (1996 :19) indicate that the reservoir of knowledge and experience in technology, management and marketing skills that could be of help to SMMEs is to be found in various elements of the business community and beyond. Most private consultants, however, target larger enterprises or public bodies as their potential clients and provide less help to small businesses because of the high consultancy costs that SMMEs cannot afford.

The White Paper (1995:12) acknowledges that small business, compared to big business worldwide, faces a wide range of constraints and problems, even in effectively functioning market economies. These constraints relate mainly to the legal and regulatory environment, access to markets, finance and affordable rental for business premises, acquisition of skills and managerial expertise, access to appropriate technology, quality of the business infrastructure and managerial expertise, access to appropriate technology, quality of the business infrastructure in poverty-stricken areas and, in some cases, the tax burden.

In addressing these constraints, the government created an enabling environment by putting the right policies in place whereby small businesses could thrive. The SMME support structures that started after 1994 were mainly by provincial SMMEs desks, the Ntsika Promotion Agency, and Khula Enterprise Finance Limited.

2.13 Conclusion

The lack of sufficient financing is a serious constraint during the formation of new ventures as well as at the later stages, as business requires additional inflows of capital to support expansion and growth (Nieuwenhuizen and Groenewald, 2004:9). Inadequate bookkeeping is also responsible for deficiencies in several other areas of financial management.

Although support providers are in place, certain businesses and prospective entrepreneurs, through either ignorance or lack of information still remain unknowledgeable about the availability of these support systems. In an investigation into the programmes being used in South Africa to develop SMME sector, Pretorius and Van Vuuren (2003:519) found that the core focus of programs from Khula, IDC and SEDA include finance, growth, expansion and competitiveness (through export) and that these skills are more relevant for existing business than for start-ups. There is a general tendency of the Khula, IDC and DTI programmes to focus on the larger and existing ventures as their target audience. Very few programmes are aimed at micro and small enterprises.

It is internationally accepted that the SMME sector is an essential factor in promoting and achieving economic growth and development and the wide spread creation of wealth and employment. However in South Africa, entrepreneurial activity is hampered by the lack of access to finance and lack of support programmes as supported by evidence conveyed in this chapter.

CHAPTER 3

RESEARCH METHODOLOGY

3.1 Introduction

The research process involves the application of various methods and techniques in order to create scientifically obtained knowledge (Welman and Kruger: 2001:2). The aim of this chapter is to present the methods and techniques applied to obtain the findings presented in Chapter 4. The background and research topic were discussed in Chapters 1 and 2.

A thorough methodological foundation directs the whole research project with respect to its planning, organization, analyzing and interpretation of data thereby ensuring the validity and reliability of all recommendations and conclusions made from this research. Aspects of the research method to be covered in this chapter include the basic type of research design, a definition of the population, the measurement instrument, the data collection method used and statistical techniques applied to analyze the data.

3.2 Research design

The research design refers to the general plan and structure of investigation conceived as to obtain answers to the research questions (Kerlinger: 1986:279). The plan is the overall scheme or program of the research.

In starting to plan the research a distinction is made between two basic types of designs: experimental and non-experimental research. Experimental designs, refers to the exposures of research subjects to something to which they otherwise would not have been subjected (Wellman and Kruger: 2001:169). Kerlinger (1986:348) provides the following definition of non-experimental designs:

“Non-experimental research is systematic, empirical inquiry in which the scientist does not have direct control of the independent variable because their manifestations have already occurred or because they are inherently not manipulable”.

Within non-experimental research designs there are again various different types of research. These include descriptive research, historical and correlation designs. Salkind (2001:11) describes the purpose of descriptive research as to describe the characteristics of an existing phenomenon. Historical research relates events that have occurred in the past to current events and correlation research examines the relationship between variables.

Kerlinger (1986:359) mentions that one of the great weaknesses of the experimental design, as compared to experimental research, is that non-experimental research lacks control, that is, control over the independent and dependent variables.

Descriptive research has several distinguishing characteristics. These include the following:

- Descriptive research is nonexperimental in that it deals with the relationships between nonmanipulated variables in a natural, rather than artificial (lab) setting. Since the events or conditions of research interest have already occurred or exist the researcher merely selects the relevant variables for an analysis of their relationships. For example, in this study, perceptions were not manipulated by the researcher. Rather they are merely measured and analyzed in relation to SMMEs’ existing demographic characteristics (gender, educational background, and race);
- Descriptive research uses logical methods of inductive and deductive reasoning in order to arrive at generalizations about the population from which the sample can be drawn;
- Descriptive research involves hypothesis formulating and testing;

- All the variables and procedures used in descriptive studies are described as completely and accurately as possible so as to permit future replication and
- Descriptive research often employs methods of randomization so that error can be estimated when inferring population characteristics from observations samples Salkind (2001:12).

It is noted that the variable under study in the current research does in fact not lend itself to manipulation and the aim of the research is to describe the phenomenon: financial management skills difficulties experienced by small businesses. Therefore the current research is classified as non-experimental research, more specifically, as a descriptive research.

The reasons for choosing this approach include the following:

- Can acquire a lot of information through description;
- Useful for identifying variables & hypothetical constructs, which can be further investigated through other means (like exploratory surgery, or like the USS Enterprise on an away mission to the moon)
- Descriptions can be used as an indirect test of a theory or model or some behaviour/situations which cannot be studied in any other way.

The current study will use the qualitative approach as it will be describing the state of access to financial management services by SMMEs in Thohoyandou Business Centre.

3.3 Population

A population is a study's objects, which may be individuals, groups, organizations, human products and events, or the conditions to which they are exposed (Welman & Kruger 2001:18). Cooper & Schindler (2001:769) similarly define population as the total collection of elements about which we wish to make some inferences.

Small businesses were targeted in the current study. The populations for the current study are defined as the entrepreneurs in the Thohoyandou Business centre. Zikmund (1997:417) describes the target population as the complete group of specific population elements relevant to the research project. For the purposes of this research, the target population comprises entrepreneurs/managers from the small, medium and micro enterprises. The geographical location is Thulamela Municipality.

Due to the fact that no complete list exists of all small, medium and micro enterprises (SMMEs) in South Africa, SEDA's (Vhembe District) Database (2009) was used to draw a sample. The SEDA's Database consisted of approximately 693 SMMEs which were registered with them for purposes of services which the Municipality rendered to them. It must be acknowledged though, that SEDA's Database, as also other lists of businesses, would include more of the formalized businesses that are licensed businesses registered for tax purposes. This shortcoming was addressed by distributing questionnaires to also informal businesses which are operating in the Thohoyandou Business Area.

3.4 Sampling.

The basic idea of sampling is that by selecting some of the elements in a population, conclusions may be drawn about the whole population (Cooper & Schindler 2001:163).

3.4.1 Reasons for sampling

- Lower cost: The economic advantages of taking a sample rather than a census are massive;
- Greater accuracy of results: Cooper & Schindler (2001:163) argue that the quality of a study is often better with sampling than with census. They suggest that sampling possesses the possibility of better interviewing, more thorough investigation of missing,

wrong, or suspicious information, better supervision and better processing than is possible with complete coverage.

- Greater speed of data collection: Sampling's speed of execution reduces the time between the recognition of a need for information and the availability of that information.
- Availability of population elements: For example, when testing the breaking strength of materials, they must be destroyed; a census would mean complete destruction of materials.

Nonetheless, Cooper & Schindler (2001:165) argue that a census is feasible when the population is small and necessary when the elements are quite different from each other. When the population is small and variable, any sample drawn may not be representative of the population from which it is drawn. The resulting values calculated from the sample would therefore be incorrect as estimates of the population values.

3.4.2 Sampling Technique

Since the aim of the study is to make probability based confident estimates of certain parameters, a probability sampling technique, namely systematic sampling will be utilized.

3.4.3 Sample Size

It is possible to construct a so called sampling frame, having defined the population. A sampling frame is a listing of all elements in a population and the actual sample is then drawn from this listing. It is possible that biases could exist between the opinions of members of the sample frame and population. Therefore, the adequacy of the sampling frame is crucial in determining the quality of the sample drawn from it.

Due to the fact that no complete list exists of all small, medium and micro enterprises (SMMEs) in South Africa, SEDA's (Vhembe District) Database (2009) was used to draw a sample. A total of 150 questionnaires were distributed to SMMEs that were located in Thohoyandou Business Centre.

3.5 Research Instrument

According to Graziano & Raulin (1998:68) variables in a scientific research must be measured. The different levels of measurement include:

- Nominal scales: this is the lowest level of measurement, the scale with the least matching to the number system. Classification of variables is into unordered qualitative categories; for example, the race variable in the current study (Graziano and Raulin: 1998:71).
- Ordinal scales: Classification into ordered qualitative categories; for example, social class (I,II, III etc.), where the values have a distinct order, but their categories are qualitative, in that there is no natural (numerical) distance between their positive values. An example of ordinal scales in the current study is the education level of respondents.
- Interval scales: When the measurement conveys information about the ordering of magnitude of the measurement and about the distance between the values (Sekeran, 2003:71). The rating of financial management service in the questionnaire, while strictly speaking are ordinal in nature, are often considered as interval scales by researchers to enable the calculation of means and parametric significance testing.
- Ratio: These are measurements where there is equal distance between the numbers, as with interval scales, yet it also has an absolute zero. No ratio variables were included in the current study.

The current study made use of one instrument, designed specifically for the population targeted: the entrepreneurs. This measurement instrument took the format of a questionnaire. A questionnaire is a general term that includes all techniques of data collection in which each person is asked to respond to the same set of questions in a predetermined order. Cooper & Schindler (2001:82) identifies two types of questionnaires:

(a) Self-administered questionnaires

- On-line questionnaire
- Postal questionnaire
- Delivery and collection questionnaire

(b). Interviewer administered questionnaires

- Telephone questionnaire;
- Structured interview.

Delivery and collection questionnaires, that is, where the questionnaires are delivered by hand to each respondent and collected later, was used to collect data from entrepreneurs. This type of questionnaire was chosen over others since the sample from this population is large. It has a moderately high response rate of 30-50%. Mainly closed questions needed to be asked from this sample, which is suitable for the purposes of this research study. The delivery and collection of questionnaires enhances respondent participation, and although the confidence that the right person had responded is low, it can be checked at collection (Cooper & Schindler (2001:84). Moreover, this type of questionnaire allows minimal staff involvement it allows respondents time to think about questions. The major drawback that was experienced by the researcher with this type of questionnaire is that there was no intervention available for probing or explanation.

The following advantages to using questionnaires are also provided:

- It is possible to survey a broader population as surveys can be mailed;
- They are cheaper than one-on-one interviews;

- People may be more willing to be truthful because their anonymity is all but guaranteed.

3.6 Data collection

Data, according to Cooper & Schindler (2001:82), are the facts presented to the researcher from the study's environment. There is no simple answer as to which of the available methods of data collection the researcher should use when collecting data. There are however, three major criteria for evaluating a measurement tool (Cooper & Schindler 2003:231):

- Validity refers to the extent to which the test measures what we actually wish to measure. It looks to the end results of the measurement. The principal question that validity asks is: Are we really measuring what we think we are measuring?
- Reliability has to do with the accuracy and precision of a measurement procedure. It asks such questions as: How accurate is the instrument that is used in making the measurement?
- Practicality is concerned with a wide range of factors of economy, convenience and interpretability.

The questionnaires were distributed to SMMEs in Thohoyandou Business Area in Thulamela Municipality in the Limpopo Province.

Format of the questionnaire

A questionnaire was sent out, focusing on the entrepreneurs in Thohoyandou Business Centre as unit of analysis. The structure of the questionnaire was as follows:

Section A: Demographic Information

This section used closed questions to gather such information as gender, age, home language and education. Participants were simply expected to tick the space containing the applicable response. The questions in this section were in a multiple choice format which allowed participants to choose one or more alternatives in some instances. The rationale behind these demographic questions is that it places the results in a frame of reference and might provide

insights into differences between demographic groups or correlation with regards to entrepreneurial behaviour.

Section B: Profile of Business Activities

Closed and open ended questions were used to gather such information as the number of years of experience as an entrepreneur; their position or role in the business and whether the business is micro, small or medium sized. Entrepreneurs were also asked how they raised start-up capital; what were the problems encountered when raising the necessary capital; does there appear to be a need for further or better support in the area of financial management amongst SMMEs.

The questionnaire was distributed with a covering letter (see addendum). The covering letter included the following:

- An explanation of the relevance of the study
- A brief description of the objectives of the study
- Instruction on how to administer the questionnaire
- Assurance of confidentiality
- Contact details if any difficulties were encountered

Registered Business Management students from the University of Venda were approached to carry out the task of distributing the questionnaires. Of the total of 150 questionnaires which were distributed to SMMEs in Thohoyandou Business Area, a total of 75 were returned. This means a response of 50%. Of the 75 questionnaires returned only 72 were used; the other three were returned not completed.

3.7 Data Analysis and Statistical techniques

There are two major components of the discipline of statistics: descriptive and inferential statistics.

Rosnow and Rosenthal (1999:10) define descriptive statistics as condensing large volumes of data into a few summary measures. Descriptive statistics in research helps by describing the

contour of data and in case of two or more groups of data, their proximity or remoteness of relationship. They also define inferential statistics as the area of statistics which extends the information extracted from the sample to the actual environment in which the problem arises. In research inferential statistics help by suggesting certain inferences as to the nature of the data.

3.7.1 Descriptive statistics

For the purposes of this research descriptive statistics was used to analyze the data which had been collected by means of the questionnaire. Descriptive statistics used in the present study included frequency counts, mean scores, standard deviations and cross tabulations. In other words, the numerical data collected were mathematically manipulated and statistically analyzed as opposed to the inductive reasoning approach which was used to analyze the data collected through the field observations.

Frequencies are defined by Kerlinger (1986:127) as the number of objects in sets or subsets. More simply, the number of times a certain answer appears in the data shows the number's frequency. The mean calculates an average across a number of observations and the standard deviation is the square root of the variance around the mean, in other words, how well the mean represents the data (Field 2005:6).

A cross tabulation is just a more advanced method of presenting frequency data. It presents the frequencies in a matrix. For instance: Number of entrepreneurs in each race group within each gender.

3.7.2 Inferential Statistics

The following inferential techniques were used:

- **Chi-Square Test**

The Chi-Square Test procedure tabulates a variable into categories and computes a chi-square statistic. This goodness-of-fit tests the expected frequencies in each category to

test that all categories contain the same proportion of values or that each category contains a user-specified proportion of values (SPSS 11.5:2004). This is the significance test when making use of the cross-tabulation technique.

- **The t-test for independent measures**

The t-test assesses whether the means of two groups are statistically different from each other. The t-test is defined as the difference between the two samples' means divided by the standard error of the difference (<http://research.med.umkc.edu/tlwboistats.html>).

3.8 Statistical Analysis Software

All statistical analyses in the present study were computed using the Statistical Package for the Social Sciences (SPSS) statistical package for Windows version 11.1 (SPSS, 2001).

3.9. Conclusion

This chapter has dealt with the research methodology of the project. The research strategy and design have been discussed at length before selecting the appropriate one for tackling the research problem at hand.

The population from which to gather data was identified, including the sampling methods to be used for the population which had been chosen and a qualitative data collection technique was used. The researcher spent four weeks delivering and collecting the questionnaires from Thohoyandou Business Centre in Thulamela Municipality in the Limpopo Province.

CHAPTER 4

DATA PRESENTATION, INTERPRETATION AND ANALYSIS

4.1 Introduction

The current chapter presents the empirical findings of the study which focused on assessing access to financial management services by SMMEs in Thohoyandou Business Centre. The analysis is based on 72 responses out of the 150 questionnaires that were sent out to small businesses.

A summary of the data collected is presented during the analysis and interpretation. Often the researcher offers his own opinion in explaining the outcomes, except where explanations were offered by the respondents in the “comment” section of the questionnaire. The use of histograms is usually made for ease of displaying a vast array of data in a brief and clear format

4.2 Business operations per economic sector

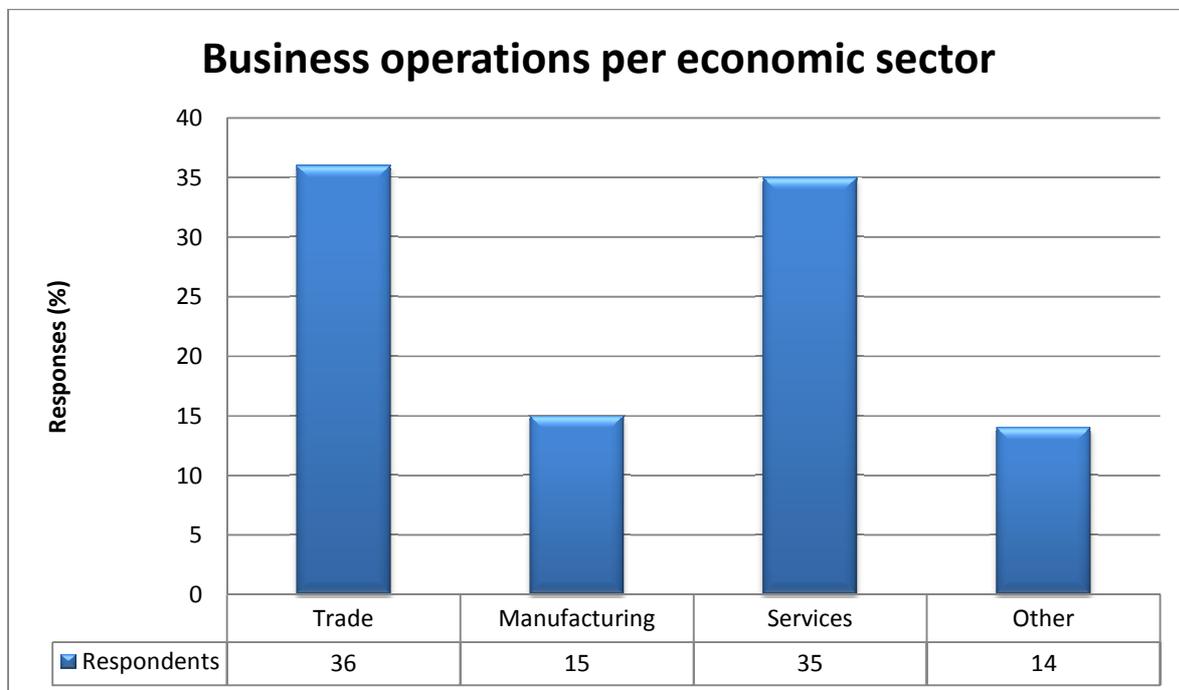


Figure 2.1: The different business operations divided according to economic sectors

The highest number (36%) of SMMEs is in trade, followed by services at 35%. Only 15% of the sample is in manufacturing and the other 14% are in an un-identified small business. The implication is that most of the SMMEs trade in finished goods. The question is who stands to benefit from this type of business operations; is it the SMMEs themselves or bid business? In other words if government was to give support to the SMMEs, given the situation, who would be the direct beneficiary. This also brings into the picture the question of sustainability of the businesses operations of the SMMEs. The sustainability of their businesses is dependent on the existence of the primary supplies. The SMMEs are evidently operating in the tertiary level of the economy, since only 15% are in manufacturing.

4.3 Legal Status of the Businesses



Figure 4.2: The legal status of the Businesses

The investigation probed into the legal status of the small businesses in the study area. It became evident that most (47%) of the businesses are registered as sole traders, with 19% registered as partnerships, 29% as close corporations and the remaining 4% as companies. The interpretation is that the majority of the SMMEs in the Thohoyandou Business Centre are focused on the welfares of either families or individuals. It implies that most of the businesses may not have easy access to financial assistance given their legal status and subsequent degree of liability. The registration of business as close corporations is gradually becoming fashionable. It however remains to be seen whether or not these close corporations are not owned by individuals. It is therefore important to determine the role played by individuals and groups in the management structures of the businesses.

4.4 The Different Roles of Individuals in the Businesses

The graph below depicts the roles or positions of individuals in the businesses. The roles are divided into owner, manager or both. Respondents were also given an opportunity to specify their roles in case they played any other role different from those given.

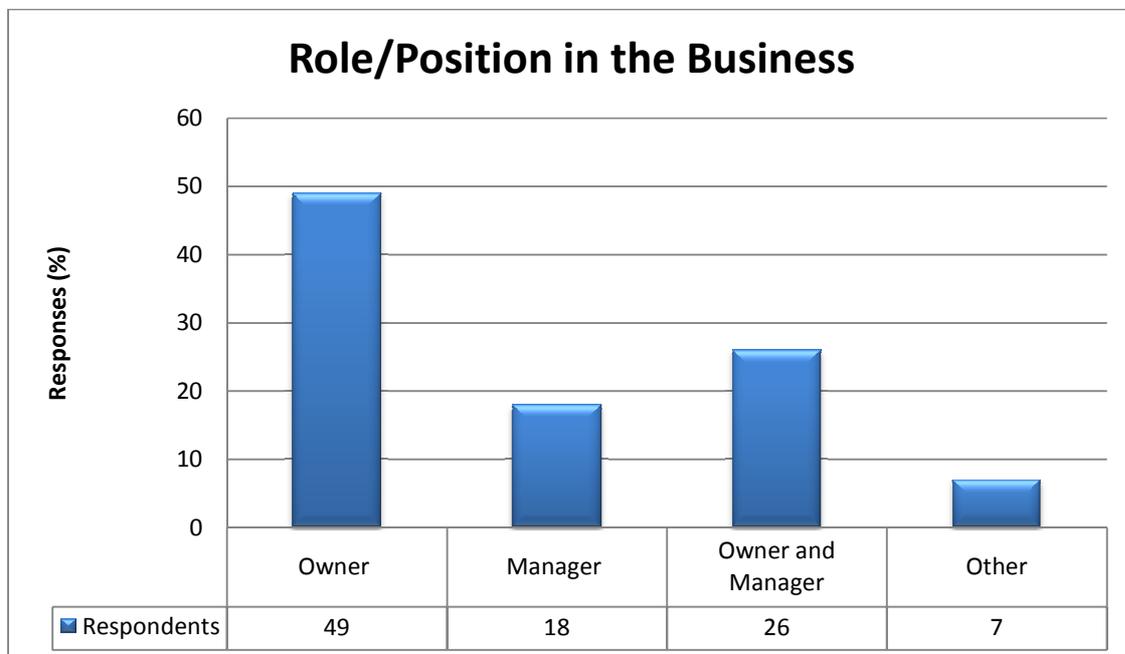


Figure 4.3: The role/position in the business

Most of the respondents in the sample are the owners of their businesses 49%; 18 % are managers and 26 % are owner and manager respectively, while the other 7% are in unidentified business role. The interpretation is that the majority of small businesses in Thohoyandou Business centre are run by their owners who also act as managers of their own businesses. This was also depicted by the type of business ownership in which sole traders were 47%. This raises the need for the owners to have the necessary skills for the proper running of their businesses, that is, financial management skills.

4.5 Number of Employees

The graph below shows the number of people employed by small businesses. The numbers are categorized by less than 5, between 6 – 50 and more than 51.

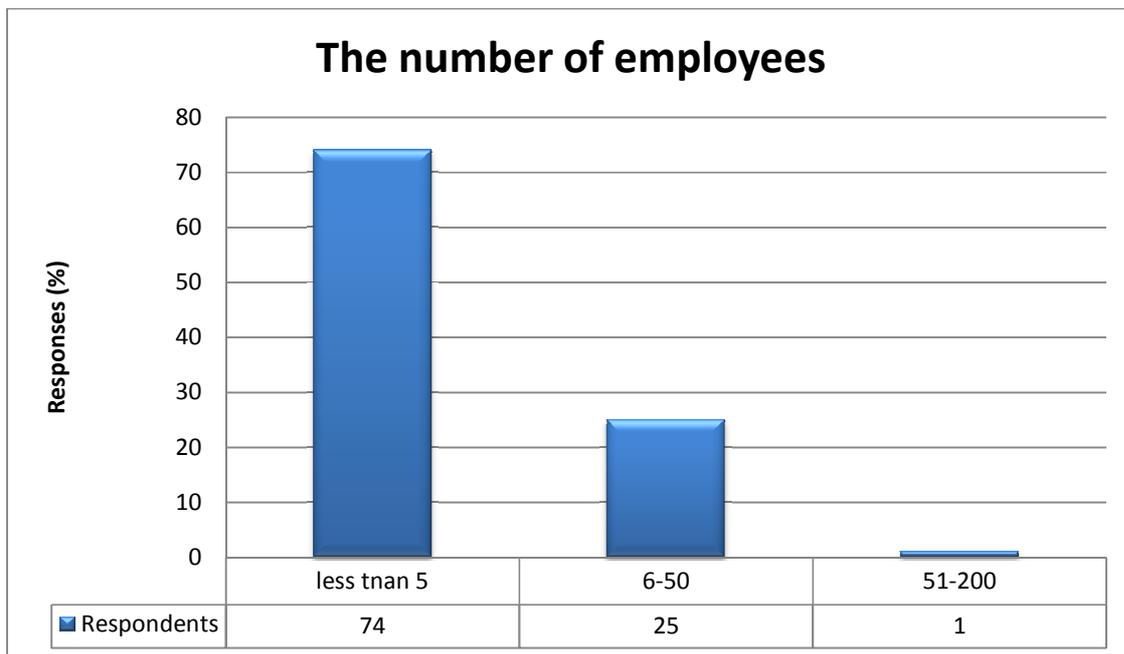


Figure 4. 4: The number of employees

Most of the respondents have employed less than five employees 74%; 25% of small businesses have employed between 6 and 50 employees, while only 1% has between 51

and 200 employees. This is the case because many small businesses are operating as small shops which are just trading (buying and selling goods) for their survival and personal gains.

4.6 The methods of fund raising

The graph below depicts the methods used by small businesses to raise the needed capital for the formation of their businesses. Various methods were indicated in order for small businesses to indicate the one they used to start their businesses.

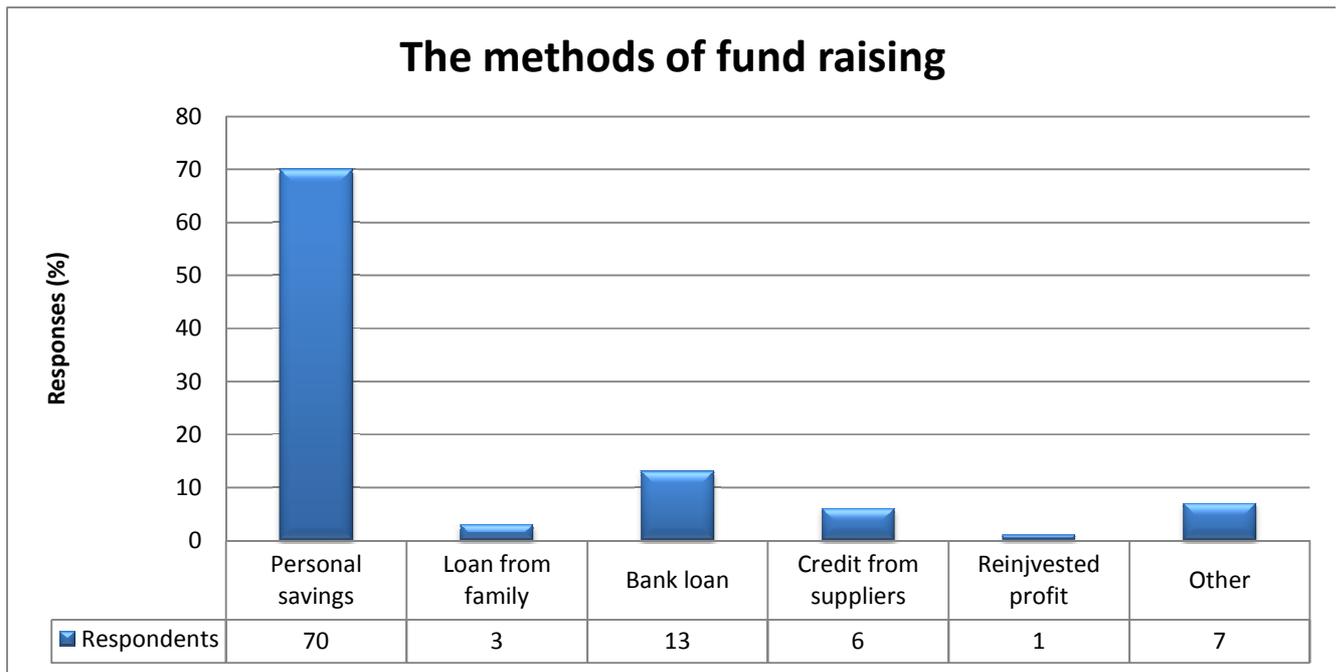


Figure 4.5: The methods of fund raising

70% made use of their own personal savings, 13% obtained the loan from Banks, 3% received loans from family members, 6% received credit from suppliers in order to start their businesses, and 1% reinvested their profits. Only 7% received their start-up capital

from un-identified sources. The 1% that reinvested their profit may be an indication that the trading undertakings may not be very profitable because of high competition in their trading undertakings. The interpretation might also be that owners had to use their own capital to get the business viable and then thereafter the bank would be willing to assist them with a loan.

4.7 Bookkeeping

The graph below depicts that most of the respondents in the sample are doing bookkeeping themselves 67%. Only 33% use external people to do bookkeeping. The interpretation may be that it is not easy to use external people for bookkeeping for small businesses as this may be expensive for them, as most are trading as sole traders.

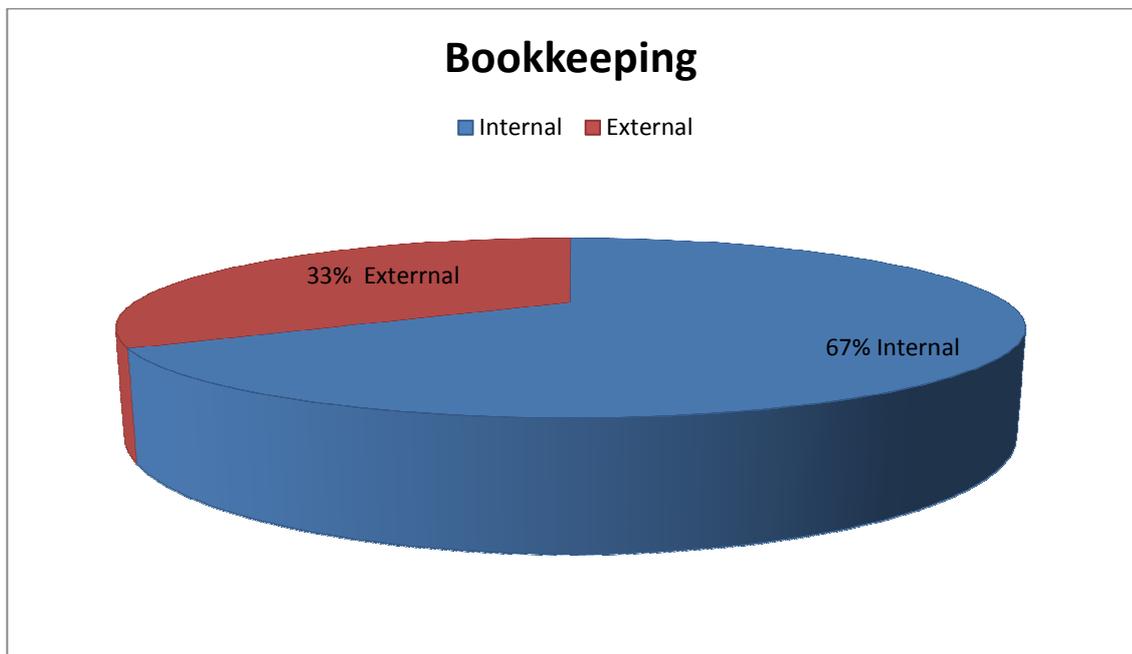


Figure 4.6: Bookkeeping

4.8 Need for support in the area of financial management

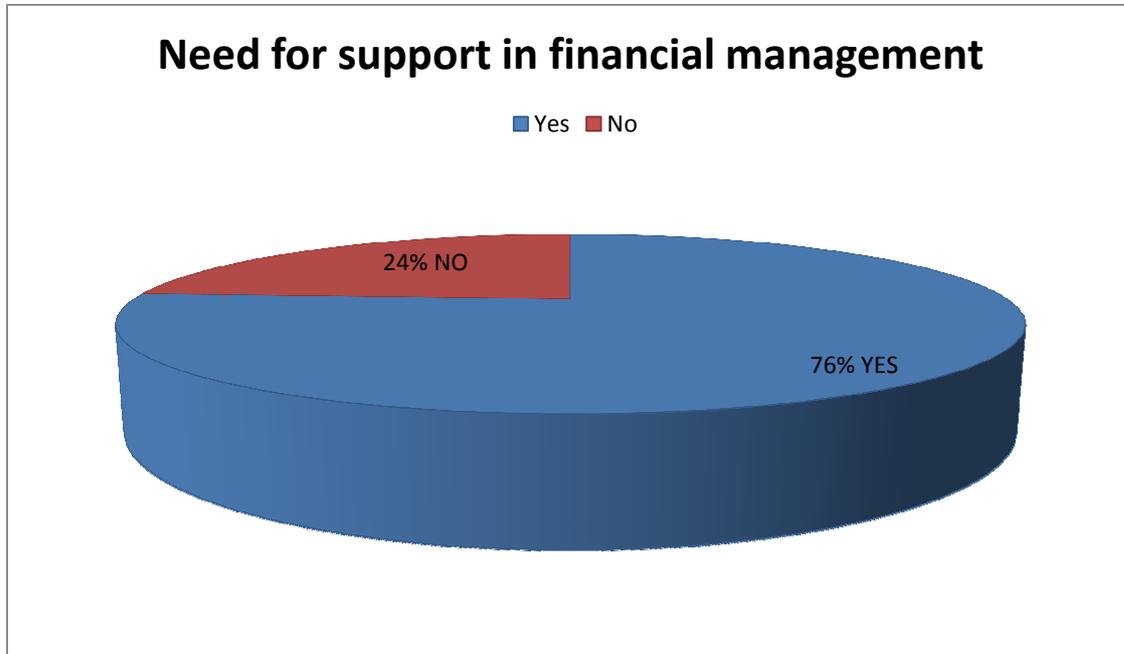


Figure 4.7: Need for support in the financial management

Most of the respondents think that there is a need for support in the area of financial management skills 76%. Only 24% think that there no need for support in financial management services. The interpretation is that many small businesses have failed due to lack of financial management services. Financial management is vital when it comes to securing loans from financial institutions.

4.9 Assistance from Government and Financial institutions

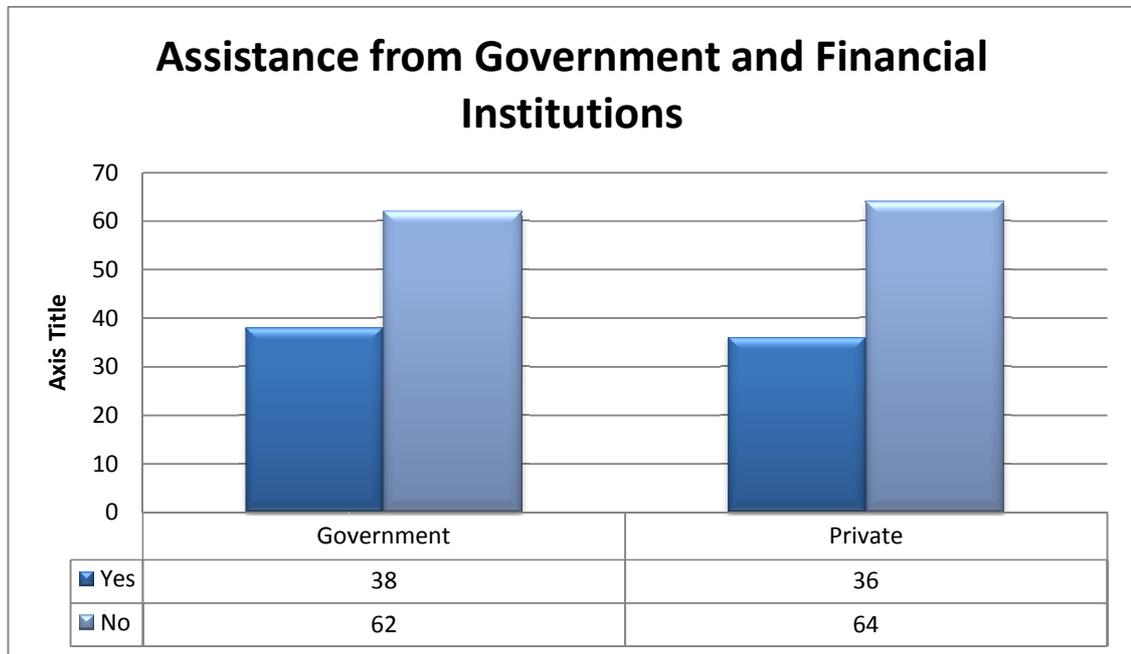


Figure 4.8: Assistance from government and financial institutions

Most of the respondents in the sample showed that they do not receive the needed assistance from both government and financial institutions with a response of 62% and 64%, respectively. Only 38% and 36% of respondents think that government and financial institutions are doing enough to assist small businesses for their growth and development. The interpretation may be that even though, services are made available by government and financial institutions, small businesses may not be in a position to access them due to a number of reasons evidenced in the literature.

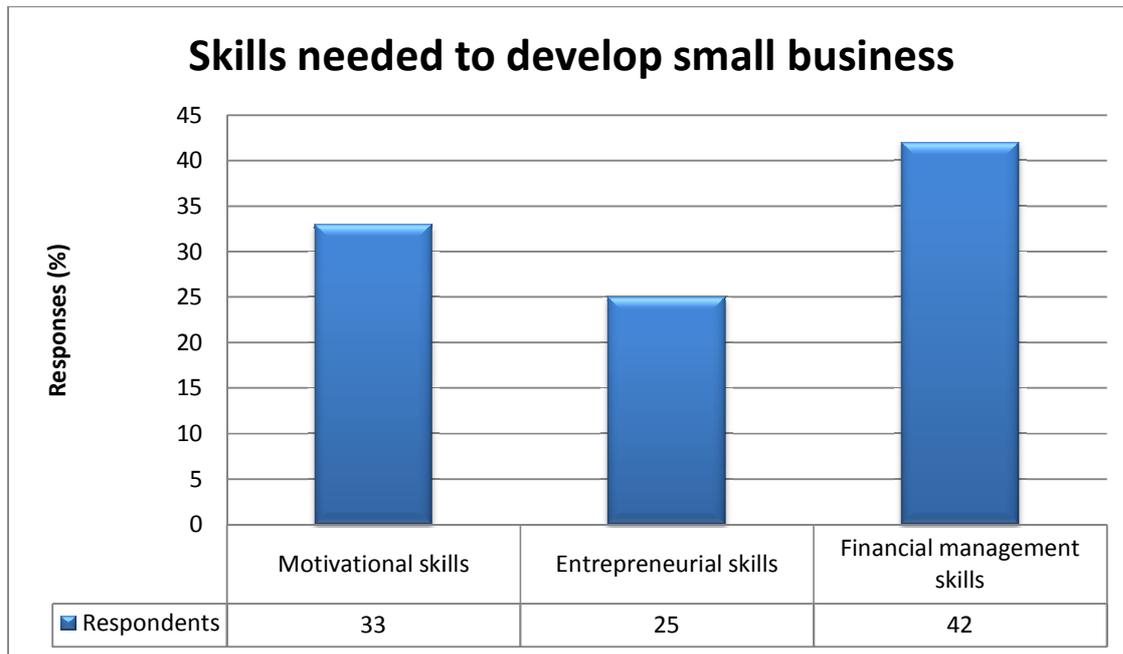


Figure 4.9: Skills needed to develop small business

Most entrepreneurs in the sample indicated that financial management skills are needed in order for small businesses to develop (42%). 33% and 25% of the entrepreneurs think that motivational skills and entrepreneurial skills are needed for the development of small businesses, respectively. What remains to be clarified is whether the small businesses are ready to receive this type of services. As many of them are owners and managers of their businesses, the question on their readiness to access financial management services is still questionable.

4.10 Conclusion

This chapter has presented the findings of the research project. The results were analyzed using the SPSS statistical package for windows version 11.1 which presented the statistical results in terms of frequencies and arithmetic means. The study revealed that there is a need for support in the area of financial management skills as this can improve the financial health of businesses.

CHAPTER 5

SUMMARY, CONCLUSIONS, AND RECOMMENDATIONS

5.1 Introduction

The White Paper for Small Business development and the National Small Business Development (Act 102 of 1996) identified access to finance, capacity building and the regulatory framework as key variables to be addressed in order to achieve faster growth in the SMME sector (Ntsika, 2000:9). While many of the constraints inhibiting SMME growth and development have somewhat relaxed, much work still remains to be done. Lack of financial managerial skills in particular, remains a high priority aspect that needs to be addressed (Ntsika, 2000:9).

The importance of SMMEs to the economy expresses itself in their contribution to the GDP and employment which is likely to be as high as the large enterprises' contribution. With the current context of negative growth in employment creation by both large and the government sectors, SMMEs have a major socio-economic role to play as already shown in the study. However, this objective fails to materialise due to the high failure rate of small pertains due to the lack of financial management skills and lack of access to finance.

This chapter highlights the key findings in an attempt to answer the aims and objectives delineated in chapter one. The chapter will combine the presentation and analysis of results gathered with the guidelines of the research methodology in chapter three and four with the review of literature in chapter two.

Chapter five concludes with a general discussion of the results obtained compared to those in the literature. It is apparent from the overall findings in this research that SMMEs face challenges in accessing finance due to financial management support services as evidenced in the current study. However, in spite of that, many do consider their business to be successful. Recommendations are also provided based on the findings from the study.

5.2 Realization of the Objectives of the Study

The growth of SMMEs in South Africa is still in process as the country rebuilds its economy. The SMME sector is making important contributions to the South African economy. Financial institutions and other institutions that provide support to the SMMEs are starting to consider all types of SMMEs and they are also realizing the importance of training entrepreneurs on how to manage their finance.

The government is also aware that indeed SMMEs are the backbone of the country's economy. This encourages them to start funding institutions to train the emerging entrepreneurs in financial management skills in anticipation that this will ease the burdens faced by SMMEs and hence their growth.

Despite the initiatives made by the government, the current study shows that lack of financial management skills and access to finance are among the most challenging factors that affect SMMEs' growth and development in South Africa.

Furthermore, the study also noted that mere mismanagement and lack of marketing skills among owners-managers cannot be underestimated as noted in the study. Other non-financial impediments identified include:

- Unfavourable legal environment;
- Lack of adequate infrastructure;
- Lack of proper operating premises;
- Lack of proper education among owner-managers and
- Lack of adequate business information and support necessary for informed business decisions or counselling services.

For the purposes of this study, the findings confirmed the general perception that many owners of SMMEs in South Africa have, among others, lack of management skills and access to finance as the main factors that impact negatively on the growth and development of

SMMEs in South Africa. Consequently, entrepreneurs find it difficult to manage their SMMEs to grow and they eventually end up failing.

5.3 Recommendations

Risk capital investment is urgently needed to enhance the rapid development of SMMEs. For financial institutions to develop appetite for and to better manage SMME risk, the sector should address the following credit analysis issues:

- Viable business model in a profitable and growing industry;
- Sound and focused management;
- Clear succession plan;
- Demonstrable financial management capabilities and
- Focused cost structure and financial planning

For SMMEs to move up the value chain in order to remain competitive, government should take a more comprehensive approach towards SMME development to improve their operations and productive capabilities through:

- Increasing their access to finance through loan guarantee schemes;
- Create an enabling business infrastructure;
- Enhance human capital development;
- SMMEs' financing through grants, which are not repayable must be reviewed because it underestimates their ability to achieve self sufficiency;
- Supportive legislation through the actual financing at subsidized rates;
- Measures should be taken to support and counsel prospective entrepreneurs when they decide to start a business. These measures should include increasing information available to people thinking of starting a business to ensure that they are well informed to make rational decisions;

- There is a need for greater government/private sector partnership to find more innovative strategies for SMMEs greater access to finance, training in financial management and marketing skills and
- Owner/manager of SMMEs must be encouraged to participate in policy-making decisions on the development of SMMEs, to ensure that all policies developed for the support of SMMEs favour all types of small businesses.

Management capability strengthens the financial capacity of SMMEs. Financial institutions are prone to be favourably biased towards SMMEs who can demonstrate eloquence in areas such as financial management (including basic bookkeeping), marketing and technology upgrading. It is recommended that government and other service providers incorporate additional simplified components of their training packages to cover such areas as bookkeeping and compilation of business plans.

Educational background of entrepreneurs also has a direct influence on how they respond to training. From the results of the study, it was noted that most of the entrepreneurs (42%) viewed financial management skills as vital for the development of their businesses. Financial institutions should make financial contributions to non-financial support services such as provision of financial management skills and mentoring.

Access to information about SMMEs should be increased to ensure that all providers and potential providers of finance have sufficient knowledge to assess the risk of SMME applications for finance. Any intervention that improves the ability of financial providers to accurately assess risk would increase their willingness to extend credit and other services to SMMEs.

Funding institutions should advertise their services so that the entrepreneurs are aware of where to go when they need capital to start-up or grow their businesses. From the result of the study, it was noted that most of the entrepreneurs (70%) used their personal savings to start their businesses. Therefore, it is recommended that there should be an improved

regulation of credit bureau in order to enhance their credibility and the integrity of the information being distributed by the bureau.

5.4 Shortcomings of the Study

- The sample was relatively small, due to the difficulty experienced in getting the entrepreneurs to co-operate.
- From the 150 questionnaires that were distributed only 75 were returned. Out of the 75 returned three were not completed, which made a sample of 72 participants.
- There has not been much documented research on the problems of accessing financial management services by SMMEs in South Africa, within an entrepreneurship research context therefore making the theoretical base for the discussions narrow.

5.5 Further Research

Further research that could be conducted includes the following:

- Certain skills are a pre-requisite for a successful application for finance such as bookkeeping, cash flow management and drafting of comprehensive business plan. Further research could be conducted into how financial institutions and government could impart financial management skills to the existing and potential entrepreneurs.
- Further research can also be conducted on obstacles to accessing financial management services by SMMEs.
- Furthermore, a research can also be conducted on the provision of Financial Management services to SMMEs by Financial Institutions.
- An exploration into financial institutions and their policy towards assisting SMMEs in accessing finance.

5.6 Conclusion

SMMEs, as engine of growth and the primary catalyst of innovation and social transformation, are important assets which must be nurtured and harnessed by the South African economy to enable it to quickly and effectively adapt to the challenges of globalization and to reap its benefits. However, government's efforts to support the SMMEs sector have so far been dismal.

The importance of SMMEs to the South African economy has already been acknowledged by government. Government, however, cannot, by itself make firms grow and employ staff, but can work towards making the environment more conducive for entrepreneurship by implementing a favourable institutional and regulatory environment. What is needed is a new approach.

Although government has tried to put in place policies and institutions with the aim of improving the accessing of finance by small business owners, their success has been minimal. It is there imperative that management capability and financial management acumen be regarded as key to easy access for funding by the entrepreneurs themselves, and the parties involved in supporting and promoting them.

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Annexure 1

Covering Letter

Dear Respondent,

RESEARCH ON ASSESSMENT OF ACCESS TO FINANCIAL MANAGEMENT SERVICES BY SMMEs IN THOHOYANDOU BUSINESS CENTRE (THULAMELA MUNICIPALITY).

The purpose of this questionnaire is to assess the provision of financial management services to SMMEs and to determine possible constraints in obtaining financial assistance from financial institutions.

This research project will assist in trying to gain a better understanding of the challenges that South African Small businesses face in an effort to access financial management services.

No identification is required to complete this questionnaire and information collected through the questionnaire will be treated as strictly confidential.

Instruction: Answer each question by ticking in the suitable box provided or write your answer in the space provided.

If you face any difficulties with the questionnaire, please phone

Mr. Ndou Muhali at 082 793 6265

Yours sincerely

Ndou Muhali

Annexure 2

QUESTIONNAIRE

Section A: Demographic Information

1. What is your gender?

| | |
|--------|--|
| Male | |
| Female | |

2. What is your race?

| | |
|----------|--|
| Black | |
| White | |
| Coloured | |
| Asian | |

3. What is your highest formal educational qualification?

| | |
|-------------------------|--|
| Matric/Grade 12 or less | |
| Certificate/Diploma | |
| Bachelor's degree | |
| Honours degree | |
| Master's degree | |
| Doctorate | |

Section B: Profile of Business Activities

1. Nature of the business: In which sector of the economy are your main operations?

| | |
|--------------------------|--|
| Trade (Retail/Wholesale) | |
| Manufacturing | |
| Services | |
| Other (Specify) | |

2. What is the legal status of your business?

| | |
|---------------------------|--|
| Sole proprietor | |
| Partnership | |
| Close corporation | |
| Limited liability company | |

3. What is your position/role in the business?

| | |
|---------|--|
| Owner | |
| Manager | |

| | |
|-----------------|--|
| Both | |
| Other (specify) | |

4. How many employees do you have?

| | |
|--------------|--|
| Less than 5 | |
| 6-50 | |
| More than 51 | |

5. Which methods of funding, in order of importance, have been employed by your business? Rank the methods from 1=most important to 7=least important.

| | |
|--------------------------|--|
| Personal savings | |
| Loan from family/friends | |
| Bank loan | |
| Credit from suppliers | |
| Reinvested profits | |
| Leasing or hire purchase | |
| Other (Specify) | |

6. What are the main problems encountered, when raising the necessary capital to start your business?

.....

7. Which of the following best describes the accounting activities of your business?(tick the most appropriate response)

| | |
|--|--|
| We do our accounts ourselves | |
| We prepare the accounts with the help of an internal professionally qualified accountant | |
| Our accounts are prepared by an external professionally qualified accountant | |
| Other (specify) | |

8. If you use an external professionally qualified accountant is he/her local (from within the Thohoyandou area)?

| | |
|-----|--|
| Yes | |
|-----|--|

| | |
|----|--|
| No | |
|----|--|

9. Does there appear to be a need for further or better support in the area of financial management amongst SMMEs?

| | |
|-----|--|
| Yes | |
| No | |

10. Does the provision of such support services lead, in turn, to a greater probability of qualifying for loan finance from the financial sector?

| | |
|-----|--|
| Yes | |
| No | |

11. Do you think there are other constraints which affect the growth of SMMEs in South Africa?

| | |
|-----|--|
| Yes | |
| No | |

If yes (specify)

.....

.....

12. What are the skills you think you need to survive as a small business?

.....

.....

13. Do you think lack of financial management skills and lack of financial access are the major constraints of SMMEs growth?

| | |
|-----|--|
| Yes | |
| No | |

14. Do you think you are getting the right assistance from government for the development of small businesses?

| | |
|-----|--|
| Yes | |
| No | |

15. Do you think you are getting the right assistance from financial institutions for the development of small businesses?

| | |
|-----|--|
| Yes | |
| No | |

16. As small businesses what help do you think you need in order to develop?

.....

.....

17. What skills do you think you need in order to develop as a small business?(tick the most appropriate answer)

| | |
|-----------------------------|--|
| Motivation skills | |
| Entrepreneurial skills | |
| Financial management skills | |
| Other (specify) | |

Thank you for dedicating your time completing the questionnaire.