

**UNIVERSITY OF KWAZULU-NATAL**

**SMME ACCESS TO FUNDING-CHALLENGES  
EXPERIENCED BY SMMEs IN UMZIMKHULU  
MUNICIPALITY**

**By**

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## **DECLARATION**

I, Christopher Robert Thulani Cele, declare that:

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## **ABSTRACT**

The purpose of this study was to investigate whether or not the SMMEs in the area of rural UMzimkhulu Municipality do access funding from the banking institutions as well as other funding organisations, government and agencies. This research looked at the challenges they have in accessing the funding for both start-ups and business development.

The research method used was qualitative and interviews conducted from a sample of SMMEs in UMzimkhulu. These challenges are viewed as possible reasons why most SMMEs are failing as a result of financial difficulties and therefore should be investigated. This kind of situation persists despite the available support by government who developed policies and strategies for support. As a result of these policies, development bodies such as DTI, SEDA and Khula enterprises and other government departments (Economic Development) in the provinces and locally (LED) to assist and give support to SMMEs. It is intended that the study of SMME challenges in relation to finance access will provide recommendations to improve their livelihood and life cycle of these businesses.

The research findings highlight some of the challenges for SMMEs such as those of being unable to provide some of the requirements of funding bodies. Furthermore, the funding bodies were found to favour those businesses that were already doing well over smaller, fledgling or struggling businesses which required funding to continue their operations. The research also found that most SMMEs do not access funding that is available because they do not know of the funding available from government agencies and also because the offices for these institutions are based in big cities far away from them. The findings from this research can be used to assist in policy development and turn-around strategies in the funding of the SMME sector. It will also potentially contribute towards addressing the challenges faced by SMMEs in other rural areas as it will reflect challenges not only in UMzimkhulu but also similar rural areas. The research also highlights the recommendations and scope for further research.

## LIST OF ACRONYMS

|        |   |
|--------|---|
| BBBEE  | Broad Based Black Economic Empowerment                |
| BSC    | Business Support Centre                               |
| CBOs   | Community Based Organisations                         |
| CEED   | Centre for Entrepreneurial and Enterprise Development |
| CHAMSA | Chamber of Commerce and Industry South Africa         |
| CLO    | Collateralised Loan Obligation fund                   |
| DAEA   | Department of Agriculture and Environmental Affairs   |
| DBSA   | Development Bank of South Africa                      |
| DEAT   | Department of Economic Development and Tourism        |
| DED    | Department of Economic Development                    |
| DM     | District Municipality                                 |
| DTI    | Department of Trade and Industry                      |
| ESS    | Entrepreneurial Support Services                      |
| EU     | European Union  |
| FABCOS | Foundation of African Business and Consumer Services  |
| GDP    | Gross Domestic Product                                |
| GEAR   | Growth Empowerment and Redistribution                 |
| HDI    | Historically Disadvantaged Individuals                |
| IDP    | Integrated Development Plan                           |
| IDC    | Industrial Development Corporation                    |
| KZN    | KwaZulu-Natal   |
| LED    | Local Economic Development                            |
| LM     | Local Municipality                                    |
| NEF    | National Empowerment Fund                             |

|       |  |
|-------|--|
| NFBI  | Non-Banking financial institution          |
| NGOs  | Non-Governmental Organisations             |
| NSBC  | National Small Business Council            |
| PGDS  | Provincial Growth and Development Strategy |
| SACOB | South African Chamber of Business          |
| SEDA  | Small Enterprise Development Agency        |
| SMMEs | Small Micro Medium Enterprises             |
| TIKZN | Trade and Investment KwaZulu-Natal         |
| UYF   | Umsobomvu Youth Fund                       |

# **TABLE OF CONTENTS**

| <b>Description</b>  | <b>Page</b> |
|---|-------------|
| Title Page  | I           |
| Declaration   | I           |
| Acknowledgements  | II          |
| Abstract  | III         |
| List of Acronyms  | IV          |
| Table of Contents   | VI          |
| <br>  |             |
| CHAPTER ONE   |             |
| 1.1 Introduction .....  | 1           |
| 1.2 Background and Context of the Study.....                                | 2           |
| 1.3 Definitions .....   | 3           |
| 1.4 Research Purpose.....   | 4           |
| 1.5 Rationale.....  | 5           |
| 1.6 Design and Methodology .....  | 7           |
| 1.7 Significance of this research.....                                      | 8           |
| 1.8 Limitations of the study.....   | 8           |
| 1.9 Synopsis of Chapters .....  | 9           |
| 1.10 Summary of Chapter One .....   | 10          |
| CHAPTER TWO.....  | 12          |
| 2.1 Introduction .....  | 12          |
| 2.2 The Economic Standing of SMMEs.....                                     | 12          |
| 2.3 Changing view and policy background on SMMEs.....                       | 14          |
| 2.4 South African policy on SMME support programmes .....                   | 18          |
| 2.5 Government funding and support to SMMEs and their challenges .....      | 21          |
| 2.6 Challenges in accessing available government funding and services ..... | 24          |
| 2.7 Private sector funding and support to SMMEs and their challenges.....   | 26          |
| 2.7.1 Credit unions and stokvels.....                                       | 26          |
| 2.8 NGOs and Private sector role .....                                      | 27          |
| 2.9 Microfinance.....   | 28          |
| 2.10 South African banking sector and SMMEs .....                           | 28          |
| 2.11 Challenges in accessing available private sector funding. ....         | 29          |

|                     |   |    |
|---------------------|---|----|
| 2.12                | GAP funding source for SMMEs .....                              | 31 |
| 2.13                | Equity and debt financing.....                                  | 32 |
| 2.14                | Summary of Chapter Two .....                                    | 32 |
| CHAPTER THREE ..... |   | 34 |
| 3.1                 | Introduction .....  | 34 |
| 3.2                 | Study Design .....  | 34 |
| 3.3                 | Qualitative research .....                                      | 34 |
| 3.3.1.              | Why qualitative research was used in this study .....           | 35 |
| 3.4                 | Data Collection .....   | 35 |
| 3.4.1               | Ethical Issues .....  | 36 |
| 3.4.2               | Data Collection Process.....                                    | 36 |
| 3.4.2.1             | Primary data collection.....                                    | 36 |
| 3.4.2.2             | Secondary data collection.....                                  | 37 |
| 3.4.3               | Interviews .....  | 37 |
| 3.5                 | Sampling method.....  | 39 |
| 3.6                 | Data Analysis.....  | 41 |
| 3.7                 | Validity and Reliability .....                                  | 42 |
| 3.8                 | Limitation to methodology .....                                 | 42 |
| 3.9.                | Summary of Chapter Three .....                                  | 42 |
| CHAPTER FOUR .....  |   | 44 |
| 4.1.                | Introduction .....  | 44 |
| 4.3                 | Requirements criteria from funders.....                         | 45 |
| 4.3.1               | Viable proposals or business plans.....                         | 46 |
| 4.4                 | SMME's as posing high risk .....                                | 49 |
| 4.5                 | Business regulations and legislation.....                       | 50 |
| 4.6                 | Lack of information and technology .....                        | 52 |
| 4.7                 | Access to information and advice.....                           | 53 |
| 4.8                 | Lack of training in entrepreneurship and management skills..... | 54 |
| 4.9                 | Required collateral security .....                              | 57 |
| 4.10.               | Summary o Chapter Four. ....                                    | 59 |
| CHAPTER FIVE .....  |   | 61 |
| 5.1                 | Introduction .....  | 61 |
| 5.2                 | Short term recommendations.....                                 | 62 |
| 5.2.1               | Challenges with the banking sector .....                        | 62 |



|       |   |    |
|-------|---|----|
| 5.2.2 | Resolution on managerial skills and strategic planning .....  | 63 |
| 5.2.3 | Resolution on access to finance.....                          | 63 |
| 5.2.4 | Resolution on Lack of Knowledge about funding available ..... | 64 |
| 5.2.5 | Access to banking services .....                              | 65 |
| 5.3   | Medium and long-term recommendations.....                     | 66 |
| 5.3.1 | Medium term recommendations.....                              | 66 |
| 5.3.2 | Long-term recommendations.....                                | 67 |
| 5.4   | Conclusion.....   | 68 |
|       | REFERENCES .....  | 70 |
|       | APPENDIX A: INFORMED CONSENT LETTER .....                     | 76 |
|       | APPENDIX B: INTERVIEW QUESTIONS .....                         | 78 |
|       | APPENDIX C: ETHICAL CLEARANCE APPROVAL .....                  | 80 |

# CHAPTER ONE

## INTRODUCTION

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### 1.1 Introduction

The 1994 elections in South Africa brought about a democratic government. This resulted in a need for integration and for the opening up of new opportunities to previously disadvantaged communities. It was during this period that number of new entrants emerged into the Small, Medium and Micro Enterprises (SMME) sector of our economy. New challenges also emerged in terms of accessing finance for these SMMEs. The government as a result gave the DTI a mandate to establish mechanisms to support SMMEs through the policy for the promotion of small medium and micro enterprises (Berry and Van Seventer, 2002). Another factor which contributed to government introduction of the SMME support policy was the worldwide consensus among policy makers that SMMEs are drivers of the economic growth (Mahembe, 2011). It is against this background that this research project aims to examine the challenges in accessing financial support available for SMME with particular reference to UMzimkhulu Municipality within KwaZulu-Natal.

In investigating the access to funding towards their development by SMMEs, the researcher aimed to examine the existing SMMEs in the UMzimkhulu municipality to find out to what extent they were able to access any form of funding towards the development of their businesses.

This chapter as an introduction will focus on outlining the background and some issues surrounding SMME development. It will further deal with defining terms that will be of significance to the study also give the purpose and rational of the research. This chapter will also give the design and methodology that is used for this research as well as the limitations of the study and synopsis of chapters.

## **1.2 Background and Context of the Study**

Since the first democratic elections of April 1994, one of the critical issues in the South African economic sphere has been economic empowerment of the previously disadvantaged groups and general economic growth in the interest of both growth and development. South Africa has millions of citizens who are unemployed and underemployed. The reduction of unemployment and poverty are some of the challenges faced by the South African government. Therefore, the government is under an obligation to prioritize issues of job creation and to ensure sustainable and equitable economic growth (Mathibe and Van Zyl, 2011).

According to Hongbo Duan (2009), Small, Medium and Micro-enterprises (SMMEs) currently create most of the jobs in the labour market and are the penetrators of new markets in expanding economies. As is the case globally, the SMMEs in South Africa are an important vehicle to address the issues of job creation, economic growth and equity in the country that are being prioritized by the state. The funding for SMMEs must be seen as a component of an integrated strategy that is to strengthen the national economy such that productivity will be enhanced, investment stimulated and entrepreneurship will flourish (Fray, 2011). According to Fray (2011), there is a need for partnerships to be forged between government, community and business to facilitate the growth of the SMME sector. That is why the government needs to prioritize the development of SMMEs and the private sector has also been urged to assist in their development.

To this end, the government in conjunction with some of the financial institutions and development agencies has come up with funding initiatives in the economic arena especially designed for the entrepreneurs and Small Business Development. It must be noted that after 1994, the Government of National Unity of South Africa placed SMMEs as one of the items on its agenda and subsequently developed a number of policies and a White Paper that promoted SMME development (Fray, 2011). The national Department of Economic Affairs was tasked with the responsibility to set up structures that will look after the interests of SMME and hence the Department of Trade and Industry (DTI) established the National Small Business Council and the Nstika Agency (DTI, 1995). Despite these institutionalised mechanisms for assistance,, entrepreneurs themselves have been seen to

play a major role in bringing about their growth and productivity and, thereby, in the economies of their countries (Christensen and Poulsen, 2006).

The research on the SMME access to funding has been triggered by an interest in the way SMMEs are progressing in UMzimkhulu within KwaZulu-Natal. This interest was initiated through observation and the interactions with SMME's that occurred within the work life of the researcher and through personal experiences with a number of initiatives provided by funding institutions. There are challenges that are experienced by the SMMEs and these are particularly related to support that they get from funding institutions. It is against this background that this study believes that if an appropriate enabling environment and financial support can be created, SMMEs in our country can develop to great heights and can make a positive impact on the country's economy (Gallagher and Robson, 1997). The study therefore seeks to establish whether or not SMMEs access funding that is made available by various agencies and to what extent they do.

### **1.3 Definitions**

According to the *National Small Business Act (Act 102 of 1996)*, the term SMME covers a vast array of businesses, in terms of ownership, structure, sectors, activities, size and formality. There are four categories into which the National Small Business Act classifies small business. The four categories are: micro enterprises, which include survivalist enterprises; very small enterprises; small enterprises; and medium enterprises.

The term Small and Medium Enterprises (SMEs) is commonly used in many countries of the world while in South Africa a term Small, Micro and Medium Enterprises (SMMEs) is used (Mathibe and Van Zyl, 2011).

The micro-enterprises are made up of very small businesses, often involving only the owner, some family member(s) and, at times, one or two paid employees. They usually show lack of 'formality' in terms of business licenses, value-added tax (VAT) registration, and do not have business premises, operating permits and accounting procedures. Usually most of them have a limited capital base and only basic technical or business skills among their operators (Ntsika, 1998). Despite all the disadvantages and hardship, many micro-enterprises advance into becoming viable small businesses. The micro-enterprises

turnover, income and earnings levels differ widely depending on the particular sector they are in, the level of growth and phase of the business, as well as the access they have to relevant support.

The small and medium enterprises constitute the bulk of the renowned businesses, with employment that ranges between five and about 50 employees. These enterprises are usually owned and managed or directly controlled by the founding owners. It is unlikely to find them operating from business or industrial premises, or for them to be registered for tax purposes so that they can meet the required prerequisites for formal registration. It is difficult to classify these business in terms of assets they own and turnover that they make, given the wide differences in various business sectors they operate in like retailing, manufacturing, professional services and construction, as stated by The White Paper on *National Strategy for the Development and Promotion of Small Businesses in South Africa (2005)*.

#### **1.4 Research Purpose**

The purpose of the research is to investigate the access to funding towards the development of SMMEs and to examine problems that would be eased by funding investment in UMzimkhulu.

This research aims to establish whether or not SMMEs in the rural town of UMzimkhulu in KwaZulu-Natal benefit from funding and what problems could be eased through funding, if accessed. The focus will be on the practicing SMMEs. The study will also look at some of the documentation that relates to funding, such as notices, requirements and forms.

In Kenya, there is a co-operative bank, the largest by assets, which has a special product for SME support. Its financial support ranges from 15 000 US\$ to 300 000 US\$, repayable in six months (Mwobobia, 2013). However the SMEs do not qualify as they usually lack title deeds and car log books, the most commonly used form of collateral for borrowing money (Mwobobia, 2013). This kind of situation is not unique to Kenya as although there are various institutions which have been created with the aim of assisting the SMMEs here in South Africa, such as the Development Bank of South Africa (DBSA), the Small

Enterprise Development Agency (SEDA) and the Department of Trade and Industry (DTI), the SMMEs surprisingly do not use them or they are unable to access the support.

In order to achieve the purpose of the study as stated above, there are a number of key questions that were answered in the course of the study.

These questions are as follows:

1. Why do SMMEs need funding in order to develop?
2. What type of funding is available for development of SMMEs?
3. How is the information for funding conveyed so that the SMMEs are informed about the available funding?
4. Do the SMMEs take advantage of the funding that is available for their development?
5. Why do some SMMEs get funded, while others do not?

## **1.5 Rationale**

The researcher, as the Local Economic Development Manager in UMzimkhulu Municipality, is aware of the critical part that is played by the SMMEs in the economic development of South Africa overall and also within the UMzimkhulu Municipality in particular. However, experience of working in the arena indicates that the formal banks are reluctant to implement the funding strategy and schemes initiated by Government in relation to SMMEs. Since the researcher started working in the LED unit with cooperatives, formal and informal business, and private companies, he has come to realize that although funds are available for SMME development from various sources, such as government departments, SMMEs are not developing as well as they should. These constraints to the growth and productivity of SMMEs need to be better understood and addressed.

Furthermore, according to The White Paper on National Strategy for the Development and Promotion of Small Business in South Africa (2005), 'In recent years research on the trends, problems and needs of small enterprises among South African Universities, Technikons and other research centers has increased significantly'. Yet the volume of research with practical direction and policy relevance is still limited, compared to the needs of the country and its overall capacity to do research. This refers in particular to the development of a relevant systematic data base and trend indicators on the SMMEs as a sector with all its complexities. Such reliable data is critical for the assessment of policy efforts and the planning of policy reforms. This study has been undertaken in order to provide some of the required data.

The findings from this research could be used by:

- Government departments dealing with funding, funders and local municipalities to reduce red tape;
- Funding institutions and government, to improve marketing strategy;
- SMMEs, to gain better access to funding; and
- The funding bodies who design the criteria, to ensure that these criteria are user-friendly for the SMMEs.

The South African economy has been praised for surviving the economic meltdown that has been destabilizing the economies of the first world countries since 2008. The system and policies of the government are seen as the reason for the survival of the South African economy. However the unemployment rate is still high and many people who are unemployed are now turning to establishing their own small businesses in order to generate income. These small businesses are run by the owner who sometimes employs a few individuals, thus creating jobs. As a result many jobs are now created by the Small and Medium Enterprise businesses. This kind of situation has been a global trend in the past two decades as it is the SMMEs who have become the big employers of people rather than the large industries. The South African government has realized the contribution of this sector in economic growth and has come up with a number of interventions to help support or fund the growth and survival of this economic sector. Somehow the effort of the government and other stakeholders does not seem to reach some of the targeted

beneficiaries and hence this study aims to try and establish what the challenges or barriers are that impede the success of these interventions, with particular reference to UMzimkhulu SMMEs.

## **1.6 Design and Methodology**

In this chapter only an overview of the research design and methodology is given and chapter 3 will give details of the methodology. The researcher started by examining the literature available to him in the area of SMMEs funding and challenges to accessing finance. After having established the theoretical framework the researcher proceeded with empirical research.

The researcher used a qualitative research approach in the form of face-to-face interviews with individual respondents. The reasons for using a qualitative research approach was to gain more understanding of the known phenomenon (Strauss 1998). These were conducted with SMMEs within the UMzimkhulu Municipality. Some attention was given to criteria used by those government departments with funding mandates, private funding institutions and those with public/private partnership funding arrangements.

The researcher made prior arrangements with the interviewees to conduct interviews. The venues times were to be those convenient for the interviewees. The ethics for conducting research were followed which included a full description of the research and the right of the interviewee to participate of his or her own free will and that they could withdraw whenever they felt like doing so.

The interview questions were all designed such that they addressed the research question and to get the required data, the questions were grouped into themes so that the findings could be made that informed the recommendations. After data collection the data analysis process was started with the collected data grouped into themes and subthemes.



## **1.7 Significance of this research**

The purpose of this research is to examine the challenges in accessing funding by the SMMEs in rural areas and in particular in the UMzikhulu Municipality. This research aimed hopefully to make a valuable contribution to municipal policy formulation in relation to access to funding of rural SMMEs.

Here are a few areas where it can assist by contributing positively. For the purpose of this research, it will be necessary to look at the new *Small Business Finance Act* to see whether there is a possibility or not for the addition of relevant clauses to existing legislation that could address a number of fundamental issues regarding the access to finance by SMMEs. Here one could include some suggestion of steps or regulation to encourage existing financial institutions to become more active in the SMME-market segments, the facilitation of deposit-taking by lender NGOs, the recognition of certain non-conventional collateral types and the widening of scope for more specialized lending and investment institutions focusing primarily on SMME needs, as stipulated in the *White Paper on National Strategy for the Development and promotion of Small business in South Africa (1995)*

## **1.8 Limitations of the study**

The research objective was to conduct research that would inform the SMMEs' support policy developers about the challenges experienced by SMMEs in accessing support assistance, especially funding. The aim was to further draw attention to the gaps and to identify areas of improvement, not only to increase awareness of available support and perhaps make the process more user-friendly, but also to capacitate SMMEs by helping them acquire the required skills to fill in necessary forms to apply for funding from the different support programmes.

During the initial information gathering and literature review it became clear that this is a huge task for this research. The focus was therefore streamlined to look at challenges faced by SMMEs in accessing funding for start-ups and business expansion in UMzikhulu. This does not mean that information research and data collected will be substandard or irrelevant or that it will fail to assist other researchers elsewhere. All efforts were made to collect data that is relevant to achieve the objectives as outlined in the research. There will

be a need for further research from the recommendations that emerge from this study in order to ensure that the initiatives with good intentions to support SMMEs are achieved. It is important that the support from stakeholders in SMME support, especially in the area of funding like the commercial banks, development bank, private sector government and NGOs, must always be to the benefit of the needy SMMEs and not those that are already doing well.

## **1.9 Synopsis of Chapters**

**Chapter 1** presents the introduction and outlines the background and issues surrounding the funding to SMMEs for their development in terms of the *Constitution of Republic of South Africa* and related legislation.

**Chapter 2** follows with the literature survey that begins by discussing funding towards development of SMMEs in UMzimkhulu. Some of the attitudes towards SMMEs and their financing like those held by the Banks that view the SMME's as posing high risk, requiring the financial history of a business and sophisticated business plans with financial projections. This will be discussed together with their relevance.

**Chapter 3** deals with the research design and methodology which was used to investigate and evaluate the problem as identified. The researcher will be focusing on the empirical design in which qualitative data collection was used using face-to-face interviews. The data collected will be analysed by grouping information into themes.

**Chapter 4** outlines the results or findings and tries to analyze and interpret them with the intention of drawing conclusive results. The key themes that emerged were:

- i. Lack of access to information and advice;
- ii. Viable proposals or business plans;
- iii. Business regulations and legislation;
- iv. Lack of information and technology;
- v. Access to markets;
- vi. Lack of training in entrepreneurship and management skills;
- vii. Financial management skills;
- viii. Record keeping skills;

- ix. Managerial Skills and strategic planning;
- x. Required collateral security; and
- xi. Knowledge about funding available for SMMEs.

**Chapter 5**, the final chapter of the thesis, includes a summary of the main conclusions of the study. This chapter presents recommendations for further research, policy and practice in funding interventions by different funding bodies.

### **1.10 Summary of Chapter One**

In order for research to be effective it requires systematic planning and execution. This chapter has presented the background and context of the study, the definitions, purpose, rationale, design, methodology and chapter synopsis.

The background indicated the hopes and expectations of previously disadvantaged SMMEs in relation to their economic conditions when South Africa gained its independence. They had hoped that their economic conditions were to be improved drastically. Although a few were moved to better socioeconomic levels through programmes like BBBEE, this was not realised by the majority. There is now a strong belief that economic growth will bring a better life and resolve the current problems of unemployment and poverty. Since the expectations were not met through the change to a democratic government, there is a belief that there is still the need for economic freedom for those previously disadvantaged. They believe that this could be achieved through various methods, such as government nationalization of key industries that may absorb a huge labour force and in that way create employment and that the government should take back land by appropriation from the farmers and give it to the previously disadvantaged communities.

However the researcher has a strong suspicion that those methods will only play a small role. It is through the empowerment of SMMEs and financial support that many of the challenges will be eased and SMMEs will be able to create more jobs as the trend shows and economic standards improve.

The next chapter looks at the literature in relation South African economic conditions relevant to the topic at hand as well as policies on SMME development and assistance. The

chapter will try to find out what the literature says and what the gaps are in the literature and in the current legislation on SMME development.

## **CHAPTER TWO**

### **LITERATURE REVIEW**

---

#### **2.1 Introduction**

In order to inform my research question, namely, “what are the challenges for some SMMEs not getting funding and support?”, and the further question concerning how well they are informed of what is available for their development, the researcher has reviewed relevant literature. Part of the purpose of the literature review is to develop an understanding of the gap between policy and practice. How do government policies and strategies and funding structures available for the support of SMMEs, actually influence practice? In reviewing the literature the researcher looked at past and current theoretical viewpoints and studies that are relevant in exploring the key research questions.

Small and Medium Enterprises (SMMEs) are currently promoted in the policy because they are believed to be the current creators of employment and contributors to the GDP in most counties of the world including South Africa’s economy (Pretorius, 2005). There are agencies created for the support and development of SMMEs and there is funding earmarked for that. The question is: do the SMMEs really access those benefits created for them and what are the challenges experienced? This literature review explored what research was available that speaks to these issues and the problems that they have picked up as well as the identified needs for further research.

In the chapter themes that are presented are the global standing of SMMEs, changing views on SMME policies and SMME-related government programmes. Further sections consider how SMMEs have funded themselves over the years and issues facing SMMEs in their development as well as types of support available and funding challenges.

#### **2.2 The Economic Standing of SMMEs**

The economic outlook of South African macroeconomic management is highly rated globally and has boosted credit and investment internationally (Lehutso, 2003). However, there are some issues in the economy that do not support the glowing picture of the state of the economy. These include chronic poverty, joblessness and a wealth gap that continues

to widen (Lehutso, 2003). It is this view that led to looking at the SMMEs and access to finance so that there is a broader picture of the South African economy and to what extent financial accessibility can contribute to equitable economic growth and tackle the issues of poverty and job creation.

It is a generally acceptable fact that access to finance is an important element for economic growth in the microeconomic sector (Hellmann, 2007). It was believed that the pro-business government policies and strategies such as Black Economic Empowerment would create stability, particularly among the majority of the marginalised population groups (South Africa, 1996). As stated by Lehutso (2003), according to global standards South Africa has a well-developed financial sector but it is still not accessible to the majority of emerging small businesses and ordinary households. There is thus a need to focus attention on issues of supply and demand in the financial access and development of the financial services. Investigating accessing to financial services in South Africa is good starting point. . If these financial services had understood SMME challenges in accessing finance they would have come up with innovative ways and designs. They could also have attempted to improve access to finance especially to the SMMEs from the previous disadvantaged communities.

Lehutso (2003) made an important observation when she stated that services like insurance or being able to secure savings is an important step for SMME businesses to start saving money to ensure financial stability and business sustainability. This will help in trying to lessen the effects of shocks to income that may be caused by unplanned events such as death, illness or disaster and weather which may result in vulnerability or poverty. In case of a disaster SMMEs could lose their assets and their businesses and staff could become jobless overnight (Lehutso, 2003). These, together with an ability to take the initiative when it comes to income-generating opportunities. Generating wealth and investment over time is the best way to achieve a sustainable economy.

Not much was found in the writings about the level of access to financial services in South Africa and what is available is not easy to measure or to define precisely. It may be easy to ascertain the number of current users of a particular financial service but not easy to estimate the number of those who have access to some kind of financial service but choose not to use it because of red tape and costs related to keeping a bank account. There are a number of reasons that can be given by those who choose not to use financial services.

According to Lehutso (2003) in 2001 about 11 353,000 South African adults were in possession of at least one kind of a basic bank account, making this only 40 per cent usage by the adult population who use the banking services. Of these 17.6 million 35 per cent are in rural areas with 25 per cent in townships (Lehutso, 2003). The usage of savings includes informal rotating savings and credit associations (RASCAS) is standing at 12.7 Million that is 44 per cent of adults in possession of a basic bank account.

Credit usage statistics shown in a report (Lehutso, 2003) from a consumer credit bureau indicate that about 16 million people are credit active. This is 55 per cent of adults in South Africa. Insurance usage is at 11 million adults which is 38 per cent of adults this includes insurance-related products like life and funeral cover. However short-term insurance usage is at a mere 10 per cent for adults (Lehutso, 2003). These figures and statistics focus on individual consumers. However, this does not mean losing sight of business entities as distinct from individual ownership. But the SMMEs derive from those individual consumers. The constraints they face in accessing financial services are extended to their businesses even more so, because business is viewed as being high risk.

### **2.3 Changing view and policy background on SMMEs**

This section focuses on the background of what the South African policy environment for SMMEs is like and the various changes that have occurred in the past two decades. It will also focus on how the SMMEs have been affected by these policies.

In most countries the world over, in the past three decades there has been a paradigm shift in looking at the issue of prioritising support and development of SMEs (Aghion, 2007). In African countries in general, government support for entrepreneurs is found to be weak (Ekeledo and Bewayo, 2009). In South Africa there was hope that the SMMEs will provide employment to the poor. After 1994 business played an important role by influencing government policy-making such as in the Macro economic framework policy (Booyesen, 2001). The South African government developed policies that focused on Small and Medium Enterprises (SMEs) with the hope that this would assist in building the economy (National Small business Act No 102 South Africa, 1996).

Before 1994 the Government of South Africa focused its attention on large business and state-owned enterprises. It was only in the late 1970s to 1980s that the realisation came of

the importance of the SMMEs sector and the important role it has to play in the economy. The South African Democratic government started to give SMMEs an opportunity to be active in the economy hence a White Paper of 1995 introduced SMME strategy followed by policy design (Mathibe and Van Zyl, 2011). The aim of the strategy was developing, promoting and supporting SMMEs. The government wanted to level the playing fields in the economy. Different support mechanisms were introduced for development and support of SMMEs under the Department of Trade and Industry (Mathibe and Van Zyl, 2011). The Small Enterprise Development Agency (SEDA) Umsobomvu Youth Fund (UYF) and similar organisations were introduced to give support to this sector.

In May 1995, a government strategy was drawn up which resulted in a White Paper by the Department of Trade and Industry (DTI), the leading department for SMME development and support, referred to as: *A National Strategy for the Development of Small Business in South Africa (DTI, 1995)*. A year later, the *National Small Business Act* was passed by Parliament, which provided for the institutions to implement this strategy (South Africa, 1996). This strategy was to address the issue of unemployment, which is rife in South Africa, and to promote the development and support for SMMEs. One of the economic challenges facing South Africa, and especially the poor, was unemployment. This has been aggravated by the fact that every year hundreds of thousands of workers lose their jobs through big companies (like mining) shedding jobs, while at the same time, every year many new job seekers enter the field having finished school or having graduated from university.

SMME development and support has been seen as the catalyst for addressing the issue of unemployment as it is acknowledged all over the world that Small, Medium and Micro Enterprises are becoming the creators of most jobs and have a huge contribution to make to economic growth (White Paper on National Strategy, 2005). This strategy was to assist in the South African Democratic Government's programme of creating a better life for all. The act provided for the restructuring of the existing institutions and the establishment of others to support and to fund SMMEs to cater for unemployed youth and women.

Since the advent of the abovementioned policy, it has become one of the objectives of government in all spheres to promote development, to support SMMEs financially and to provide nonfinancial assistance. Most national, provincial and government departments



have developed strategies in line with the national strategy for the support and development of SMMEs, the Departments of Agriculture, Rural Development and Housing, to name but a few (Swanepoel, 2010).

The South African government strategy and policies that have been developed seem to predetermine the capacity to which the SMMEs are able to develop. This is because, such policies do not always seem to promote business as they were designed to do. Access to funding and resources and import licenses are not easily obtained by SMMEs and the government, therefore, needs to adapt the framework to cater for small businesses and thus make the playing field level for all economic role players (Luiz, 2002).

It is indeed true, as stated above, that all over the world, as well as here in South Africa, governments are attempting to assist the SMMEs for different reasons as they believe that the SMMEs are the creators of most jobs (Luiz, 2002). However, when they also do it in order to address unemployment and poverty issues, it becomes problematic as the push to enable SMME success can end up being a political issue. For instance, the South African government is trying to attend to issues of BBBEE and to assist the rural communities who produce traditional goods in arts and culture so that poverty can be alleviated (South Africa, 1996). SMMEs become exploited as a development mechanism because they are less capital intensive, use fewer resources and require less management than big firms (Luiz, 2002). These are some of the reasons why SMMEs complain of the shortage of capital resources, which plays a big role in their ability to invest in important assets like equipment and raw material, resulting in their inability to be sustainable and which ultimately can lead to their demise.

Although it is seen in South Africa that the government is trying to address the funding and capacity issues as per strategy, it remains to be tested whether those intended recipients do actually have access to the funding or whether it is more accessible to the rich who do not really need it, but who have the knowledge of the potential source of funding and assets (Luiz, 2002). It is important to mention that the private sector also needs to come to the party to support and promote SMMEs in complementing it by addressing the demand of small business and subcontracting them.

In the early 2000's the then president of South Africa Mr Mbeki was advised by business people and organisations like the National Chamber of Commerce (NAFCOC) Business

South Africa (BSA) and others on economic matters (Booyesen, 2001). However, many of these members became the beneficiaries of the government policies they helped to develop. These policies were dealing with both privatization and outsourcing of services. Their aim was to support Black Economic Empowerment (BEE). With BEE, the government wanted to uplift black business so that the poor may get jobs and move from poverty. However, the result is that a new rich black elite group is perceived to benefit more than the man in the street. The South African government had to rethink its strategy so that it can help benefit those it was created to benefit. This was not only the problem in South Africa but also elsewhere in the world (Mathibe and Van Zyl, 2011).

The following six changes were made in business support in the international arena which were: sustainable provision of service, client bases approach, poverty and gender to making the markets work for the poor (Mathibe and Van Zyl, 2011). However, with this shift there was a criticism in that not much has been done globally in the area of development and support of SMEs. The traditional approach of permanent donor funding that was used was not helpful to the needs of SMEs (Mathibe and Van Zyl, 2011). That is why this approach of permanent donor funding was stopped and a start-up funding approach was favoured for sustainable business support. The previous approach did not reach all small businesses in need of support. The new approach was aimed at more effectively reaching more small businesses (Mathibe and Van Zyl, 2011).

In 2005 South Africa introduced the Integrated Small Business Strategy. This followed after the unsuccessful strategy which resulted in economic growth without job creation. The *National Small Business Enabling Act in 1996* by Government introduced support programmes through the DTI such as Khula and Nstika to help in the skills development of entrepreneurs. However, they were not very successful. Thus, in 2005 a national strategy was introduced which focused on previously disadvantaged individuals giving them empowerment support and entrepreneur promotion to enhance competitiveness as a means of creating an enabling environment. To be specific, the policy looked at capacity-building, business growth transformation and access to finance and market opportunities. This was done in order to assist the SMMEs to contribute to the growth of the country's economy through creation of sustainable jobs by this sector (Mathibe and Van Zyl, 2011).

In this section policies were discussed that were introduced by the South African government with an aim of levelling the playing field for SMMEs from previously disadvantaged communities. The 1995 White Paper and a national Strategy for the development of small business were adopted. Also the 1996 the *Small business act no 102* was passed in 1996. BEE with the aim to uplift Black business and to address poverty and gender representation was introduced. Further in 2005 a White Paper was introduced with an aim to correct some issues that were not covered like the introduction of support agencies for SMMEs like SEDA, Ntsika and Umsobomvu to name a few.

#### **2.4 South African policy on SMME support programmes**

As South Africa was integrating with the rest of the global community and economy from 1994, it found itself having to cope with a number of challenges. One of the challenges was the enhancement and growth of its economy (Rogerson, 2004). Another was the alleviation of poverty among the majority of our citizens. Globally the economy works on the assumption that SMMEs are vehicles for economic growth and job creation. It is not surprising that South Africa decided to make programmes for the support of Small Medium and Micro Enterprises (Lehutso, 2003). This was done as a result of the view that SMMEs could have an impact on poverty alleviation, job creation and national economic growth. The first step was setting objectives based on competitiveness, employment creation and distribution of income. This was followed by policy development that was focused on the SMME promotion and development (Rogerson, 2004).

Like most countries after apartheid South Africa found itself in the forefront of developing a number of policies that were supportive of SMME (Rogerson, 2001). Policies like those promoting job creation, poverty alleviation and economic reconstruction were among those developed at that time. The Department of Trade and Industry released a new SMME strategy that replaced the policy that was in operation since 1994 (Rogerson, 2004). Due to limited data on these programmes it is not easy to tell how much impact the previous policy had on SMMEs. The change of this strategy can be viewed as a disappointment to the policy programmes that were introduced after 1994 such as the White Paper of 1995 focusing on Local Economic Development (LED) and black economic empowerment (BEE). The White Paper in 1996 *National Small Business Development Act* resulted in a

number of institutions supporting SMMEs like Nstika Enterprise, Khula Enterprise and tender advice centres (Rogerson, 2004).

In 1995 the government introduced a Growth, Employment and Redistribution strategy (GEAR) where the SMME development framework was reflected in the White Paper on Small Business and in the national *Small business Development Act of 1996* (Rogerson 2004). By developing these strategies and policies the SA government was moving in line with the best practice in both developed and developing countries of the world. The policy initiatives for SMME support led to the creation of institutions which were to be pillars of small business development. Nstika Enterprise Promotion Agency was created through government initiative through the DTI and its function was to assist SMMEs with non-financial business development services (Lehutso, 2003).

Khula enterprise finance was a wholesale finance institution which had to assist a variety of retail finance intermediaries to deal directly with SMMEs. It was created to provide institutional support like tender advice centres offering advice on tendering and tender processes as well as on new guidelines introduced. More important was the establishment of a decentralised support services which were later know as Local Business Service Centres (LBSCs) providing business information, business management, aftercare and networking with other service providers (Rogerson 2004). The other support services that were made available were the manufacturing advice centres (MACs) for SMMEs in Manufacturing, Local Industrial Parks (LIPs) and small incubator programmes supporting the growth of the new emerging enterprises. With all the support initiatives by government there is still limited data on the support programmes on the SMMEs as well as the impact they had in the economy as a whole (Rogerson, 2004).

The South African Government also hoped to alleviate poverty through SMME support (South Africa, 1996). There is some controversy as to the feasibility and practicality of that. However some argue that there can be some positive outcomes through such programmes that contribute to poverty improvement (Rogerson, 2004). Those who disagree argue that support programmes offer little to survivalist enterprises belonging to woman and rural and township groups. Those support programmes that favour black economic empowerment have become channels of wealth to some black entrepreneurs. They are said to have created wealth for a few because they have failed to reduce income

inequality within the economy of South Africa. Rogerson, 2004 estimated that only 4 to 6 per cent of funding was given to SMMEs belonging to previously disadvantaged groups while 95 per cent of it was used by Department of Trade and Industry to fund growth of white-owned enterprises (Rogerson, 2004). Even today the support that the BEE receives is still below an acceptable level.

Furthermore it was discovered that there is lack of knowledge in the SMME community as to how to access support services as a result of mistrust by SMMEs of the external agencies (Hellmann, 2007). The lack of capacity of institutions to create awareness of their existence and the uneven geographic distribution of support institutions as well as the cumbersome procedure involved in making application for funding has deterred SMMEs from applying for support (Kesper, 2001). Another stumbling block in the way of the success of support structures is the unclear priorities. It was not clear whether they prioritised economic, political or welfare objectives. Those who are in favour of welfare objectives in supporting SMMEs focused on poverty alleviation while those in favour of political objectives saw empowerment of the previously disadvantaged as important. Those who favour economic objectives focused on competitiveness. These conflicting objectives have led to a lack of clear criteria in selection for support. There is a need to have a balance in the SMME development objectives and not to focus on one at the expense of the other (Rogerson 2004).

The reasons given by Rogerson (2004) for no improvement in SMMEs and job creation are that the SMMEs tended to compete rather than complement the larger enterprises. They also often lacked the drive to expand to become more than a one person business and there was jobless growth. This means that even when they made profits economically they did not lead to employment creation for the bulk of the SA labour force (Kesper, 2001). Although the anticipated jobs were not created, the assistance was found to have had other results by default. Those results were poverty alleviation as many females and disabled people and rural communities participated in SMMEs economy and the survival groups were found to flourish (Kesper, 2001). This however does not mean the success of the government programme but rather of local government policy in terms of opening markets for the survivalists.

In realising that it had challenges to enhance the growth of its economy, create jobs and alleviate poverty, policies were developed that were biased in favour of SMME development. There were policies like the White Paper of 1996 on small business development and GEAR. The government further established institutions that were to assist SMME development. With all the interventions to assist SMMEs they continued to compete with big entrepreneurs rather than complement each other. The SMMEs also lacked knowledge for accessing services and funding. The established policies failed to address the problems faced by SMMEs of accessing funding created for them. This meant there were challenges that needed to be researched to address the SMME access to funding.

## **2.5 Government funding and support to SMMEs and their challenges**

This section will look at the various funding mechanisms and services that were developed to be of help to the SMMEs as well as challenges to determine why funding was not reaching the intended recipients. Soon after South Africa attaining its first democracy it created policies that were, as stated above, intended to uplift Black businesses and to address poverty.

Friedrich & Isaacs (2010) indicated that government service delivery all over the world has turned to Small Medium and Microenterprises (SMMEs). Globally governments have seen that their partnerships with SMMEs will make a positive contribution towards addressing environmental, social and economic problems. This is because of the realisation that in order to address the socio-economic and environmental challenges it is better to look to the private sector especially the entrepreneurs. South Africa as part of the Global community is not left out in this. We have also joined in with an aim to reduce unemployment and poverty (Rogerson, 2008). We have also done as the rest of the world has done by identifying SMME development as a way to address the socio-economic needs of the community. The South African Government has developed the national strategy for the promotion of SMMEs in 1995 with five objectives and eleven inhibiting factors that need attention (Friedrich and Isaacs, 2010).

The South African Government had a conviction that if they devise a policy framework to support SMMEs it will help them to triumph, become vibrant and contribute positively to sustainable jobs and alleviate poverty (Friedrich and Isaacs, 2010). This policy had an objective of job creation and poverty alleviation. They had hoped that part of this could be achieved by creating a level playing field between the developed business and the emerging business. This was to be achieved by using a special kind of service delivery to SMMEs. In order to achieve this they used the resources of government to support this sector. However when a review was done in 2004 by DTI it was realised that the service that was offered to support SMMEs was satisfactory. It was then decided that those non-performing agencies should be replaced by those that would meet the expected level. The mandate was to deliver to SMMEs relevant information, market intelligence, relevant publications, advice and mentoring facilities. Over and above they should assist in research and offer training and advice on training opportunities. The forms of support by government were focused on disadvantaged people of rural communities, women, youth and people with disabilities (Friedrich and Isaacs, 2010). Because there is no change in the existing landscape and challenges of the SMME the researcher decided to undertake further research. The aim was to check on how supporting organisations policies and resources are accessed by the SMMEs, and why there is no change in the economy and the SMME themselves. Despite the National strategy objectives which aimed at greater income facilitation, there was no sustainable job creation, no economic growth, no collaboration between small and big enterprises and no levelling of the playing field between big and small enterprises.

There were also inhibiting factors identified for the SMMEs to develop and access funding support that seem not to have been addressed by the supporting organisations and need to be part of the research. Those factors were: low education level amongst SMME owners; lack of transport; water and premises. Others were shortage of innovation experience and previous knowledge of business management (Massey, 2000). There are two other factors that were mentioned by Massey (2000) which are: necessity driven business start-ups; and lack of growth from small to big enterprises in the informal sector. Access to finance, inability to meet strict government regulations, shortage of risk takers and no aggressive approach were also mentioned. These factors inhibited the growth of SMMEs.

The South African government in its national strategy had five objectives and inhibiting factors. The strategy set up organisations through the DTI. These are Khula Enterprise, Industrial Development Corporation (IDC), Provincial and Regional and local government structures as well as training and research institutions in Technical Colleges and Universities (Friedrich and Isaacs, 2010). According to Friedrich & Isaacs (2010) these institutions lacked capacity and professionalism to deliver a quality service to SMMEs. Although the government was satisfied according to its report in the DTI, it replaced its strategy with the Integrated Small Enterprise Development strategy with three pillars to unlock entrepreneur's potential. These pillars were to enhance competitiveness of existing SMMEs, promote entrepreneurship and to create an enabling environment (Friedrich and Isaacs, 2010). In this strategy more SMME support organisations were recognised like the private services and community and private sector initiatives. There was some degree of confidence that service delivery to SMMEs would improve as a result of the existing ability of these organisations. However SMMEs had a negative attitude towards the private sector because of its bureaucratic principles and approach which are supply driven and which do not address the target groups. According to Friedrich and Isaacs, (2010) the SMMEs turned to use their own accounts and banks as supporting organisations were viewed as being incompetent in their support. As a result the SMMEs ended up not knowing the service providers and the services they provide.

Friedrich and Isaacs (2010) further indicated the contradiction in success of government strategy between DTI government and the SMME owner. Government claimed unsuccessful business support for SMME's indicates lack of knowledge by SMME's of the business support organisations and type of support available which is a barrier in SMME accessing this support. Further the location of supporting organisation in big cities means that they are out of reach of SMMEs in the rural and disadvantaged communities. This means that they only benefitted those in large cities. The colleges and Technical Universities used an old approach focusing on training instead of those that can be used by SMMEs to develop and result in growth. Most often the research results are not distributed to businesses.

As a result Friedrich and Isaacs (2010) recommended that further research be done to determine why SMMEs are not keen to use support organisations and another must compare those SMMEs that were supported to those not supported. They further stated that



the government objectives were currently not achieved. They recommended that as it is done worldwide there is a need to have collaboration between public private and non-profit sectors. The identified stakeholders need to contribute to the challenges of SMMEs to have a credible impact and difference in SMME development thus promoting job creation, poverty alleviation and economic growth.

This section in looking at services for SMMEs has highlighted that government intension to render services in order to uplift the black business failed. Those agencies which were created through the National strategy for Small Business in 1999 to promote entrepreneurship, capacity and fund start-ups failed to reach SMMEs. They failed to reach the intended beneficiaries by making them aware of the services they provide. They only focused on big cities where SMMEs were already doing well.

The government uses banks as intermediaries for its programmes to fund SMMEs. The reason given for this is that the banks have an experience in evaluating small and medium borrowers and in collection of debt. The banks also have an existing network of branches in most parts of the country including rural areas. Because of this they are said to be in a good position to administer funding programmes of the government agencies.

## **2.6 Challenges in accessing available government funding and services**

Worldwide the SMMEs are recognised as the important sector in economic and industrial development. As stated by Straus (2006), government should encourage SMME development by ensuring that capital is more accessible, by promoting entrepreneurship, by providing business education by reducing regulations and by protecting intellectual property. Most of the countries of the world have developed strategy and mechanisms to facilitate, promote and develop the creation of SMMEs. In South Africa the Government has done the same. However, to date little has been achieved. The failure rate of SMMEs in South Africa is between 70% and 80% and millions of Rands are invested in the programmes and are lost through failure (Ncwadi, 2012).

For the South African Government SMMEs promotion and support is one of the top priorities. This is demonstrated by the funding and the number of support structures developed for this sector after the enactment of the White Paper on SMMEs. The Department of Trade and Industry (DTI) was mandated to develop institutions to service

SMMEs like Nstika, Khula enterprise finance and credit guarantee and National Small Business Council. According to Ncwadi (2012) most of the small businesses, supported by Local Business support Service Centres (LBSC), were start-ups instead of existing ones.

The effort that was initiated by the South African government to establish structures to support small business has continued to fail by not being effective in achieving the goals created for SMME development. According to Ncwadi (2012) the failure rate of SMMEs was estimated to be between 70% and 80%. This means that the Millions of rands for this programme were lost as there was no measurable impact on business. Ncwadi (2012) highlights a few reasons for this failure: lack of capacity in the implementing agent's staff who are unable to offer relevant advice to entrepreneurs; locality of these centres that were based in large cities or towns and many in medium sized towns and no centres in small towns and townships where most of the survivalist population is to be found; information available was not easy to be understood by the new-comers in the business sector; and the inability to diversify the services as they were to service a wide range of businesses as envisaged. Ncwadi (2012) also viewed education level to be another thing that hindered the SMMEs from accessing support from the Local Business Service Centres (LBSCs) as only 8% had post-metric certificates and 13% grades 1 to 7 almost 51% had grade 8-10 and 14% grades 11 -12.

The support for small businesses is part of policy of the Government of South Africa that prioritises development and support for entrepreneurs (Ncwadi, 2012). That is the reason why the democratic government after 1994 developed a White Paper. It stated that it was to create an enabling environment so that the economy is turned around by equalising wealth as well as by creating sustainable jobs and through economic growth. They wanted to create cohesion between small and big enterprises. A recommendation was made that SMME support should not be based on local Business Services Centres (LBSCs) alone but on an integrated approach that needed to be used where all supporting stakeholders must play their part. Thus Ncwadi (2012) was in favour of an integrated strategy for SMME development where all challenges of SMMEs can be addressed. She says the current national Small business strategy although it is useful is only a starting point towards meeting the needs of the disadvantaged entrepreneurs in South Africa.

South Africa has an abundance of public and private sector funding available, however, there is little and disappointing utilisation of these funds due to lack of awareness of these programmes (Fin scope, 2010). These funds are not used because of lack of a single source of information available for SMMEs on how to access the available funds. This results in South Africa lagging behind other developing countries to promote growth and sustainability of SMMEs (DTI, 2010). To address this issue DTI has come up with an initiative to develop a directory to be used as a one stop shop to provide information that can be accessed by the Small business owner the directory is called the *National directory of Small business support programmes* (DTI, 2010).

This directory includes all national, provincial, local Government and other donors. It is revised annually (DTI, 2010). Some believe it is a good initiative but there are other programmes that were left out. Those left out are requested to forward their information on funding support for future inclusion (Harrington et al., 2010).

## **2.7 Private sector funding and support to SMMEs and their challenges**

This section looks at various private sector funding and support available for SMMEs as well as challenges faced by SMMEs to access them. These will include funding methods such as credit unions in the United Kingdom, stokvels in South Africa, NGOs and private banking institutions.

### **2.7.1 Credit unions and stokvels**

There is a form of saving and funding that is used by people and SMMEs to finance their business start-ups or development. This is known as credit unions in United Kingdom (UK) and Stokvels in South Africa (SA). According to Cornelius, (2009) credit unions involve savings by people who are trying to pull themselves up financially. They are sustained by members who do not want to rely on borrowed funding with costs. They prefer to use their withdrawals for children's education, home improvements and to start small businesses.

It works by members making voluntary regular contributions. They invest them for mutual benefit and profit, they grant loans and profits are distributed equally among its members.

In the UK a *Credit Act 1997* was developed that allowed people to register the credit unions in *Industrial and Provident Society Act of 1965* (Cornelius 2009). In South Africa the laws prior 1994 prevented access to banking for the majority of its citizens and after apartheid still many could not afford the exorbitant bank charges levied to manage accounts. This led to a proliferation of micro-lenders and loan sharks. Then an alternative was explored in the form of stokvels which are similar to credit unions. Stokvels are an informal funding organisation where members collectively put predetermined financial resources together and make rotating loans in turns monthly each receiving pooled amounts. Some become more elaborate by seeking profit using the collected resources for investment on properties and loans to credit seekers at a fair interest rate.

The *National Credit Act of 2005* content reflects that stokvels in SA were similar to credit Unions in concept. They both involve voluntary association and a pledge for mutual support for financial objectives. Both create a pool of capital generated by members, they offer credit and members receive shares. Both depend on self-regulation (Cornelius 2009). Cornelius (2009) also highlighted some differences between the two in that Credit Unions are subjected to regulation while stokvels have no regulation. The only regulation is the Banks provision under the *National Credit Act 2005*. In SA stokvels are common in SMMEs especially for business improvement and as a source of capital for a number of activities required by businesses.

## **2.8 NGOs and Private sector role**

Most of the organisations outside the public sector, the non-governmental organisations (NGOs) and community-based organisations (CBOs) which are active in SMME support, are faced with a decline in funding from foreign and domestic public funders. These organisations provide assistance to SMMEs in the form of funding, designing and research. Their support played a leading role in funding and spreading SMME support to less developed areas. However the funding support for SMMEs from these organisations is very scarce (Tim, 2011).

In the early 1990s some NGOs and CBOs entered the field of funding SMMEs with the hope of getting assistance from Khula to assist SMMEs accessing finance but they all failed and lost funds but at the same time some microfinance agencies made sizeable

profits on their investments through lending to a relatively small percentage of SMMEs (Tim, 2011).

## **2.9 Microfinance**

While banks were more willing to assist with lending to larger corporations, microfinance emerged due to a demand to serve the smallest enterprises. A rapid growth in the micro finance industry was prevalent in the early 1990s. There were about 1500 registered microfinance institutions that were registered with Microfinance South Africa (MFSA) by May 2008 (Skowronski, 2010). They provided small loans and have, since establishment, disbursed 412 820 loans to the value of R 532 Million. This sector has played a vital role in the financing of SMMEs because of the nature of its lending criteria which is simpler than that of the commercial banks.

## **2.10 South African banking sector and SMMEs**

The name 'bank' is synonymous with finance and this is the same when it comes to SMMEs. The researcher examined the literature to find out what the South African banking sector offer to SMMEs and how it is viewed by the SMMEs. On the 31 of December 2010 there were 17 operating commercial banks in South Africa and of these the four largest banks were ABSA, Ned bank, Standard Bank and First National bank (FNB) together they accounted to 84.6% of the total banking sector assets (Mahembe, 2011). The loan book of these four major banks revealed that standard bank has the highest SMME market share of 35%.

According to a 2007 world bank study on barriers to accessing loans it revealed that accessing banking loans in South Africa was very low compared to the international average and accessing an SMME loan took two times longer than other business loans (Dalberg, 2011).

The commercial banks have lending criteria. They check the business risk credit bureau for judgements. Also the fulltime employees of the business are checked together with their qualifications Commercial banks view SMME s as high risk businesses and as a result they use criteria that are stringent. Some require curriculum vitae and experience of the SMME

owners. For SMMEs banks will further look at management, marketing and financial skills to run the business. For business to be funded it will need to ensure that it has secured a business assurance for the business and owner as well.

The banks in funding SMMEs also look at the environment. Here they look at the type of industry portfolio as they believe some of the industries are regarded as high risk for example the textile industries. These are viewed in this way because of the high international competition. The other risk associated with SMME funding is the financial risk. Here the banks would want to share risk of funding with the owner by requesting a portion of owner contribution of around 20% to 25% for start-ups. A further requirement will be a demonstration of strong cash flow to support borrowing. Over and above this the banks would request collateral in line with the banks ratio. These criteria either discourage the SMME from applying for funding or they result in very few applications being successful and a large percentage of the SMMEs are unable to access funding that is available.

### **2.11 Challenges in accessing available private sector funding.**

A survey by the World Bank has rated South African banking system on loan processing very high compared to other banks around the world. South African SMMEs barriers to accessing loans according to the world bank 2007 study of world banking institutions is ranking very low as it takes 4.13 days to process an SMME loan compared to 11.03 worldwide (Beck and Demirguc-Kunt, 2009). Over and above this, South Africa has four leading banks that have support desks for small business lending or support portfolios.

The requirements by the lending banks and other funding institutions pose barriers to accessing funding and loan services (Harrington, 2010). According to Bae, (1987) the major barrier that is faced by SMMEs in accessing funding is the information between lender and borrower that is asymmetric. The large and small enterprises are subjected to similar criteria when applying for funding when they are not at the same level of development but when it comes to interest rate they are charged differently.

There are other factors such as Management competencies, availability of collateral and quality of business information that impacts negatively on a business's ability to access funding (Barbosa and Maraes, 2004). Chimucheka and Rugan (2001) found that some

SMMEs indicated that the high interest rate charged by banks for new enterprises and poor or unviable business plans and ideas affected their access to finance. The legality of the enterprise is one factor that affected access to finance as registrations make it easy to separate the owner from the business. Registered businesses rejected for funding were less than unregistered according to World bank enterprise survey of 2008 (Magistea et al., 2010). According to Fin Mark trust (2010) the age of the SMMEs also plays a role in credit access since the banks and creditors are reluctant to loan to new enterprises and supplier crediting is non-existent to the new comers.

It is common all over the world that SMMEs have less access to finance than larger enterprises (Harrington, 2010). It is further stated that about 59% of the SMMEs use credit products compared to 82% of large corporative. The micro enterprises are likely to report access to finance as the barrier to growth. Micro enterprises are also less likely to have a bank account. The financing institutions say it is more expensive to provide funding to SMMEs as they apply for small amounts which end up costing the banks in credit assessment and monitoring (Falkena et al., 2004).

A study by Chimucheka and Rugan (2011) of South Africa's SMME shows that of the 84% of SMMEs who applied for loans 25% were successful. However from the 25% successful applications about 85% accepted the loan and 18% ended up getting the loan. This was due to SMME failure to meet some of the terms and conditions of the loan application such as lack of collateral and lack of financial deposit (Herrington, 2010). The credit histories were also cited as the reasons for the rejection of loan applications.

The SMME owner's experiences with the banks are that SMMEs are prejudiced by the banks interest in skills and experience of the owner. As historically disadvantaged entrepreneurs' they score poorly in these areas. The banks believe that the higher the managerial level of owners the greater will be the potential viability and survival of the SMME It will be likely to be successful and thus likely to access credit (Rudez and Mihahi, 2007).

African owners are likely to use bank loans for working capital despite the subjective hindrances. The previously disadvantaged SMMEs have historically been undermined in the accumulation of traditional resources (Falkena et al., 2004). They cannot use their

resources as security for loans which are refused. This means that a large demand for loans by SMMEs is unmet as they have difficulty with access.

New SMMEs encounter problems in providing quality reliable information. They also encounter problems in accessing information about credit standing and risk of borrowing as they do not have a credit history available for them to hand to the banks or credit bureaus (Falkena et al., 2013). The new enterprises need to develop comprehensive business plans that can assist them to access funding. It is common amongst SMMEs to depend on their own funds or family and friend's funding as they find it difficult to access bank credit and supplier credit (Magistea et al., 2010).

The demand for loans in SMMEs is less as many of them do not want to apply for a loan for a number of perceived reasons such as fear of the high rejection rate. Some also cite no need to apply for a loan (Mengistae et al., 2010). These SMMEs believe that the applications from SMMEs hardly ever succeed and therefore they prefer not to attempt to apply for funding. The second group just do not believe in a loan application as they either have their own sources of funding or they do not think they will meet the criteria for a loan as these are too complicated. This suggests that there is a need for loans but SMMEs believe that they have very little chance to access the loans. Another study showed that some SMMEs never applied for any loan from the banks citing reasons that they do not know sources of finance and the procedure for applying for the loan (Chimucheka and Rgani, 2011). In some instances the loan application does not get a response from banks as to why they were not approved.

## **2.12 GAP funding source for SMMEs**

A number of bottlenecks exist in developing countries that affect the growth ability of SMMEs. These include funding, lack of managerial skills, equipment, regulations and technology (Anhever and Sabel, 1987 Steel and Webster Gockel and Akoena, 2012). A significant constraint is placed on SMMEs due to lack of managerial knowledge. These SMMEs have self-motivated managers who cannot compete with larger enterprises.

The gap still exists in the SMME sector despite the training and advisory support by other institutions (Kayanula and Ouatey, 2000). There are two reasons for this, one being the



SMME inability to afford the high cost associated with training and advisory services the other being that some do not see a need to upgrade their knowledge and skills (Aryeetey et al., 1994). According to the Fin scope survey (2010) the gap is further created by the number of people who do not use any financial services or products who use own or friends and family funding. This group do not even apply for funding as they don't have knowledge about financial products and even if they did they do not meet the minimum application requirements like bank statements and financial credit records.

### **2.13 Equity and debt financing**

Equity and debt financing are the two sources of external finance for new SMMEs (Demirguc, Kunt et al., 2006). Equity or venture capital is usually not available for new SMMEs as a result of the SMMEs depending on banks loans whose access is very limited especially to new SMMEs in developing countries (Mengistrae et al., 2010).

Having mentioned lack of funding to SMMEs in South Africa and other parts of the world (Herrington et al., 2010) the MFI came to service the SMME sector while banks serviced the larger corporations. However some of the SMMEs are still left out as they fall between the two markets where there is a gap (Mengistrae et al., 2010).

### **2.14 Summary of Chapter Two**

The purpose of this study was to assess SMME access to funding and challenges experienced by SMMEs in this regard. It also intends to make policy recommendations. The literature review revealed some consensus that exists among different researchers about the challenges and shortcomings in funding and access of funding for the SMMEs. Emanating from the literature review in this chapter there is a strong belief that SMMEs have a huge role to play in the economic development and job creation. It is also clear that the South African Government is prepared to offer support to SMMEs both financially and in capacity building. However the support seems not to be achieving the set goals especially for the masses of SMMEs that were previously disadvantaged hence most do not survive.

This shows that there is a need for the research to establish what the challenges are that are faced by the SMMEs to access funding support that is created for them. The other area to be looked into is whether or not the agencies that are currently in place to support SMMEs are doing enough to assist them? It is a view of other authors that government financial services need to look at their strategies involving how they are helping SMMEs to access the support available.

It is true that SMMEs still encounter challenges in their development due to lack of access to funding that is available for them because of a number of barriers ranging from lack of knowledge to high or strict requirements that they cannot meet because of their level of growth. The following chapters looks at the SMMEs and they will try to establish the challenges that they encounter in accessing support provided by different institutions.

## **CHAPTER THREE**

### **RESEARCH METHODOLOGY**

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#### **3.1 Introduction**

This chapter discusses the research design and the approach that was used in this research. The researcher explains how data was collected for the study and also provide a rationale for the credibility of the research approach and the validity of the data.

#### **3.2 Study Design**

The area of SMME development and access to funding in the UMzimkhulu Municipality is very challenging, as was presented in the literature review in Chapter Two. An exploratory research design with the qualitative research approach was therefore selected with the aim of gaining insight into challenges faced by SMMEs when trying to access funding to start and grow their businesses. This is appropriate to enhance knowledge when there is a gap in the literature (Sekaran, 1992). In this case, the gap deals with SMME access to finance whilst looking at the environment within which the SMME businesses are placed.

#### **3.3 Qualitative research**

The approach used for this is a qualitative research study. Leedy and Ormrod (2014) highlight that qualitative research is particularly appropriate for rich description and in-depth understanding within a purposive research sample. It is intended to enrich understanding of perspectives rather than to give indicative data relating to a representative sample of a large population. The researcher intended to identify the key problem areas that SMME's are experiencing in their relationship with government support agencies.

This is of particular interest to the researcher as a LED practitioner because it informs his own learning. In this study, a qualitative research method, which is sometimes called a natural inquiry, was used because it focuses on the natural setting where there are no predefined responses and no response is taken for granted (Sherman and Webb, 1988). In other words the study looks at events as they happen as respondents speak for themselves. In a qualitative approach, in-depth interviews are conducted with an aim to get a deeper

understanding of similar causes and effects of particular events. In this way the researcher can establish accurate knowledge and come to understand situations and come with detailed descriptions and analyses as described by Carson and Gilmore, (2001).

### 3.3.1. Why qualitative research was used in this study

Qualitative research methodology was used because the researcher considered this approach best for this research. The researcher wanted to know what experiences the SMME's encountered in the life history of their businesses. This method was best in that it can meet a variety of the study objectives like identifying and examining experiences as well as cause and effect (Wellman, 2005).

Through the qualitative research the researcher comes face-to-face with the respondents who share their personal behaviour, experiences and how their daily life is influenced (Eisner and Peshkin, 1990). The qualitative research is useful in understanding different behaviour of people as their daily life forces them to react in a number of ways in responding to different circumstances. The qualitative method also allows the researcher to have a holistic overview of a particular context under study as it is conducted through contact with respondents (Miles and Huberman, 1994).

The qualitative research approach is associated with collection and analyses of verbal text or direct observation of behaviour (Cassell and Gallian, 2004). The benefits of this kind of research are that the researcher is provided with direct information in the form of stories told by the respondents. These stories can be analysed and shared through information sharing so that other people can learn from other people's experiences and feelings.

## 3.4 Data Collection

The data collection process entailed setting the parameters for the study, collecting information through semi-structured interviews, management reports and determining protocols for recording data/information.

### 3.4.1 Ethical Issues

Wellman, Kruger and Mitchell (2005) stated the importance of ethical consideration in doing research which ensures that researchers do not manipulate respondents and that they treat them with dignity when data is gathered. The researcher followed University of KwaZulu-Natal approved protocol for conducting the study, prior to collection of data (Appendix 3).

In this research permission to conduct the research was sought from the respondents who signed Informed Consent Forms (Appendix 1) which were outlining the aim and objectives of the research as well as their rights of refusal to participate or withdraw from the research. The respondents were informed that their names and businesses would be kept confidential and that they were not going to be prejudiced in any way. This was done especially because the researcher works in the Municipality as an LED practitioner and he is usually in interaction with the SMME's offering different types of information and assistance.

### 3.4.2 Data Collection Process

The research explored funding challenges experienced by SMMEs in the uMzimkhulu Municipality which meant focusing on the human aspect of behaviour and characteristics by examining the individual feelings, experiences, perceptions and opinions (Leedy and Ormrod, 2005). The chosen method of gathering data was to interview the selected participants and a semi-structured approach was adopted where the largest part of interview was guided by a list of question and issues to be explored.

#### 3.4.2.1 Primary data collection

Primary data collection through interviews and direct observation was seen as being appropriate for the study because data was collected directly from the affected SMMEs through face-to-face interviews and discussions with members of the affected community. Data collected through interviews is regarded as a rich data which allows the respondents to share their experiences and feelings on the study being investigated (Leedy and Ormrod, 2005).

### 3.4.2.2 Secondary data collection

Various reports from different funding institutions especially those owned by government were analysed which served as a means of collecting data. Wellman (2005) indicated that secondary data can comprise published research, internet materials and media reports which can be used to build a shared picture of the study being undertaken.

### 3.4.3 Interviews

The research questions were formulated to be used for interviewing a representative sample of SMMEs in this research. The questions assisted in evaluating the current challenges encountered by SMMEs in accessing support funding from the banks and from government and other funding agencies. The interview questions will also help to establish recommendations towards addressing the challenges encountered by SMMEs. The researcher administered the interviews face-to-face to a sample of SMMEs personally. The researcher's interview aimed to provide some information on the lending criteria used by both banks and government schemes towards SMME and challenges thereof faced by the Small businesses. The interview method was chosen because it is an interaction between an interviewer and the interviewee with a clear aim to get information that is valid and reliable. By using an interview tool a large amount of valuable data can be collected within a short space of time.

There are three types of in-depth interviews that are closely related as stated by Bogdan and Taylor (1984) namely life history interview, in-depth interview, and participant observation research. Each interview is done in order to draw some information from the participant. The life history interview is usually used when the researcher intend to capture the salient experience in an interviewees life as well as their description of those experiences thus revealing the inner feelings of a person. With the interviewer being a person familiar with the community and their culture they will interact comfortably with respect and confidence.

On the other hand an in-depth interview can be described as having face-to-face encounters between the interviewer and the interviewee on a number of occasions with an aim of getting direct information and to know the perspective and experience of the participant

regarding the situation. Sometimes this type of interview can be used in order to get information about those activities that cannot be observed thus the interviewer will depend on the description of the interviewee and on his views of the events. The questions used have been designed to gather information in line with these methods so that the researcher could acquire enough information to make informed recommendations.

To guide the interview the rationale for research and reasons for the interview was used as a framework for the interview. Some structured interviews are of a conversational nature as defined by Ballard, (2002), as they provide a detailed in-depth and rich textual material. The conversation depending on the interest and experience of each interviewee may flow discovering other important information.

Interviews were about 20 minutes long. Permission was sought from the interviewee for the interview to be recorded. Some notes were taken during the interview and later edited with the help of the recorded interview. The interview allows the respondent to discuss issues in their own words from their perspective and can explain further when necessary. The researcher can also explore deeper. With this method the researcher may reveal interesting themes and perspectives which will explain the respondent's interpretation and understanding of their environment. The interviews were conducted between February and June 2014. Since the study was qualitative in nature, the research questions focused on perceptions, views, ideas and feelings of the respondents in respect of the research topic.

To ensure that the main areas for discussion were covered and to provide structure and direction, the questions were developed with guideline themes. The approach used was flexible in that it uses interview question sequence but at times the sequence was not followed. This was done to allow for the flow of conversation (Kitchin and Tate, 2000). The interviewer kept track of the issues already discussed and steered the conversation in the correct direction when he felt it was going off track. The respondent sometimes takes the conversation in other directions due to their feelings about the experiences thus raising other important perspectives unrelated to the issues at hand.

Some of the issues initially were not adequately explored in the way that one would have liked. The researcher in the later interviews managed to focus more on important issues. The method used also helped to gather a wealth of unexpected information that would not

have been gathered if another form of research design had been used like a quantitative design.

The research questions drew on theory which guided the study and were structured in accordance with the research questions (Appendix 2) which investigated the following issues:

- Why do SMMEs need funding in order to develop?
- What type of funding is available for the development of SMMEs?
- How is the information for funding conveyed so that the SMMEs are informed about the available funding?
- Do the SMMEs take advantage of the funding that is available for their development?
- Why do some SMMEs get funded, while others do not?

### **3.5 Sampling method**

Sampling is one of the research design requirements that serve as the criteria for the evaluation of the reports for research (Welman, 2005). It is therefore important that a sample is defined before sampling is discussed. To discuss a sample it is better first to talk of a population so that a distinction is made between the two. Population is the sum total of all cases, units of analysis from which a sample is taken. Therefore the sample is a unit of analysis drawn from the entire population. The unit of analysis refers to the elements or members of the population it may refer to humans, organisations events and human products (Welman, 2005).

In this research, fifteen SMME's that were interviewed were selected purposely and participated willingly and generalisation was made from the findings. Sampling was used because it was not practical to use all members of the population in the research. In human behavioural sciences it is usually not practical to involve the whole population as that usually deals with a large population (Welman, 2005).

Welman, Kruger and Mitchell (2005) emphasized that purposive sampling depends on the researcher's choice in selecting participants and this has advantage of being economical



and convenient because participants are easily identified in view of their experience of the issue being investigated.

The UMzimkhulu Municipality SMME database was used to select participants from different sectors. The data base comprises 350 SMMEs 50% being retail, 15 construction, 15% hospitality and catering and 20 % in arts & craft as well as manufacturing. Participants comprised five from retail, three from catering and hospitality, three from construction and four from crafters arts and manufacturing sectors. Selection of different sectors was done to ensure that the sample used represented different sectors of UMzimkhulu SMMEs also the random selection method was used in each category to select SMMEs.

A list was generated with candidates to be interviewed and the candidates were contacted telephonically in order to request an interview.

The table below indicates the demographic and sector information of the respondents sampled for the interviews:

Table 3.1: Demographical Information of Sample: Interview respondents

| Respondent | Gender | Sector                   | Years in business | Date of interview |
|------------|--------|--------------------------|-------------------|-------------------|
| R1         | Female | Crafter                  | 8yrs              | 03-11-2013        |
| R2         | Female | Crafter                  | 19yrs             | 14-01-2013        |
| R3         | Male   | Retailer                 | 27yrs             | 15-11-2013        |
| R4         | Female | Catering and hospitality | 7yrs              | 15-11-2013        |
| R5         | Male   | Retailer                 | 20yrs             | 18-11-2013        |
| R6         | Female | Retailer                 | 29yrs             | 19-11-2013        |
| R7         | Male   | Construction             | 10yrs             | 20-11-2013        |
| R8         | Female | Construction             | 16yrs             | 22-11-2013        |
| R9         | Male   | Retailer                 | 21yrs             | 25-11-2013        |
| R10        | Male   | Construction             | 18yrs             | 26-11-2013        |
| R11        | Female | Catering and hospitality | 11yrs             | 26-11-2013        |

|     |        |                             |       |            |
|-----|--------|-----------------------------|-------|------------|
| R12 | Male   | Retailer                    | 30yrs | 27-11-2013 |
| R13 | Male   | Catering and<br>hospitality | 4yrs  | 28-11-2013 |
| R14 | Male   | Crafter                     | 10yrs | 29-11-2013 |
| R15 | Female | Crafter                     | 10yrs | 02-12-2013 |

### 3.6 Data Analysis

According to Irvine and Gaffikin (2006) data analysis is supposed to be done concurrently with theory development leading to data collection. The researcher can start early to understand and nurture the study as it continues, but it should be allowed to grow naturally without being predictable (Irvine and Gaffikin, 2006).

In this study the researcher organised data, breaking them into manageable units, searching for patterns and identifying important lessons. After which the relevant data was shared with others. This is emphasised by Westbrook (1994) who highlighted qualitative data analysis requiring an ongoing process that feeds back into the research design and fulfils the objectives of the study.

After each interview the researcher created some time on the same day to try to transcribe and analyse the interview. This chapter presents the analyses of the data collected through qualitative research in the form of interviews. The interviews were conducted to investigate SMME access to funding and challenges they experience in UMzinkhulu Municipality.

It is not an easy task to come up with a generally acceptable definition of qualitative data analysis however the one by (Babbie, 2007) seems to serve as a good working definition: “Qualitative analysis is the non-numerical examination and interpretation of observations, for the purpose of discovering underlying meanings and patterns of relationships.”

In research it is easy to be lost in logistics of data collection and to lose sight of theory as stated by Babbie (2007) however with qualitative research it is unlikely as theory, data collection and analyses are entangled. Content analysis was used to obtain results from

various open-ended questions. Once data was collected themes were developed from highlights within the notes. The literature review details combined with the other information to form part of the detailed thematic system.

### **3.7 Validity and Reliability**

Reliability and validity of data can be ensured through the researcher's understanding of the industry and also of the subject; in this case, the researcher is in the LED practitioner working at UMzimkhulu Municipality and he understands the sector as well as the environment. The researcher remained objective and not biased in his opinion which makes the research trustworthy. IsiZulu as the participants vernacular language was used to engage participants, which made them felt comfortable in expressing their opinions and responses later translated by the researcher who understand both languages to ensure that ambiguity was eliminated (Creswell, 2009).

### **3.8 Limitation to methodology**

Some slight limitations were experienced in relation to the data collection methods of using an interview. The limitation was as a result of the process of data collection method as it was lengthy due to the types of questions used which were open-ended. Another limitation was due to the perception of the respondents who felt that the interview was invading their privacy as questions were inquiring into part of their life history and their businesses. Some SMMEs were not willing to reveal some information due to researcher coming from the government institution dealing with business, however, assurance was given that the research was for academic purposes only.

### **3.9. Summary of Chapter Three**

This chapter contains a detailed explanation the researcher's methodology followed in doing this research. The reason for using face-to-face interviews to extract information, to analyse and evaluate whether or not the Small, Medium and Micro Enterprises (SMME's) of UMzimkhulu had access to funding was discussed. Also, the chapter elaborated on the limitations of the research methodology used for this research. The chapter covered the aspect of verification of information to ensure trustworthiness in the research. Lastly the chapter dealt with some of the challenges faced by the researcher when engaging in this

process, such as availability of interviewees and time limitations. Challenges will always be encountered as interviews depend on availability of people the SMMEs who are dynamic and have diverse lifestyles. The next chapter looks at the data that has been collected and organise it into themes which will form part of the research findings. The responses will be analysed against the research questions and research objective and discussed with reference to the literature review.

## **CHAPTER FOUR**

### **DATA ANALYSIS DISCUSSION**

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#### **4.1. Introduction**

In this chapter the focus is on the research findings as emanating from the interview responses to the key questions of the research and research objective which was to establish whether or not SMMEs in the rural town of UMzimkhulu in KwaZulu-Natal benefit from funding and what problems could be eased through funding if accessed. Some key questions that arise from the general enquiry are: Why do SMMEs need funding? What funding is available for SMME development? Are there any SMMEs who have accessed funding and what are the challenges faced by the SMMEs in accessing funding? Categories of information were elicited from the respondents. The following are some of the points that are covered as they emerged in the data collection and from the literature review: viable proposals or business plans, Banks view the SMME's as posing high risk, business regulations and legislation, Lack of information and technology, access to information and advice and accessing markets, to name a few.

#### **4.2 Themes and sub-themes**

In analysing the data from the interviews the notes were read a number of times in order to develop themes and highlights discovered within the notes. The interview highlights and some literature review information from research literature were all combined to form part of a detailed thematic system. The data collected was analysed using thematic analysis. The available data collected was firstly condensed and then structured into the following categories of themes:

- There were those that pointed to the SMME owner's lack of skills for example lack of financial management, record keeping and entrepreneurship training.;
- There were also some that pointed to Banks attitude and criteria that they use towards the SMMEs, for example, banks view SMMEs as requiring high risk collateral.;

- There were those that link to geographic positioning of the area under research; that it is rural small town where most resources and information channels are lacking.; and
- Finally there were those that link to the regulatory environment that impact positively and those that impact negatively.

Other issues of importance are:

- Viable proposals or business plans;
- Banks' view the SMME's as posing a high risk investment;
- Business regulations and legislation;
- Lack of information and technology;
- Access to information and advice;
- Accessing markets;
- Lack of training in entrepreneurship and management skills;
- Financial management skills;
- Record keeping skills;
- Managerial skills and strategic planning;
- Required collateral security;
- Knowledge about funding available for SMMEs; and
- Lack of access to finance.

These main themes emerged from the qualitative data collected through interviews. The themes give expression to the feelings of the SMMEs with regard to challenges to accessing finance in their business environment. Although it was based on the rural UMzimkhulu SMMEs the issues may be true for other rural communities located remotely from big and advanced economic hubs.

### **4.3 Requirements criteria from funders**

In this section the requirement by both commercial banks and public sector of viable business plans and proposals were covered. These requirements were looked at in relation to how they influence SMME access to funding.

#### 4.3.1 Viable proposals or business plans

Here the respondents highlighted how the requirement of viable business plans or proposals had a negative impact on them in their efforts to access funding. They stated various challenges such as lack of skills to compile these documents in a way that is acceptable to funders. They further indicated the challenge of getting assistance from the agencies that were created to help them as they are based in large towns away from rural communities.

As a response from a question asked to find out if the SMMEs knew about the funding institutions. While they were aware of their existence only respondents R1(13/11/2013), R3(15/11/2013), R4(15/11/2013), R7(20/11/2013), R8(22/11/2013) and R11(26/11/2013) approached the banks for funding. Out of those only R 3(15/11/2013) was successful to a point of getting the funding. All the six respondents had approached more than one bank for funding where they were not successful until only one got the loan funding. It is therefore important for the development funding institutions to relax their funding criteria so that more SMMEs can get access to the funds available for their development.

Almost all the respondents who approached the banks for funding have indicated that they were aware that banks do offer funding in the form of loans however the process was complicated and need a lot of documents. SMMEs have pointed out that banks in order to fund they put their requirements upfront and one of them is a viable proposal or business plan. The SMMEs were told that the banks as businesses were expected to make a profit, hence they could only lend to businesses that provided them with viable initiatives. These could be start-up business or those that aimed at growth and development.

One respondent from those who had applied for funding from the bank was outraged by some of the requirements that were requested for the application since the application was for a business start-up. “When I was applying for funding to start my business from the bank they requested the vat registration number a copy of the tax clearance and the financial statement” R7(20/11/2013) “When I applied for funding one requirement was that I provide the business turnover when my business had not made any money” R4(15/11/2013).

Nine of the respondents (R 2(14/11/2013), R5(18/11/2013), R6(19/11/2013), R9(25/11/2013), R10(26/11/2013), R12(27/11/2013), R13(28/11/2013), R14(29/11/2013) and R15(02/12/2013) chose not to approach any banking institution and instead preferred to use their own savings or family financial resources. The common reason for not approaching the banks was that banks required viable business plans and this was too complicated for many potential applicants. They were of the view that to come up with a viable business plan required some expertise to meet the banks requirements of viability. The SMMEs needed some external assistance to develop such business plans and because of the rural nature of the town such services are not readily available. One respondent R10 (26/11/2013), who was not able to source funding because he was discouraged by the requirements from the bank that he could not meet, stated:

“I talked to one of the businessmen about the funding I was looking for and he said I need to have a good business plan if I want money from the bank and I should not take a chance but get some professional person to assist me to be successful”. R10 (26/11/2013).

One respondent R8(22/11/2013) who ended up using his own savings said:

“It seems as if the banks do not have any other means to assess the viability of the businesses except the business plans. It is so interesting to note that my business having used my own and family resources it has managed to do very well and has grown.” R8(22/11/2013).

It is important to note based on the findings that most of the respondents never approached the banks due to assumptions of the complicated banking system. It is important to note also that of those who did approach the banks only one was successful and they also cited the bank application process as being problematic as it required a viable business plan. This removes the notion that the issue of a viable business plan is just an assumption but a reality which keeps SMMEs away from approaching banks for funding. Most respondents who approached the bank for funding mentioned that the development of a business plan as required by the banks requires a particular skill which they do not have.

While on the issue of viable business plans the analysis of data from those respondents who approached the funders R1(13/11/2013), R3(15/11/2013), R7(20/11/2013), R8(22/11/2013), and R11(26/11/2013) shows that they had gone to request the services of professionals to assist in development of their business plans. They stated that they heard



from other business people in Durban a city about 250km away that there were consultants who assist in developing business plans. Just because they had transport, they contacted those consultants. It is also noted by the researcher that not all of them were successful even having business plans developed with the help of the consultants. Only R4(15/11/2013) made his own business plan with the help of his daughter.

Those that were unsuccessful did not know why their applications were not successful as they were only informed that their applications were unsuccessful R1(13/11/2013), R4(15/11/2013), R7(20/11/2013), R8(22/11/2013) and R11(26/11/2013). They were of the view that their business plans were not as viable as the bank required. This was just an assumption which they had. They indicated that they were not told but it was their view.

Those who did not approach the banks said they are aware of other people who applied to the banks for loans and were not successful because they did not have good or viable business plans. These SMMEs said they do not have knowledge and skill to develop a business plan so it prevented them from applying. From the above the researcher noted that the issue of viable business plan is one of the hindrances for business to approach banks for funding.

One of the questions asked in the interview wanted to know what the SMMEs know about the government assistance funding schemes. According to respondent R1(13/11/2013), R3(15/11/2013), R4(15/11/2013), R7(20/11/2013), R8(22/11/2013), and R11(26/11/2013) the schemes are known for not focusing on the collateral but they also look for the viable business plans or proposal. According to Strause (2006) government should assist SMMEs by capacitating them with skills to be able to meet the criteria set by funders for accessing funding. This is the same problem with the banks as these SMMEs are having a problem with banks on the similar issue of not being able to provide good business plans due to lack of financial training.

It was also noted that there is a need for these funding institutions including banks to give feedback to the SMMEs not only to say the application is successful or not but to further give reasons for the rejection. This will assist them to come up with better proposals or the funder can further assist in directing the SMMEs to people or institutions who can assist in the development of better proposals.

#### **4.4 SMME's as posing high risk**

This section will present the SMMEs challenge of accessing finance because their sector is viewed as high risk by the funding institutions especially commercial banks.

It was noted by most respondents that they were informed that the banks are reluctant to lend SMMEs funding because they are a high risk in terms of their ability to pay back R1(13/11/2013), R4(15/11/2013), R7(20/11/2013), R8(22/11/2013), R9(25/11/2013), R11(26/11/2013) and R15(02/12/2013). There were two things that were common among the respondents in relation to this statement. One is that the SMME sector is unreliable and highly competitive and therefore unsustainable. This is supported by a statement from Beck (2009) that banks' lending is based on the sector risk. Those that are viewed as high risk do not access funding very easy. Their business was penalised for not having statements detailing cash flow this would be demonstrated in the risk portfolio as part of the business plan. The second one is that the SMME owners failed to produce tangible collateral outside the core business. This statement also came up in the literature review where Herrington (2010) stated that banks are reluctant to lend to SMMEs because of their lack of collateral and lack of a financial deposit. Almost all SMMEs respondents supported this view by saying those in urban areas are better off because they have property which they can use as collateral but if they are from rural areas their properties do not have title deeds. The example is R1(13/11/2013) who stated that " When we ask what type of collateral is required the funders ask for investment or life cover policies as well as title deeds for property we own, when we tell them that in rural areas we do not have title deeds as we live on communal land than we get rejected. " The banks recognise the properties with title deeds as collateral.

This can be regarded as a huge setback in the ability of the UMzimkhulu and other rural SMMEs to access funding and only one out of six respondents, R3(15/11/2013) was able to get hold of a loan from the bank. The risk in banks goes with the interest that will be required from the lender. Therefore since the SMMEs were regarded as high risk business they would be required to have additional collateral and their interest rate is set higher. This is an additional burden to UMzimkhulu SMMEs. A study by (Barbosa and Maraes, 2004) found that interest rate charged by banks for new enterprises are higher than old and

large enterprises. Also Harrington (2010) claims that it is common all over the world that SMMEs have less access to funding than large enterprises.

All the respondents pointed to obstacles in their way to getting funding from the banks and many have not had any kind of a relationship with banks before. The South African laws, prior to the 1994, prevented access to banking for the majority of its citizens and after apartheid still many could not afford exorbitant bank charges levied to manage accounts. That is why many of the previously disadvantaged communities did not open bank accounts due to the reasons already outlined but in addition one of the reasons was the requirements for opening the account itself. The previously disadvantaged SMMEs have historically been undermined in the accumulation of traditional resources (Falkena et al., 2004). As Cornelius (2009) stated, people used a form of saving similar to credit unions called stokvels as the *National Credit Act of 2005* allowed voluntary associations.

The reasons stated by the SMMEs which prevented most of them from accessing funding were not just that funding was not available and their business were not viable. It was the lack of assistance to help them get skills to be able to express their ideas in the form of a funder's acceptable business plan format. The preconceived assumption that the SMME businesses were high risk also contributed to stringent requirements from SMMEs.

#### **4.5 Business regulations and legislation**

In this section the regulations and legislations both from the past and current history are highlighted as being part of a challenge in SMME access to finance.

Respondents were asked about the source of funding they used to start their businesses. One common thing that the researcher noted from ten respondents R2(14/11/2013), R5(18/11/2013), R6(19/11/2013), R7(20/11/2013), R10(26/11/2013), R11(26/11/2013), R12(27/11/2013), R13(28/11/2013), R14(29/11/2013) and R15(02/12/2013) is that they cited the regulations and legislations which govern business as another reason that discouraged them from sourcing funding. The feeling was that the collateral regulations and the business registration laws were daunting. As stated by Magistea (2010) the world bank survey of 2008 cited that the rate of registered businesses rejected for funding were less than that of unregistered businesses. Other laws cited were laws governing the debt

recovery and the credit bureau and administration of justice. All of these were cited as areas needing to be made simpler. The laws mentioned also included the *Usury Act* which limits the scope of lending on the part of businesses (Magistea, 2010).

On the subject of business registration, all the respondents felt that it is difficult for the rural SMMEs as there are no institutions in UMzimkhulu that assist in business registration. They are sited in big cities. They also stated that even if they go to those cities, the registering agencies still forward the registration to a central registration body based in Pretoria for the whole of South Africa. R15(02/12/2013) stated that “we are delayed by the CIPC, a central registration body, to get registration documents required in order to apply for funding as per regulations”.

All respondents except four felt that the legislation governing the debt recovery was another barrier in getting loans from the banks and other funding institutions. They cited the credit bureau as being a big problem because they keep records even after one has fully paid the debt and, as a result, the applications for funding get rejected. The way the banks operate is such that it is not negotiable. The applicant must have a clear record with the credit bureau. Should there be a judgement they require a letter or written report from the judgement creditor stating that the debt has been settled. These respondents were thus of the view that it's very difficult in their geographic location to be able to meet all these legal requirements. The reason cited being that there are no institutions that can assist them within the town and district. This is a problem they see specifically from the rural and previously disadvantaged groups in assessing finance. As stated by R1 (13/11/2013), R4 (15/11/2013) and R7 (20/11/2013) “all the institutions that assist with getting documents required by funders are based in big cities and we have to commute for long distances”. This is also seen to be related to historical imbalances setting up limits in their capacity to function in a rigorous global business environment. Falkena (2004) also mentioned the lack of credit record or history as being a disadvantaging element in accessing funding in the early stages of the enterprise.

#### **4.6 Lack of information and technology**

In this section the points on lack of information and technology as a barrier to SMME access to funding and other resources were looked at as one of the issues that came up in responses to the interviews.

According to the majority of respondents R4(15/11/2013), R6(19/11/2013), R7(20/11/2013), R9(25/11/2013), R10(26/11/2013), R11(26/11/2013), R12(27/11/2013), R14(29/11/2013) and R15(02/12/2013) when they were asked about their knowledge of other funding from government and NGOs they were not aware where and how that kind of assistance is accessed. They seem to have heard about funds provided by government for business and projects from the media however these are based in big cities far away from the rural areas like UMzimkhulu.

Chimucheka and Rugan (2001) and the World Bank (2007) study on barriers to accessing loans revealed the unwillingness of the banking sector to lend to SMMEs due to poor business plans and lack of tangible collateral. These being the case the SMMEs are not aware that Khula is delegated by DTI to provide guarantees for entrepreneurs with viable business plans but who are unable to meet the requirements of a collateral guarantee. The researcher as a government official is also not aware how this Khula scheme can be accessed. This shows that the SMMEs were not lacking initiative when they said they were not aware of the government schemes designed for their assistance.

This lack of information can be seen as two-fold. One because of the inability of those who are offering the services to market their services to the target groups. The DTI, Khula Department of Economic Development in national and provincial level have all failed the SMMEs especially in rural and previously disadvantaged groups by not being there to assist when they were seeking funding. They did not make themselves known or created means whereby the banks can refer those SMMEs to available support schemes if the unfulfilled criteria for accessing funding be lack of collateral. Secondly, the lack of information can also be seen as being the result of geographic and historical dimensions (Kesper, 2001). The geographically uneven distribution of the funding supporting institutions affects access for SMMEs in the rural areas like the one under study. The majority of the respondents also cited the lack of well-developed infrastructure. This

includes the information and technology infrastructure as a barrier of not being able to access information as some of these notices and documents require internet access. Some of the areas still do not have electricity connections while the national provider ESKOM still has capacity problems. They say rural SMMEs are the ones who suffer the most. Lack of electricity has a ripple effect on other infrastructure like telecommunication and broadband access. In UMzikhulu there are areas where the broadband is still not available people cannot use cell phones or internet and Telkom is dysfunctional. R6 (19/11/2013), R12(27/11/2013) and R15(02/12/2013) indicated that they do not have access to newspapers and daily they rely on radio as a means of communication. Most respondents also complained that government departments also use the lack of infrastructure as being the reasons for them not to have offices to offer the required services to the SMMEs. Hence the lack of information about the various government funding schemes available for the SMMEs.

From the information provided by the respondents above it is clear that they are still having challenges of lack of information and technology. These result in SMMEs struggling to access information thus deprived them of funding opportunities.

#### **4.7 Access to information and advice**

This section will deal with challenges for SMMEs posed by lack of access to information and advice for accessing funding and non-funding support. This was as a response to a question that was asked about the information about funding availability.

The respondents cited that they don't get enough information about funding available both from banks and government. As one respondent stated:

“ when I applied for the jobs fund I was told the forms are available on line and I tried to fill them and I had to phone an office in Pretoria where the lady who was supposed to help me was always not available and I ended up getting late for submission.” R11(26/11/2013). What was noted by the researcher from the response was that the SMMEs lacked information and advice when it comes to requirements for applying for funding and available business support available for financial assistance.

Due to imbalances of the past, the problem of information and advice is severe amongst the previously disadvantaged especially the blacks who are found predominantly in rural areas. There were attempts by the democratic government after 1994 to try and make information available and is establishing relevant agencies for dissemination of information. Relevant information and advice however to date has reached very few SMMEs especially in rural and township areas. This is supported by information from the respondents from the interviewees who indicated that they do not have knowledge of other supporting institutions who offer either financial or non-financial assistance R2(14/11/2013), R5(18/11/2013), R6(19/11/2013), R9(25/11/2013), R10(26/11/2013), R12(27/11/2013), R13(28/11/2013) and R15(02/12/2013).

Eleven respondents out of fifteen have never had contact with any supporting institution. Five respondents indicated that they had never heard about the funding support programmes available from government. These respondents said people who are working in these programmes need to come to the rural areas to inform them about the funding support programmes available.

The responses of the SMMEs above indicated clearly the challenge in accessing information and advice. There was also a suggestion by the SMMEs that the institutions that provide support and advice should come to the rural areas to provide support and advice to the rural SMMEs. One respondent R9 (25/11/2013) said; “The government must also bring the offices to us in rural towns so that we can get help near our homes”. This shows a feeling by most SMMEs that the government should ensure that agencies are decentralised and that they should come to rural towns.

#### **4.8 Lack of training in entrepreneurship and management skills**

This section looks at the suggested advice from the respondents that they felt they could give to new SMMEs entering business as one of the questions that they were asked. The issues of skills capacity in business management and financial management and planning are highlighted as barriers towards access to financial assistance.

The acquisition of the business management and planning skills, financial management skills and basic business skills are generally regarded as one of the critical basic business

skills in order for SMMEs to succeed R3(15/11/2013). When SMMEs are asked what advice they would give to other people intending to venture into business, most of the responders indicated that they would advise that they have adequate funding for running their business. The reason they gave was that if the Small enterprise owner does not have enough funds it is not easy to get financial assistance from banks or government. As stated by Strause (2006) the government should assist SMMEs with skills to meet funding criteria of funders.

Another respondent suggested that over and above having money they would advise prospective SMMEs to get necessary vocational technical and business skills training because they are essential for success in small enterprises.

“it is important to have the necessary critical skills required in running a business as a rural previously disadvantaged community our literacy level is low and we have a challenge as the language used in filling forms is English and the forms use terms like business profile and financial statements R8(22/11/2013)”. From these responses it is clear that the lack in these skills contributes to the inability of SMMEs to access funding that is available from the banks and other funding institutions and agencies.

The section above highlighted some of the suggestions and advice that the SMMEs would give to prospective enterprise owners. Here are some of the responses to a question regarding the source of funding for the participants businesses. Here the skill of managing finance came up as an important element in success of a business and in the ability to attract more funding:

Some respondents R 2(14/11/2013), R5(18/11/2013), R6(19/11/2013), R9(25/11/2013), R10(26/11/2013), R12(27/11/2013), R13(28/11/2013), R14(29/11/2013) and R15(02/12/2013) said that they started their businesses with their own savings which they had while working and money they were paid when they left work. These respondents indicated that the savings they had was not enough to start their intended businesses which is why they approached the family members and close friends for further financial assistance. This response is similar to a statement by Magistea (2010) that it is common amongst SMMEs to depend on their own funds or family and friends' funds as they find it difficult to access bank credit and supplier credit.



“When I applied for funding they refused because I did not have any proof of training in business management and the business I wanted to start and I started with my own savings without a building and office but after seven months the CEO of one of the companies that refused to fund me flew from Johannesburg to offer me funding because of the money I was making without a revised business plan”R3(15/11/2013).

This was a proof that funders look for management of financial skills as stated by Shane and Stuart (2002) that banks believe that the higher the managerial level of owners the greater will be the viability and survival rate of the SMME and that it will be successful. The funders are more likely to give credit if the SMME has the above characteristics.

When asked whether they know about other sources of funding most respondents indicated that they do have a little knowledge however those institutions want people who have vast knowledge and experience in business and financial management. The respondents further stated the reason for this as that those funders want business books and records of finance over a period of time, at least a year.

Most of the respondents indicated that when they started their businesses they did not have knowledge of organising matters of business finance and formalised financial management which was a disadvantage for them.

There were only three respondents who had some limited skill of keeping records because their family operated a business and they were assisting in the running of the family business. Two of them indicated that they had done subjects in business economics while at school but they had not formally managed their finances as they were starting up and using their own funds.

From the above responses the researcher concluded that the financial management skills were an impediment to SMMEs accessing funding if they lacked these skills. Also those respondents who had applied for funding indicated that some of the requirements indicated by the funders did require some information on the business financials and it was clear that the absence of this information would impact on the decision to fund or not to fund a business.

One respondent argued: “As most of the SMMEs of UMzimkhulu are from the previously disadvantaged groups there is a need for the financing sector to offer us some basic training in financial management. This will assist them to access the already available funding for us Small business provided by the government in order to redress the imbalances of the period before 1994” R5(18/11/2013).

It is important that the rural SMMEs are also empowered in these skills as those in urban areas through the agencies like SEDA provided by government (DTI, 2005)

This above discussion shows how the SMMEs feel about the need for a person in business to have the skills in business management and financial management. These skills are not only necessary for managing a business however they assist the SMME to be successful in operating the business and to attract more needed funding to grow the business. The other important advice given by SMMEs here is that if there is a strong business idea one should not rely only on funding from government or private institutions but use one’s own savings as well as those of close friends or family. Lack of business and financial management skills can contribute to a business not accessing the funding from the different funding sources.

#### **4.9 Required collateral security**

This theme deals with collateral security and is related to commercial banks requirements. The respondents indicated their views and experiences with regards to required collateral security.

The five respondents from those who said they have approached the banks revealed that lack of tangible collateral is a problem for them in obtaining funding from commercial banks. When their credit assessment is done the banks tend to look at larger well-developed businesses who manage to get better credit facilities due to strong financial muscle in the form of security. “We are from a rural tribal authority areas and we have good built houses on our land however we do not have title deeds which we can present to the banks as part of our security” R1(13/11/2013), 4(15/11/2013), R7 and R8(22/11/2013).

One respondent stated that the developed business when they submit business concepts they are approved for funding even without the strong viable plan that is required of them.

Banks are focusing more on what they will make in terms of interest in returns R 9(25/11/2013). It is therefore clear that there is a need to have a special funding body or a bank that will cater solely for the small business financial needs. This bank should assist in business start-up, business expansion and working capital R11(26/11/2013).

This response indicated a need for an intervention to address the funding of this sector especially start-ups in rural areas and townships where the previously disadvantaged SMMEs come from. However the banks are profit-making entities and they cannot be forced to use credit guarantee schemes they can only do it on goodwill. The banks evaluation focuses on profitability of their selection and they usually do not offer incentives to unknown clientele.

There are some issues that were identified as gaps in the distribution of information to the SMMEs. The government through the DTI has made funding available for the SMME sector however this is not known to rural SMMEs like those in UMzimkhulu. This is true even when you look for the offices of these agencies and departments they are operating from the big cities and do not have visibility in rural areas. Therefore there is a need to targeted marketing and communication efforts aimed at creating awareness of these schemes and products. These should focus on marketing these schemes starting with those of capacity building directed to the SMMEs especially black and historically disadvantaged segments. They should assist in skills like business management skills, financial control, business tax and business regulations.

In this section the SMMEs felt they were disadvantaged in getting funding because of the required collateral which they did not have as rural SMMEs. The funders require a tangible collateral the rural SMMEs in communal land do not have title deeds but a letter of occupation which is not recognised by funders. There is a strong feeling about a need for funding structure to address the rural SMMEs without a collateral. Some of government available funding must be ring-fenced for rural SMMEs and the private sector can do it as goodwill. These initiatives should be marketed to rural SMMEs as they are at a disadvantage.

#### **4.10. Summary of Chapter Four.**

This chapter presented data analyses and findings of this research whose aim was to investigate whether or not the SMMEs access funding. It also looked at the challenges experienced in this regard by SMMEs in the UMzimkhulu Municipality. In this chapter themes were identified which emerged from the data collected and the literature. Various trends have emerged from the above analyses and discussions. Small medium micro enterprises (SMMEs) have a problem in accessing finance. This is seen as the major challenge hindering their development and success. A majority of Respondents indicated that financiers and funders are, to a certain extent, failing the SMMEs by not providing the assistance that is needed for sustainable participation in the economy. They further cited a number of challenges one of which is funding that prevents them to be sustainable and to participate in the Local Economy of UMzimkhulu and South Africa as a whole. The majority of the respondents also indicated that they were discouraged to apply for funding because of the challenges encountered by their counterparts in the process of accessing funding.

The results of the study indicated that there are challenges faced by SMMEs when it comes to accessing funding. Some of these challenges are situated within the SMMEs themselves while others are external and relate to funders and other supporting institutions created to assist the SMME development. The study also indicated that there was a general lack of awareness regarding the entire funding linked to the government policy of SMME development in some of the banks, agencies and NGOs. The hardest hit SMMEs are those operating at the low economic areas as they need start-ups and business expansion, bridging and working capital finance. There is a need for the business organisations, government departments & Development finance institutions (DFIs) to come up with strategies and proposals to improve the situation. There is also a need to revisit evaluation criteria's so that they do not lack consideration of diversity in their approach to SMMEs. While the banks are said to have funding targeted to Black SMMEs financing as transformation strategy they still needed a more substantial footprint in the rural areas like UMzimkhulu as the study shows how difficult it is for the rural SMMEs to access funding.

Only a small proportion of SMMEs were courageous enough, despite the challenges, to attempt accessing finance from banking financiers. Out of that small proportion also the

majority of them were unsuccessful in obtaining the funding. They could not approach government and the state agencies for SMME development as they were nowhere to be found due to the rural location of UMzimkhulu where these SMMEs are located.

It can be concluded that the findings of this study answer the key research question. SMMEs in rural towns like UMzimkhulu are unable to access funding because of their rural nature which makes them far from available help. The funding institutions need compliance documents which the SMMEs do not have skills to develop. The research also suggested interventions that can be implemented to overcome the challenges faced by the SMMEs in accessing funding. The fact that the majority of the SMMEs businesses are sustainable after having used funding either from their own savings, or from family and friends means that their business cases were viable and sustainable. It shows that they only lacked information and skills which could have been made available if relevant role players were available and effective.

The next chapter focuses on the recommendations both short term and long term. This chapter is aimed at reflecting the extent to which the research objectives and questions were answered and highlighting limitations from the study and provide recommendations for further research.

## CHAPTER FIVE

### CONCLUSION AND RECOMMENDATIONS

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#### 5.1 Introduction

This chapter presents the short to long-term recommendations and conclusions that arise from this study. The aim of this Study was to investigate whether or not the SMMEs access funding and considered the challenges experienced in this regard by SMMEs in the UMzimkhulu Municipality. The research aimed to find out if the SMMEs do access the funding from different funding institutions and what the challenges are that they face in accessing funding. This research is hoping to contribute to raising awareness of the funding needs of the entrepreneurs in rural areas like UMzimkhulu Municipality.

The research recommendations in this chapter may contribute to future government policies. The Government has a role as stated in its policy objective to ensure that they make markets work for the SMMEs. To achieve this they have to make it possible that SMMEs acquire knowledge and leverage capital resources. There is a hope that the research will also contribute to addressing the social imbalances of the past by having funding categorised according to the funding requirements of the SMMEs such as start-up infrastructure for investment, capital for operational costs, a growth fund for business expansion and for those that need funds for unexpected opportunities that need urgent funding.

Since the social systems are socially constructed the researcher conducted the research with the knowledge that he himself, as an individual, can change the system by contributing in the form of research. As Ryan (2003) states social constructs can be changed by activities of individuals placed in a specific social context. In that way the researcher sees himself as a part of the hoped-for change.

## **5.2 Short term recommendations**

### **5.2.1 Challenges with the banking sector**

One of the deterrents for the SMMEs to approach the banking sector and some funding institutions was the fear of the inability to produce the so-called viable business plans especially the new start-up SMMEs. Their fear was due to the lack of skill to develop a business plan let alone a viable one. The researcher views Banks' requirements for viable business plans as limiting to rural SMMEs like UMzinkhulu. Most applications get rejected as a risk minimisation on the part of the banking sector and not too many of the SMMEs' applications are viable in design. It is therefore recommended that the SMMEs should be assisted by the funding institutions in developing the right skills for the compilation of the business plans or provided with professional assistance where they can be assisted to draft the business plans. Another recommendation is for the government institutions created for supporting SMMEs with financial aid to also have programmes in place where they can provide training in business plan development. This will help in creating confidence among the new entrepreneurs who want funding for start-ups and who wish to apply to the various institutions.

Those whose applications were not successful felt that the reasons for their rejection were not given. The respondents who were rejected felt it would have helped them if the reasons were clearly stated to correct those weak areas in their proposals. The unsuccessful applicants view was that they would have benefitted from the assistance from experts found in the urban towns and cities who understood the lending sector. The uncertainty created by lack of feedback from applications resulted in those who were unsuccessful informing those who still want to apply for funding that it not possible to access funding. It is therefore recommended that the applicants are given feedback so that they know where they have not supplied the required information or given reasons why they did not qualify for funding.

Having had a look at the interview results, the data trends to indicate that substantial effort needs to be focused on SMMEs especially in rural and previously disadvantaged areas by offering assistance programmes in business management and administration. The SMMEs

when they start their businesses do not have a formalised way of keeping their financial books and when they want to expand their business these records are needed. The lack of financial records and not having the financial statement for the previous year's results in failure of SMMEs to prove the viability of their businesses. It is therefore necessary to develop these skills among the SMMEs if they are to succeed in accessing funding.

### 5.2.2 Resolution on managerial skills and strategic planning

The shortage of skills in business management, finance and strategic planning contribute to high number of SMMEs not accessing funding. Entrepreneurs go into business because they have a big business idea which they have researched so that it can be sustainable however when it comes to procedures and processes of the funders they are not well informed. As one of the respondents related his story when he tried five companies for funding his petrol filling station business when he started and was refused he eventually managed to use his own savings and a loan from his family. After four months he was already doing well but did not have buildings for an office. After seven months the CEO of a company that refused funding flew from Johannesburg to give him funding to build an office and other buildings without a revised business plan.

A recommendation is for the establishment of a mentorship programme for business start-ups. The mentorship programme should not use a blanket approach as SMMEs' needs vary. There is a need to conduct a basic skills audit before embarking on the mentorship so that the SMME are provided with skills they do not have or are lacking. The mentorship programme will best be suited for the strategic planning and a few managerial skills.

When it comes to business management and finance a generic programme can be used for both start-ups and those already in business. The recommendation is that this should be a long-term approach. The skills development offered should be developmental taking into account the SMME different levels of need.

### 5.2.3 Resolution on access to finance

Lack of access to funding for the SMME especially in their early stages of growth is often a huge handicap for their development. The majority of the respondents interviewed in



UMzimkhulu relied only on their personal funding resources such as their own funds and loans from friends and family to start the enterprises. The South African government put in place initiatives to try and help the SMMEs where possible through finance, training and other forms of support by using the government departments, parastatals and agencies. This assistance seems to lack marketing and monitoring as in some areas in the country like UMzimkhulu they are not known. Their offices are only in big cities. They either help those who are already developed or they help those who can afford to come to the big cities.

Research results indicated that the requirement of a viable sophisticated business plan from SMMEs does not guarantee a business to get funding. The SMME owners felt that money that is paid for the development of a business plan which was unsuccessful to get funding is a waste of money that they need to develop the business. This is because to develop such business plans they require the services of consultants who are paid a huge amount of money irrespective of whether they get the funding or not. In this respect it is recommended that a regulation be drafted with clearly defined objectives for internal processes and customer relations within the financial assistance schemes. The funders also need to have motivated consultants and leadership in the institutions that have expertise in and understanding of the end-user needs. The institutions need to be innovative by using an integrated approach for both financial and non-financial support. There should be a way of ensuring commitment from the commercial banking institutions to help SMMEs with meeting qualifying criteria before the assessment of applications.

The DTI has sector programmes however they need to have SMMEs sector-focused programmes which must be marketed specifically to this sector. To promote these programmes DTI needs to come up with a SMME targeted sector-marketing strategy with the aim of communicating the programmes, monitoring and evaluating the programmes to improve the accessing of funding by SMMEs.

#### 5.2.4 Resolution on Lack of Knowledge about funding available

Lack of knowledge about funding was identified in the research as being caused by failure of the institutions to market the incentives and the centralisation of the funding institutions in big cities. A recommendation in this regard is for the marketing of SMME funding

programmes from DTI, commercial banks and other agencies to target the non-urban market. It is also recommended that these funding institutions be localised so that they can focus on localities which they service especially in rural communities and previously disadvantaged communities.

#### 5.2.5 Access to banking services

The problem of SMMEs not being able to access funding cannot be separated from the problem of individual access to banking services. Banks in South Africa have a tendency not to have branches in rural areas and townships as they say they do not want to operate unprofitable branches. However they have realised that there is market in black townships and they are opening branches there. In chapter two literature review it was mentioned that the level of access to banking services was very low amongst the previously disadvantaged groups due to the social conditions they were subjected to. The other reason mentioned was the costs associated with banking services.

The majority of the funding institutions require the financial statement for a minimum of three months which can only be provided by a person or business that has access to banking services. That is why the issue of access to banking services of individuals cannot be separated from SMMEs access to finance.

It is not only the banks that offer debt finance to SMMEs but a number of other intermediations and agencies; they offer debt finance in the name of the SMME owners. Most of them include financial statements as part of the evaluation criteria. To rural people and previously disadvantaged groups this requirement is an obstacle as most do not have a long-term history of using banking services especially for the start-up businesses.

It is recommended that some form of incentives be created to create credit scoring for SMMEs who do not have a long-term history of using banking services. This is necessary for as long as the scoring system rely on credit performance and financial history the SMMEs will not be able to access funding especially those in rural areas. The system gives strong preference to long- term clients of the banking sector at the expense of the start-ups. It is recommended that banks consider lower levels of bank charges for basic financial services such as money transmission. It is also recommended that the Government promote

and encourage the development of co-operative banks and community banks with low entry requirements since the current requirements for entering a banking system are too steep for new entrants. These banks can assist the rural communities and SMMEs first to access banking services cheaper and offer funding at a competitive rate.

### **5.3 Medium and long-term recommendations**

Here the long-term and short-term recommendations will be discussed as prompted by the data collected from interviews. The respondents pointed to lack of awareness of the available financial and non-financial support available for SMMEs. They also pointed to the one-size-fits-all approach of the lending criteria used by the funding institutions and suggested diversified criteria which would be suitable to the SMMEs. There was also a strong view on the establishment of a legislation to cater for the SMME support in rural and disadvantaged SMMEs. These recommendations can be implemented on a long-term as well as a short-term basis depending on the logistics needed before they can be put into use.

#### **5.3.1 Medium term recommendations**

The results indicated that there is a lack or very low level of awareness when it comes to the alternative financial and non-financial support available from various government agencies including NGOs. This indicates that there is some work which needs to be done to improve the level of environmental awareness. The SMMEs operate in a particular environment and they therefore need to understand the business environment issues so that their operations are designed to meet the demands of the environment and also benefit from it.

It is therefore recommended that an environment be created in which SMMEs may prosper in the long-term without being dependent on government support. This can be done firstly by promotion of a dynamic and efficient SMME sector. There is a need to transform the SMMEs so that they can meet challenges of the marketplace (Kayanila and Quatey, 2000). There is a need for capacity development which need to be monitored and measured through benefits received and success of the SMME beneficiaries. The DTI should ensure that it brings their capacity development programmes closer to the rural SMMEs so that the

SMMEs can access them. The DTI should also fill the gap of a need business angels by establishing business angels which will mentor the entrepreneurs. There is a need to do a research on the incentives that can be offered to these Business Angels. Government should devise financial policies to encouraged big business to offer support to SMMEs as part of their corporate social responsibility commitments.

There is a need to introduce and promote subsidized credit and for this to be marketed to SMMEs. The government should also make legislation ensuring that the commercial banks make available a stipulated portion of their portfolio to the SMMEs. There should be some form of differentiation made in the interest rate charged to SMMEs and to large businesses as the SMMEs find it difficult to compete against large business due to high cost of borrowing which ends up putting a burden on their resources. This can be done by introducing a fixed interest rate for SMMEs which is not affected by the hike in interest rate. These reforms can go a long way to creating better opportunities for the SMMEs to access funding for both star-ups and business expansion.

### 5.3.2 Long-term recommendations

These refer to government and legislation that can have an impact on delivery programmes in the finance sector that can unlock access to funding. These can include but not limited to financial and non-financial support biased ton the previously disadvantaged communities. The legislative framework that exists seems to be a good product however they seem to be borrowed from overseas experiences and as such they overlook the relevance to the South African situation. There is a need to develop frameworks tailored for South African consumption so that they can be effective. Legislation is needed that will ensure that the commercial banks revise their lending criteria to SMMEs appropriate for a developing economy. There is a need to look at establishing a bank that will specialise in SMMEs controlled by government with SMME-friendly policies and procedures. The bank should have a mix of staff from both government agencies and commercial banks. Government should offer incentives in the form of tax rebates to attract capital from private sector sources such as venture capital.

Another area which must be investigated for feasibility is the legislation for the establishment of different kinds of banking institutions including co-operative banks,

village banks, micro lenders or some other form of a financial institution. This bank will have as its mandate to look at lowering the capital and compliance costs and thus being a financial institution appropriate for creation of emerging market environment for SMMEs. There should be a regulatory authority established for such institutions in order to enhance the credibility of these institutions. These recommendations are made with a belief that they will contribute to increased opportunities for SMMEs to access funding. There is also a belief that they will develop innovation in the financial servicing sector and also increase competition in the financial services sector. To implement these recommendations there is a need for greater co-operation amongst various government departments, financing agencies and regulatory agencies so that progress can be monitored and evaluated.

#### **5.4 Conclusion**

The research recommendations in this chapter will hopefully contribute to future policies as Government has a role in its objective policies to ensure that they make markets work for the SMMEs by making it possible that they acquire knowledge and can leverage capital resources. The importance of SMMEs as a sector cannot be overemphasised as one of the wealth creators however the contribution in wealth creation depends on the support they receive to develop and grow their businesses. The support in the form of funding and acquisition of knowledge is fundamental to SMME sustainability especially in rural areas and previously disadvantaged communities like UMzimkhulu. The government has however since 1994 come up with policies, regulations and strategies to enable the development and growth of SMMEs which has to date not reached the intended recipients in rural regions of UMzimkhulu.

The aim of this research has been to establish the challenges faced by the SMMEs in accessing funding in rural areas with particular reference to UMzimkhulu. Thus the challenges were identified which pointed to the internal constraints within the SMMEs themselves and external constraints on the part of funding institutions. These were the lack of knowledge of the available funding institutions, complexity of the criteria used by the banking institutions as well as the lack of the SMME business management and entrepreneurial skills.

This knowledge about the challenges experienced by the SMMEs can assist in providing valuable information for both policy makers and funding institutions in the government and private sectors. This will assist stakeholders in SMME development and like government departments, its agencies and the private sector to formulate and develop policies, strategies and programmes to assist SMMEs access funding to start and develop their businesses. The recommendations are useful also for rural areas like UMzimkhulu and funding institutions to unlock the challenges so that SMMEs can have knowledge of support and access to the funding they require.

As previously cited that SMMEs are wealth creators and job creators and they rightfully deserve to be given the support that will help them to contribute to the economy of UMzimkhulu and the country as a whole.

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## APPENDIX A: INFORMED CONSENT LETTER

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UNIVERSITY OF KWAZULU-NATAL  
GRADUATE SCHOOL OF BUSINESS AND LEADERSHIP

MComm Research Project  
Researcher: Christopher Robert Thulani Cele (082 4108477)  
Supervisor: Dr. Jennifer Houghton (031 260 7429)  
Research Office: Ms P Ximba 031-2603587

Dear Respondent,

I, Christopher Robert Thulani Cele am a Masters of Commerce in Leadership Studies student, at the Graduate School of Business and Leadership, of the University of KwaZulu-Natal. You are invited to participate in a research project entitled: **SMME Access to Funding -Challenges Experienced by SMMEs in UMzimkhulu Municipality**. The aim of this study is to gather the information with regards to access to funding towards the development of SMMEs with particular reference to UMzimkhulu and problems that would be eased through investment.

Through your participation I hope to understand the problems experienced in finding funding assistance as well as assistance that you received in starting or developing your business.

Your participation in this project is voluntary. You may refuse to participate or withdraw from the project at any time with no negative consequence. There will be no monetary gain from participating in this survey. Confidentiality and anonymity of records identifying you as a participant will be maintained by the Graduate School of Business and Leadership, UKZN.

If you have any questions or concerns about completing the questionnaire or participating in the interview or focus group or about participating in this study, you may contact me or my supervisor at the numbers listed above.

The interview or focus group should take about 45 minutes to an hour. I hope you will take the time to participate in the interview

Sincerely

Investigator's signature \_\_\_\_\_ Date \_\_\_\_\_

This page is to be retained by the participant

UNIVERSITY OF KWAZULU-NATAL  
GRADUATE SCHOOL OF BUSINESS AND LEADERSHIP

Master of Commerce Research Project  
Researcher: Christopher Robert Thulani Cele (082 4108477)  
Supervisor: Dr. Jennifer Houghton (031 260 7429)  
Research Office: Ms P Ximba 031-2603587

CONSENT

I ..... (full names of participant) hereby confirm that I understand the contents of this document and the nature of the research project, and I consent to participating in the research project.

I understand that I am at liberty to withdraw from the project at any time, should I so desire.

I hereby consent/do not consent to audio tape recording of the interview.

SIGNATURE OF PARTICIPANT

DATE

.....

This page is to be retained by the researcher

**APPENDIX B: INTERVIEW QUESTIONS**

---

**University of KwaZulu-Natal  
Graduate School of Business and Leadership  
Westville Campus**

**Title of Research:**

**SMMME ACCESS TO FUNDING -CHALLENGES EXPERIENCED BY SMMES IN  
UMZIMKHULU MUNICIPALITY**

Date of interview:

Name of interviewee:

Name of business:

**A: SMME BACKGROUND**

Q1. What products/services are the business offering?

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Q2. How long has the business been operating?

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Q3. Could you briefly describe when and how the business was started?

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**B: CURRENT FUNDING ENVIRONMENT**

Q4. Please explain where you got money to start your business and how long did it take?

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Q5. Explain the financial challenges you had when establishing the business and how you overcome them?

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Q6. Name a few funding institutions that you approached and explain how they responded?

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Q7. Briefly explain the importance of funding and how you feel funding contributed to your business?

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C: INFORMATION ABOUT FUNDING

Q8. How were you informed about the available funding?

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Q9. What types of funding do you know and do you think other SMMEs know about this funding?

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Q10. If you were to start afresh how would you go about in requesting funding?

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D: CHALLENGES IN FUNDING

Q11. How did you apply for the funding give a step-by-step account of the process?

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Q12. What are the challenges you encountered when applying for funding?

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Q13. Why do you think some SMMEs are not getting funded?

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Q14. What advice would you give someone who wants to apply for funding?

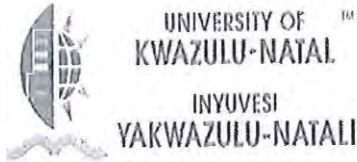
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## APPENDIX C: ETHICAL CLEARANCE APPROVAL

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08 November 2013

Mr Christopher T Cele (212561594)  
Graduate School of Business & Leadership  
Westville Campus

Protocol reference number: HSS/1154/013M  
Project title: SMMME Access to Funding – Challenges experiences by SMMES in Umzimkhulu Municipality

Dear Mr Cele,


**Expedited Approval**

I wish to inform you that your application has been granted Full Approval.

Any alteration/s to the approved research protocol i.e. Questionnaire/Interview Schedule, Informed Consent Form, Title of the Project, Location of the Study, Research Approach and Methods must be reviewed and approved through the amendment/modification prior to its implementation. In case you have further queries, please quote the above reference number. Please note: Research data should be securely stored in the discipline/department for a period of 5 years.

I take this opportunity of wishing you everything of the best with your study.

Yours faithfully

  
.....  
Dr Shonuka Singh (Acting Chair)

/ms

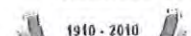
cc Supervisor: Dr Stan Hardman  
cc Academic Leader Research: Dr E Munapo  
cc School Administrator: Ms Wendy Clarke

---

Humanities & Social Sciences Research Ethics Committee  
Dr Shonuka Singh (Acting Chair)

Westville Campus, Govan Mbeki Building  
Postal Address: Private Bag X54001, Durban 4000

Telephone: +27 (0) 31 260 3587/8350/4557 Facsimile: +27 (0) 31 260 4600 Email: [ximbap@ukzn.ac.za](mailto:ximbap@ukzn.ac.za) / [snymann@ukzn.ac.za](mailto:snymann@ukzn.ac.za) / [mohunn@ukzn.ac.za](mailto:mohunn@ukzn.ac.za)  
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