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Preference in Sourcing Business Financing in Maiduguri Metropolis: Evaluation of the Differences among Micro, Small and Medium Enterprises (MSMEs)

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ABSTRACT

Business financing is one of the major areas of concern to potential and established business owners. Small businesses in particular, face many challenges in making choices on which source of finance could be used the study, therefore, evaluates the differences in preference among small businesses in Maiduguri metropolis with regards to sources of generating finance. Data were collected through the administration of a structured questionnaire to small business owners where a sample of 310 respondents were drawn using Krejcie and Morgan small sample technique from a population of 1595 registered small businesses in Maiduguri. The finding of the study shows that among the four sources of finance utilized in the study only personal savings varies significantly among entrepreneurs of small business other three sources of business financing loan from friends and relatives, loan from non-bank financial institutions and loan from banks vary insignificantly among entrepreneurs. Based on the findings the study recommends that government should encourage small business owners by providing soft loans with low-interest charges so that they can be motivated and adopt it to expand their business instead of relying mostly on personal savings where expansion is minimal or difficult.

Keywords: Business finance, Maiduguri, Micro, Small and Medium Enterprises.

1. INTRODUCTION

Micro, small and medium enterprises MSMEs in various countries are being classified differently based on the number of employees, turn over and total asset. In most cases, size provides the practical basis of classification. In countries such as the USA, Britain and Canada, small-scale businesses are defined in terms of annual turnover and number of employees. According to the European Commission (EC), small businesses are those employing less than 50 people and with total assets of not more than 13 million dollars, while micro businesses are those with less than 10 people as employees with annual sales not more than 3 million dollars. Similarly, the Asia Pacific Economic Cooperation (APEC) defines MSMEs as businesses with not up to 100 people as employees, where medium size employs between 20 and 99 people, a small enterprise employs between 5 and 19 and Micro less than 5 people as employees.

In Nigeria, before 2007 when SMEDAN was launched various institutions gave different definitions to MSMEs according to their perception of the concept. The National Policy on MSMEs in Nigeria (2007) provided a general classification of MSMEs where it identifies medium enterprise as businesses with 50 to 199 employees and total asset greater than 50 but less than 500 million. Consequently, small enterprises as those between 10 and 49 people as employees and 5 to less than 50 million naira as a total asset and micro businesses are businesses with less than 10 people with less than 5million naira as their total asset excluding lands and buildings.

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Finance serves as a life wire that motivates the start of an entrepreneurial venture. In business particularly, it is the first consideration before even the intent of establishing an entrepreneurial activity. The consideration of finance in the behaviour of an entrepreneur and the growth of the business is paramount and basic because non-availability of funds deter the drive towards an entrepreneurial activity. There are various sources of finance available to entrepreneurs as owners of business entities. Aminu (2012) identified sources of finance to include personal savings, loan from friends' relatives and close associates, trade credit, equipment loans and leasing, internally generated funds, ploughed back profit, loan from financial institutions, issuance of corporate securities, issue of debenture stock, instalment credits, other forms of borrowed finance and money lenders.

Similarly, Ayyagari, Demirguc-Kunt, and Maksimovic (2008) presented some of the sources as personal savings, a loan from friends and relations, banks, non-bank financial institutions, share venture capital, retained earnings hire and leasing, factoring among others. In this study, personal savings, loan from friends and relatives, loan from banks and non-bank financial institutions are the sources mostly employed by entrepreneurs in financing their businesses. The reason behind this selection was based on the fact that they are the most likely sources being employed by small businesses. Business financing is one of the most challenging areas of concern to business owners, particularly small businesses face so many challenges in financing their businesses.

This study extended the literature by evaluating the difference in preference among small businesses in Maiduguri metropolitan with regards to sources of generating finance. Four out of many available sources of finance were selected based on the fact that small businesses mostly utilize these sources in financing their businesses.

2. LITERATURE REVIEW

2.1 Theory of Finance, Entrepreneurship and Growth

King and Levine (1993) provided a highlight on this theory based on the work of previous scholars such as Goldsmith, (1969), Mc Kannon, (1973) and Shaw (1973). According to King and Levine (1993), these scholars were of the view that the financial market is based on the role they play on economic activities. They based their reasons on the quantity and quality of services provided by financial institutions as could in some extent give reasons why the rate of growth differs from country to country. Robinson (1972) as cited in King and Levine, viewed finance as essentially handmaiden to industries, how cross-country differs in their rate of growth is based on the response of other factors.

Robinson (1972) looked at how the financial system affects entrepreneurial activities positively in four ways. First, the financial system makes an evaluation of choosing promising projects. Second, mobilize fund for the finance required to meet up the promising project. Third, it allows diversification of risk that is associated with uncertainty of creating new ways of doing things in other words innovation, and fourth it spelt out the benefits of innovation and make necessary ways of making existing products with existing techniques.

The theory further explains how the choice of higher quality entrepreneurs, projects and source of financing required externally; and creating ways to manage the risk of innovation effectively. The study spelt out clearly that higher profit is associated with uncertain business innovation. When the objective mentioned above is achieved, it is believed that it would result to better financial system which could aid economic growth (King & Levine, 1993).

The theory established positive effect of finance on entrepreneurial activities by making funds available for the activities and by diversifying risk through innovative processes. The theory has also addressed how risk could be minimize through innovation, where both risk and innovation are major indicators of the entrepreneur's behaviour. Finance is a foundation of every business intent, and growth is what lies in the mind of every entrepreneur to achieve. Even though the theory did not address the issue of the relationship between these variables in question, this study expected that the findings would contribute to how the choice of source of finance strengthens or weaken the relationship. Considering this fact, therefore, the theory would go a long way in contributing to achieving the desired goal of this study.

2.2 Sources of Finance

Lee, Sameen and Cowling (2015) defined Sources of Finance as avenues for obtaining funds that come from outside an organization. Sail, (2006) viewed Sources of Finance as the various ways a company would choose in sourcing the required capital depending on the amount and period needed. Akinola (2013) defined the Sources of Finance as those sources that are short term and must be pay back within a year, and other sources that are long term and can be pay back over many years. From the foregoing definitions of sources of business funds, it could be understand that one central issue here is that fund is required at a different level and from different means to finance small businesses. Therefore, this study defines sources of finance as different ways of obtaining business fund depending on the perception of the entrepreneurs towards the available sources.

2.3 Preference of Sources of Finance among Entrepreneurs

Sources of finance discussed in this section using different opinions of researchers on sources of finance available for entrepreneurs to finance their businesses. It is therefore important to see what these studies suggest as sources of business finance. Ayyagari, Kunt and Maksimovic (2008), in a study, categorized sources of business funds based on period, source of generation and ownership where it was named period basis, ownership basis and source of generation basis. The scholars further suggest that the period basis can be further classified as long, medium and short-term sources, while ownership basis can be divided into the owner's funds and borrowed funds. Accordingly, the source of generation could be internally generated or externally generated. Delmar (1996) suggested that prior to the commencement of a business an entrepreneur needs to evaluate the cost of financing the business.

Secondly, an entrepreneur needs to consider available sources of fund and decide on the structure of the financing plan, i.e., how much money is available and how much to be borrowed from the available sources. Then the entrepreneur needs to prepare a technical report like opening balance sheets, profit and loss account and cash flow projected for 2 – 3 years and if necessary involve the help of a professional. While Ayyagari, Kunt and Maksimovic (2008) dealt with how funds are categorized based on period time and owners fund to help entrepreneurs with funding differences, Delmar looked at the strategies to be utilized by an entrepreneur to decide on how to source funds.

In a related study, Evbuomwan, Ikpi, Okoruwa, and Akinyosoye (2013) assessed sources of finance for MSMEs in Nigeria and found commercial bank's loan constituted over 90% of sources of funds to Micro Small and Medium Enterprises in Nigeria. There is an indication that their loans and advances to the agricultural and manufacturing sectors combined where most of the beneficiaries are the MSMEs. However, MSMEs operators still do not find enough funds for their activities as the analysis show that inadequate fund was the most mentioned problem.

Fraser, Bhaumik, and Wright (2013) opined that the aftermath of a financial crisis is a sluggish economic recovery. This is as a result of the decline in both debt, and equity finance flows to

SMEs even though the policymakers' assumed was that private sectors should have access to adequate finance. There is an indication that funding gap is created that is yet to be filled up and it is assumed that this problem would bring about a sluggish growth in the private sector; therefore, there is need to develop a policy that would target funding gaps to promote firm growth. An analysis is required of both the factors that affect funding and the nature of the relationship between funding gaps and business growth. Even though the factors were not clearly understood, the objective of the paper was to differentiate between issues that are well understood and issues that look at the relationship between economic variables, such as funding gap and firm growth that are difficult to understand.

The study also suggested that if a firm has collateral, it can have an increase in access to finance, but it happens only where there exists a steady relationship with banks. It also depends on if they can obtain trade credit from their business partners which also mean is more beneficial to existing firms that have goodwill on credit ratings. New firms would, therefore, find it difficult to access such funds given these peculiarities. Similarly, Oladele et al. (2014) examined the effects of financial sources on SMEs performance in Ado-Ekiti, to find out their performance based on the sources of finance they adopted have in one way or the other, a connection with the performance of the SMEs. The study reported a positive relationship between the sources of finance and business performance and indicates that the formal sources of business finance as the most significant variables that change SMEs performance in Ado- Ekiti. This implies that entrepreneurs that resort to the formal sources were performing very well than their counterparts that choose the informal sources in funding their businesses.

Dearman and Bell (2011) investigated factors that influence entrepreneurs' decision to prepare a business plan. The use of additional fund of debt or equity and the owner's attitude towards various funding options. It was found that factors such as required initial fund proportion and additional outside sources and self-assessment of financial knowledge influence the decision to prepare a formal business plan. Similarly, Moses and Adebisi (2013) examined the existence of Angels as a source of financial, human and social capital to overcome the challenges of funding for small businesses in Nigeria. The study found Angel financing as a suitable and alternate source of financing small business in Nigeria. There is a need for publicity for the activities of Angel venture network in supporting all government activities on small businesses.

Olajide, (2014) discussed the reasons and stages where entrepreneurs need funds. The first stage is where an entrepreneur decide to start a business. Funds are needed in some cases immediately the business commences, while some are required for day to day operations. The categories are fixed capital requirement and working capital requirement, where fixed capital requirements are needed for the purchase of fixed assets like machinery, land and building, while the working capital requirements are for the routine operation of the business. In case of sole proprietorship business, funds may be raised either from personal sources or borrowed from banks, friends and the likes; but in case of a company, it can be classified based on period, ownership and source of generating funds. Under the basis of ownership, they are further divided into a long, medium and short term of ownership, there are owners' funds, and borrowed funds and on generation, it constitutes internal and external sources.

Thus, Lee, Sameen and Cowling (2015), said for proprietorship business, funds could be sourced from personal savings and borrowing from friends. It further explained that finance is the lifeblood of any business, how it could be sourced can be from various sources where each source is being characterized by so many factors that would enable the entrepreneur to understand and chooses the best option that will suit the business. Though there is no single best source of business finance for all organizations, every source has its merits and demerits on shareholders. Retained earnings is being termed as a permanent source of funds available in an organization, and there is flexibility and freedom of operations since it is internally generated, but it could cause dissatisfaction to shareholders as they would get a lower dividend.

Similarly, Aminu (2012), outlined sources of finance as entrepreneur's personal savings, loan from friends, relatives and close associates, trade credit, equipment loan and leasing, internally generated funds, ploughed back profit, loan from financial institutions, issuance of corporate securities, issue of debenture stock, instalment credits, other forms of borrowed finance and money lenders. However, for an entrepreneur to venture into business, there is a need to identify how capital can be sourced considering various sources of finance available for the entrepreneurs. This sources could be based on the nature of the entrepreneur as a person, ability, scale of investment, the motive of investment and the appropriate time to get the funds. Depending on the above sources of business capital, it is therefore left to an entrepreneur to decide on how appropriate and reliable business funds could be sourced.

Beck and Demirguc-Kunt (2006) found out that SMEs face greater challenges in accessing formal sources of business finance and more substantial growth constraints which explain their inability to contribute to economic growth. The study further highlighted that financial and institutional development help to alleviate these growth constraints and improve upon their access to external finance. It also explained that financing tools like leasing and factoring could be useful in facilitating greater access to finance even when there are no well-developed institutions. The study found that since the major constraint faced by SMEs is access to finance. The financial and legal institutions would play a vital role in relaxing such constraints. It is desirable therefore to improve the business environment for all firms instead of promoting a large SME sector which might be characterized by a large number of small but stagnant firms.

This study was carried out on the access of finance by small and medium size enterprises found out that SME's face greater challenges towards accessing formal sources of business finance and substantial growth constraints which explains their inability to contribute to the economic growth. It further highlighted that financial and institutional development helps to alleviate suits growth constraints and improve upon their access to external finance. It further explained that financing tools like leasing and factoring could be useful in facilitating greater access to finance even when there are no well-developed institutions. The study concludes that since the major constraint faced by SME's is access to finance, financial and legal institutions that play a vital role in relaxing such constraints. It is desirable therefore to improve the business environment for all firms instead of promoting a large SME sector which might be characterized by a large number of small but stagnant firms. Based on the above reasons that access to finance is an important thing that influences inflows and outflows and growth of firms then it is essential for the development process (Beck & Asli 2006).

Akinola (2013), on entrepreneurship in Nigeria – funding and financing strategies, highlighted that for any economy to develop it has to consider the strength of entrepreneurship activities because development cannot be achieved without the contribution of entrepreneurship. The role of entrepreneurship is highly significant because it exists in both the public and private sectors of any economy. Even though the role played by entrepreneurship in every economy is known, but the achievement of the desired goal cannot be possible without the availability of finance. The availability of finance itself which serve as a first factor to be considered in entrepreneurial activities cannot guarantee the success of an enterprise without strategies for funding and investment need of the enterprise. The study, therefore, suggested among other strategies that could be embraced by entrepreneurs to enable them to have access to finance easily. These include; constructive cash budget, choosing banks for a relationship, possession of best financial leverage, technical knowledge of specialized financial institutions and agencies, transparent financial records, membership of trade associations, identification of appropriate source and choice of finance and business plan. Adopting the earlier mentioned strategies could ease their stress of accessing appropriate sources of finance because without adequate funding there will be no feasibility of an enterprise existence (Akinola, 2013).

Based on the above reasons that access to finance is an important thing that influences inflows and outflows and growth of firms, it is thus considered to be essential for the development process. By looking at the challenges faced by entrepreneurs in accessing formal sources of funds, Akinola, (2013) opined that for any economy to develop, it has to consider the strength of entrepreneurship activities because development cannot be achieved without the contribution of entrepreneurship. The role of entrepreneurship is highly significant because it exists in both the public and private sectors of any economy. Even though the role played by entrepreneurship in every economy is known, but the achievement of the desired goal cannot be possible without the availability of finance.

The availability of finance itself which serves as a first factor to be considered in entrepreneurial activities cannot guarantee the success of an enterprise without strategies for funding and investment need of the enterprise. The study, therefore, suggested some strategies among other strategies that could be embraced by entrepreneurs to enable them to have access to finance easily. These strategies include constructive cash budget, choosing banks for a relationship, possession of best financial leverage, technical knowledge of specialized financial institutions and agencies, transparent financial records, membership of trade associations, identification of the appropriate source and choice of finance and business plan. Adopting the strategies mentioned above could ease their stress of accessing appropriate sources of finance because without adequate funding there will be no feasibility of an enterprise existence.

Based on different opinions on sources of finance available for entrepreneurs, this study disagrees with the views of Ayyagari, Kunt and Masmovic where only categories of sources of finance are considered, and that of Delmar who suggested only funding strategy. Both views appear inadequate to this study. The suggestions of Lee, Sameen and Cowling (2015), on the choice of sources of finance based on the type of business is also inadequate to business growth because it favours only big businesses to have access to the formal fund while small businesses will be faced with growth constraints due to limited access to funds.

However, this study agrees with the suggestions of Beck and Dermigue-kunt (2006) on the challenges faced by entrepreneurs in accessing formal sources of finance and supported by Akinola (2013) where the emphasis is made on formulating strategies that would enable small businesses to have easy access to formal sources of funds. This study, therefore, believes that small businesses be given more priorities and encouragement by authorities through making available and accessible formal sources of finance, and to improve its abilities on the utilization of these sources so that economic growth would be achieved. Results from the analysis have shown that small business owners mostly relied so much on personal savings as their main sources of business capital where among the sources employed indicated only personal savings vary significantly as preference source among small business owners in Maiduguri.

3. METHODS

The study was carried out in Maiduguri the capital of Borno state where three categories of businesses were considered. The population of the study consists of all registered and functional small businesses in Maiduguri. There are 1595 active small businesses. A sample of 310 respondents was drawn using a stratified sampling method, and a sampling technique of Krejcie and Morgan small sample was utilized. Primary data was collected through the administration of structured questionnaire while spearman's' rank correlation was the tool employed in analysing the data. However, a reliability test was carried out where a Cronbach's alpha of 0.774 was obtained indicating that the data collected were reliable for analysis.

4. RESULTS AND DISCUSSION

Table 1 presents the results of the study.

Table 1 Spearman's rank correlation analysis on entrepreneur's preference among sources of finance

Null Hypothesis	Test	Level of Significance	Decision
The distribution of personal savings is the same across categories of organizational size.	Independent samples	0.021 (significant)	Reject the null hypothesis
The distribution of loan from friends and relatives is the same across categories of organizational size.	Independent sample	0.409 (not significant)	Retain the null hypothesis.
The distribution of loan from non-bank financial institutions is the same across categories of organizational size.	Independent sample	0.116 (not significant)	Retain the null hypothesis
The distribution of loan from bank is the same across categories of organizational size.	Independent sample	0.523 (not significant)	Retain the null hypothesis

Source: Field Survey, 2018.

Table 1 presents the results obtained from the Spearman's rank correlation analysis. It found personal savings = 0.021, loan from friends and relatives = 0.409, loan from non-bank financial institutions = 0.116 and loan from banks = 0.523 Level of significance. This result indicates that personal savings vary significantly as a preference of sources of finance among small businesses, while the loan from friends and relatives, loan from non-bank financial institutions and loan from banks vary insignificantly among small businesses in Maiduguri. As observed in the table, only personal savings as a preference of finance significantly varies among small businesses with a P value = 0.021, while the other three sources of finance vary insignificantly as preferences among small businesses in Maiduguri.

Evaluation of the objective of the paper was based on responses obtained from the questionnaires distributed to owners of small businesses. The outcome showed that personal savings varies significantly as a preference of finance among small businesses with a P value of (0.021) while other sources; loan from friends and relatives, loan from non-bank financial institutions and loan from banks varies insignificantly among small business with P values of (0.409, 0.116 and 0.523) respectively. Based on a study by Kisaka (2014), examined attitude towards savings, borrowing and investment found most entrepreneurs rely mainly on personal savings as the only source of finance for investment. This may suggest the reason for a variation on personal savings.

5. CONCLUSION

The study was carried out to evaluate the difference of preference among small businesses in Maiduguri Metropolis with regard to the source of generating finance. In conclusion, personal savings are the most preferred sources of finance among entrepreneurs over the other three sources which constitutes loan from friends and relatives, loan from non- bank financial institutions and loan from banks. However personal savings differ significantly among small business while the other three sources vary insignificantly.

RECOMMENDATION

Based on the findings, the study recommends that:

i. The entrepreneurs should be enlightened on the benefits of considering other sources of finance rather than relying on personal savings that cannot guarantee growth or expansion of their businesses.
ii. The government should empower small business owners by providing them with soft loans which would assist them in expanding their businesses and this could result to economic growth.
iii. The Small businesses are the catalyst of economic growth, and therefore, special attention need to be channelled towards motivating and empowering potential entrepreneurs so that industrialization could be achieved.

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