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FINANCING SMALL BUSINESSES

A Study of the Sources of Initial, Continuing and Growth Financing for 452 Small Businesses in the Massey University Region

by

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A thesis presented in partial fulfilment of the requirements for the degree of Master of Business Studies in Accounting and Finance at Massey University, Palmerston North, New Zealand.

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In recent years there has been a widespread interest in the importance of small businesses. There is much evidence to indicate that small businesses are important to the New Zealand economy. A large segment of the population is directly affected by the prosperity of small businesses.

In New Zealand, there has been a dearth of studies on the financing of small businesses. There are few official government statistics or studies on the subject in New Zealand. This research was therefore undertaken to fill part of this information gap, and to serve as a basis for further inquiry into and support for small business activity.

The primary objective of the study was to identify the sources and types of finance that small businesses in the Massey University region used at three crucial stages of their development, namely:

(1) When starting the business (Initial Financing)
(2) For current operations (Financing Going Concern)
(3) For future growth (Development and Growth Financing)

Corollaries to the primary objective were the areas in which the small businesses have the greatest financial need, the problems encountered by the small businesses when raising finance, and the criteria some lenders use when assessing the financial needs of the small businesses.

A survey of books and periodicals dealing with the financing practices of the small businesses was made to obtain any information relevant to the study. A postal questionnaire was used to obtain data from small businesses.
The major findings were:

(1) The major sources of funds utilised in starting a business were from the owner's and their family's savings. Some short-term finance was available from trading banks and to a lesser extent through credit facilities provided by the suppliers.

(2) Owner's investment and family sources continued to play a major role in the provision of continuing capital to small businesses. However, bank credit assumed a somewhat greater relative importance. Other sources (such as credit from suppliers, hire purchase financing and loans from finance companies) still played a minor role in the provision of current capital requirements for small businesses.

A significant group indicated that the existing sources did not provide sufficient funds for their current level of operations. More than half of the borrowing was to finance working capital needs.

(3) The majority of the respondents indicated plans for growing slowly and remaining independent. A very small number had any active plans to expand rapidly. Therefore the funds they indicated using were mostly of a short term nature with trading bank again overshadowing all other sources.

(4) A small number of the respondents indicated having serious difficulties in obtaining finance, mainly for working capital requirements.
(5) Interviews with some lenders revealed no evidence of any policy amongst them restricting loans to the businesses because of their small size. In normal times, frequently the main cause of refusal was the borrowers' inability to provide adequate and safe security and their inability to service the loan.
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Mohan Lal
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