

Copyright is owned by the Author of the thesis. Permission is given for a copy to be downloaded by an individual for the purpose of research and private study only. The thesis may not be reproduced elsewhere without the permission of the Author.

F I N A N C I N G S M A L L B U S I N E S S E S

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

by

Mohan Lal

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.

December 1977

A B S T R A C T

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.

ACKNOWLEDGMENTS

I would like to express my sincere thanks to Professor George Hines and to Mr B. R. Wilson for their time and assistance in developing and finalising the thesis.

I am indebted to the business community in the Massey University region, particularly the 452 small business owners and managers who formed part of the survey, for their co-operation and help in answering the many questions contained in the questionnaire. This research would not be possible without their co-operation.

I would also like to acknowledge the support and encouragement of my wife Elizabeth without which completion would never have been possible.

Mohan Lal

TABLE OF CONTENTS

	<u>PAGE</u>
ABSTRACT	ii.
ACKNOWLEDGEMENTS	v.
LIST OF TABLES	viii.
 <u>CHAPTER</u>	
1. <u>INTRODUCTION</u>	1
1.1 A Background and Justification for the Study	1
1.2 Organisation of the Study	10
2. <u>REVIEW OF THE LITERATURE</u>	11
2.1 Introduction	11
2.2 Financing Small Businesses	11
2.2.1 Available Sources and Types of Funds	11
2.2.2 Financing Small Businesses - United States	21
2.2.3 Financing Small Businesses - United Kingdom	33
2.2.4 Financing Small Businesses - New Zealand	40
2.2.5 Summary	43
2.3 Summary	46
3. <u>METHOD OF RESEARCH</u>	48
3.1 Research Objectives	48
3.2 Definition of Terms	49
3.3 Description of Research Method	50
4. <u>PRESENTATION AND ANALYSIS OF FINDINGS</u>	54
4.1 Introduction	54
4.2 Characteristics of Respondent Firms	55
4.3 Sources of Initial and Continuing Finance	55
4.4 Financing Current Operations	67
4.5 Borrowing	71
4.6 Financing Growth	76
4.7 General Summary	81

5.	<u>ANALYSIS OF FINANCIAL FACILITIES FOR SMALL BUSINESSES</u>	84
5.1	Availability of Finance, and Financing Problem	84
5.2	Financial Facilities for Small Businesses	86
5.3	Summary	93
6.	<u>SUMMARY AND CONCLUSIONS</u>	96
6.1	Restatement of the Aims of the Study	96
6.2	Summary of Findings	96
6.3	Conclusions	99
	BIBLIOGRAPHY	102
APPENDIX 1	Copy of Letter Sent to Partici- pating Small Businesses with Sample Questionnaire	106

LIST OF TABLES

<u>TABLE NO.</u>		<u>PAGE</u>
1-1	Distribution of Total Labour Force by Industrial Divisions	3
2-1	Distribution of Firms and Paid Employment by Size of Firms - United States	21
2-2	Comparative Summary of United States Studies	44
4-1	Location of Respondent Firms by Form of Legal Ownership	56
4-2	Distribution of Respondent Firms by Industry Classification	57
4-3	Distribution of Respondent Firms by Number of Employees by Industry Group	58
4-4	Sources of Initial Finance	60
4-5	Sources of Continuing Finance	63
4-6	Adequacy of Current Sources of Finance	64
4-7	Financing Current Operation - Working Capital	68
4-8	Financing Current Operation - Other Assets	70
4-9	Borrowing in the Past Five Years	71
4-10	Sources of Borrowing	72
4-11	Purpose for which the Money was Borrowed	73
4-12	Businesses Most Pressing Financial Needs	74
4-13	Growth and Development	77
4-14	Financing Growth	78