Sources of Financing Small Scale Enterprises (SSEs) in Akwapim North Municipal Assembly, Ghana

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ABSTRACT: The main objective of the study is to evaluate the extent of financing of SSEs within the Akwapim North Municipal Assembly in the Eastern Region, taking cognizance of the role and contributions of small scale enterprises for socio-economic development in the country, and to find out whether small scale businesses especially in the retail trading, dress making, Furniture works in the Akuapem North Municipal Assembly practice proper and effective financial records, managerial and accounting principles and skills in their field, to help them assess funds for their operations. In most jurisdictions, commercial banks as a group are the main source of external finance for SSEs. Most commercial banks are often unwilling to increase loan funding without an increase in the security given thereby leading to stagnation of growth and certain instances unable to expand to enjoy economies of scale necessary to serve their potential of being an engine of national growth and are thus collapsing. In view of the findings, we recommend that the National Board for Small Scale industries (NBSSI) should establish more of its offices in the district to make services more accessible to people in the rural areas.

KEYWORDS: Financing, Small Scale Enterprises, Constraints and Bureaucratic

I. INTRODUCTION

The dynamic role of small scale enterprises in developing countries as engines through which the growth objectives of developing countries can be achieved has long been recognized. After nearly two decades of structural adjustment programs in Africa, the state of African industrialization and efforts to build or rehabilitee technological capacities, it was argued that industry and every more technology has been largely ignored in nearly two decades of structural adjustment and that there is a serious mismatch between policies being pursued in the region and measures that are needed to rebuild industrial and technological capabilities.

The interest in the role of small scale industry in the development process continues to be in the forefront of policy debates in developing countries. The advantage claimed for the small scale industry are various, including the encouragement of entrepreneurship, the greater likelihood that small scale industries will utilize labour intensive technologies and thus have an immediate impact on employment generation; they can usually be established rapidly and put into operation to produce quick returns. Small scale industries development can encourage the process of both inter- and intra-regional decentralization; and they may well become a countervailing force against the economic power of larger enterprises. More generally, development of small scale industries is seen as accelerating the achievement of wider economic and socio-economic objectives, including poverty alleviation.

Typically, Smaller Enterprises face higher costs than larger enterprises in obtaining credit. Insufficient funding has been made available to finance working capital. Poor management and accounting practices to raise finance, information asymmetries associated with lending to small scale borrowers have restricted the flow of finance to smaller enterprises. An approach to learning how small enterprises(SSEs) perceive the impact of financial, regulatory, technical, marketing, and other input constraints, and to evaluating the results in relation to other empirical indicators.

Lack of access to finance emerges as the binding constraint for smaller, less established firms in Ghana and for all the SSEs—not only is informal financing limited for Ghanaian firms, even firms of adequate size and experience have difficulty borrowing from banks, and, if they do borrow, have difficult relations with their lenders. In Ghana regulatory and tax constraints appear largest for the smallest firms, declining somewhat as firms grow: because enforcement is comprehensive, the bureaucratic burden of negotiating with government officials is greatest for small firms.

By contrast, in Ghana the regulatory burden rises with firm size, because enforcement is more stringent for the larger and more visible firms. Constraints on physical inputs continue to inhibit Ghanaian SSEs. However, to the best knowledge of the researcher, no work has ever been done to ascertain the sources of financing the SSEs in Ghana and Akwapim North Municipal Assembly hence this research.

II. LITERATURE REVIEW

A. THE CONCEPT OF SSEs

In Storey, (1994)'s opinion there is no single, uniformly acceptable, definition of small firm. Firms differ in their levels of capitalization, sale and employment. Hence, definitions which employ measures of size (number of employees, turnover, profitability, not worth, etc.) when applied to one sector could lead to all firms being classified as small, which the same size definition when applied to a different sector could lead to a result.

The first attempt to overcome this definition problem was [3] formulated an 'economic' 'and 'statistical' definition.

Under the economic definition, a firm is regarded as a small if it meets the following criteria: It has a relatively small share of their market place; It is managed by owners or part owners in a personalized way, and not through medium of a formalized management structure; It is independent, in the sense of not forming part of large enterprise.

The Committee also devised a "statistical'' definition to be used in three main areas; Quantifying the size of the small firm sector and its contribution to GDP, employment, export etc; Comparing the extent to which the small firm sector's economic contribution has changed over time; Applying the statistical definition in a cross-country comparison of the small firms' economic contribution.

B. GHANA'S DEFINITION OF SSEs

Small scale enterprises have been variously defined, but the most commonly used criterion is the number of employees of the enterprise. In applying this definition, confusion often arises in respect of the arbitrariness and cut off points used by the various official sources. In [1] Boapeah et al, (1993) opinion, the number of employees in Ghana is the common criterion used in official circles to classify firms by size. As contained in its industrial Statistics, the Ghana Statistical Service (GSS) considers firms with less than 10 employees as Small Scale Enterprises and their counterparts with more than 10 employees as Medium and Large-Sized Enterprises. Ironically, the GSS in its national accounts considered companies with up to 9 employees as small and medium enterprises.

An alternative criterion used in defining small and medium enterprises is the value of fixed assets in the organization. However, the National Board of Small Scale Industries (NBSSI) in Ghana applies both the fixed asset and number of employees' criteria. It defines a Small Scale Enterprise as one with not more than 9 workers, has plant and machinery (excluding land, buildings and vehicles) not exceeding 10million cedis (US $9506, using 1994 exchange rate). The Ghana Enterprise Development commission (GEDC) on the other hand uses a 10 million cedis upper limit definition for plant and machinery. A point of caution is that the process of valuing fixed asset in it poses a problem. Secondly, the continuous depreciation in the exchange rate often makes such definition out-dated.

Small Scale Enterprises in Ghana, used the employment cut off point of 30 employees to indicate Small Scale Enterprises [2].

The later however dis-aggregated small scale enterprises into 3 categories:

- Micro – employing less than 6 people;
- Very small, those employing 6-9 people;
- Small- between 10-29 employees.

From the various definitions above, it can be said that there is no unique definition for a small scale enterprise thus, operational definition is required. This is one of the main issues this project intends to address.

C. THE FINANCING GAP

On a theoretical level, there is some controversy as to whether it is meaningful to speak of a "financing gap" [4]. Clearly, there can be such a gap if the authorities intervene in the market and maintain interest rates below the equilibrium rate, which would inevitably lead to excess demand for loanable funds. In the past, some analysts argued that it was not meaningful to speak of a funding gap unless the authorities actually kept interest rates below market clearing levels. It was held that as risks rise, providers of financial resources would sufficiently increase interest rates charged to all borrowers to bring the supply and demand for credit into balance. Due to problems of asymmetric information and agency problems, banks have difficulties distinguishing good risks from bad risks and in monitoring borrowers once funds have been advanced. Moreover, banks will hesitate to use interest rate changes to compensate for risk in the belief that by driving out lower-risk borrowers, high interest rates may lead to a riskier loan portfolio, thus setting in motion a process of adverse credit selection.

Banks could maximize their return by setting an interest rate that left large numbers of potential borrowers without credit.

D. THE DISTINCTIVE CHALLENGES OF SSEs FINANCE

Any potential provider of external debt or equity finance will want to monitor the company to determine whether it is acting in accord with the initial contract, to follow the progression of the firm and to have the means to oblige the user of funds to respect the interests of the provider of funds. There are numerous reasons why doing this effectively is more problematic for SSEs than for larger firms. Hence, banks are more likely to engage in credit rationing (i.e. not extending the full amount of credit demanded, even when the borrower is willing to pay higher rates) to SSEs than to larger companies (Stiglitz and Weiss, 1981; Hoff and Stiglitz, 1999).

In the first place, the SSEs sector is characterized by wider variance of profitability and growth than larger enterprises. SSEs also exhibit greater year-to-year volatility in earnings. The survival rate of SSEs is considerably lower than that of larger firms. Thus, one analyst found that manufacturing firms with fewer than 20 employees were five times more likely to fail in a given year than larger firms [5]. In the case of SSEs, it is very difficult to distinguish the financial situation of the firm from that of its owners. The use of company cars and home accommodations for both private and business purposes are clear cases in point. Furthermore, estate tax and intergenerational succession are important issues in SSEs but usually unimportant for larger companies.

SSEs often obtain funds from informal sources and, thus, may be less linked to trends in the formal fixed-income or equity markets. SSEs often use internally generated funds or loans from family and friends in "quasi-equity form". Funds from close acquaintances may be obtained at sub-market rates while borrowing from formal markets may be at rates higher than those available to larger companies.

Trade credit, i.e. credit supplied by non-financial entities, has always been an important component of SSEs finance and many analysts argue that the development of trade credit is an important element in assuring adequate finance for SSEs in emerging markets.

There are also potential principal/agent problems. The provider of credit will seek to require the borrower to act so as to maximize the probability that the loan is repaid, while the borrower may seek higher risk/higher return solutions.

Once financing is received, the entrepreneur may be motivated to undertake excessively risky projects, since all of the upside of the project belongs to the entrepreneur, while the lender prefers a less risky project that increases the probability that the loan will be repaid.

This problem, which is potentially present in all lending, is more serious for smaller firms than for larger firms because of the blurring of the line between the firm and the entrepreneur, and due to information asymmetries (Storey, 1995).

III. METHODOLOGY

The design of the study was the descriptive type. This type of study design can be described as a study which involves systematic collection and presentation of data to give a clear picture of a particular situation. The study area for the research is the Akwapim North Municipal Assembly. Emphasis was laid on the small scale enterprises which are dominant in the

Assembly.In order to achieve the desired aim of the project work, a population forty (40) of small scale industries in Dressmaking (Garments), Furniture works and Metal Work were studied through questionnaires and interviews.

Primary data was collected by the use of structured questionnaires which were designed and administered to SSEs. The study showed that most the respondents got their financing from personal savings, friends and family members.

IV. RESULTS

A. COMPOSITION OF RESPONDENTS

The chart bellow shows the distribution of sample size among entrepreneurs. The chart shows that the entrepreneurs in the furniture are more than the other two (2) that is dressmaking and metal works.

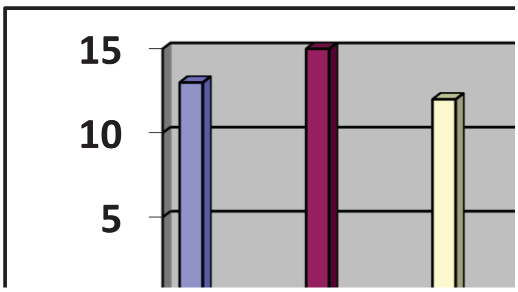

Figure 4.1 composition of respondents

B. INITIAL CAPITAL

Initial capital the respondent used in starting the business about 12.5% of the respondents said they started their business with an amount of money below GhȻ150, 45% said their capital ranged from GhȻ150 to GhȻ 300 , 22.5% had their capital ranged from GhȻ300 to GhȻ450. The rest of the respondents representing 20% started theirs with GhȻ 450 and above. This implies that the business does not require huge sum of money before one can start. Figure 4.2 below show the various amount each respondents used to start a business.

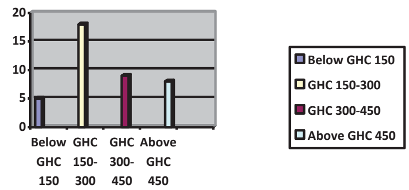

Figure 4.2 Initial Capital by respondents

C. RECORD KEEPING

It is obvious from figure 4.8 below that majority of small scale business owners that is 80% or 36 of the respondents record their income and expenditure whether daily, weekly, monthly, quarterly or yearly. The rest 8 who represent 20% of the respondent did not record their income and expenditure. They said, they see no reason why they should record their income and expenditure because whether they record or not it was the same profit and as matter of fact they are not accountable to anybody.

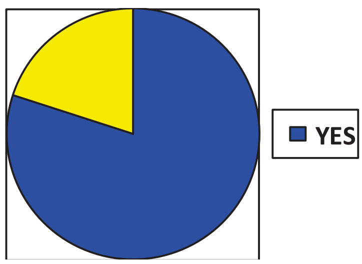

Figure 4.3 Record Keeping by Respondents

D. PROBLEMS ENCOUNTERED BEFORE SETTING UP THE BUSINESS

The figure 4.4 below shows, out of the total number of the 40 respondents who answered the questionnaires, 33 or 38.8% of the respondents was facing financial problems being the highest percentage. It was obvious that 30 being 35.3% of the respondents attributed their problem to location.15.3% of the respondents being 13 attributed to government restrictions.

Budget preparation also accounted for 10.6% that is 9 of the respondents. During the interview we found out that small scale business owners lack planning skills, thus they are usually unable to forecast customer demand owing to their liability to conduct market research.

They also lack managerial skills such as supervision, controlling and coordination. They explained that the financial problem they were facing was mainly high interest rate on loans, lack of collateral security for obtaining loans and high cost of business expenses for example income tax and rent.

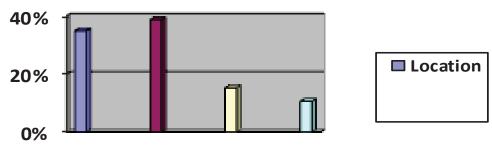

Figure 4.4 Problems Encountered Before Setting Up the Business

E. SOURCE OF CAPITAL

The source of capital talks about how the respondents get funds to start their operation the table below show how they organize their funds. Some of them got it from friends, families, financial institutions representing 30%, 50% and 20% respectively. Graph 4.5 shows the percentage of their source of capital.

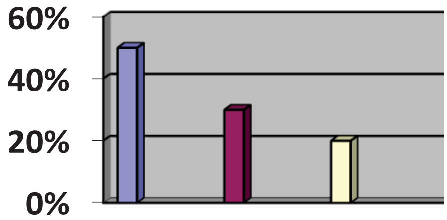

Figure 4.5 Source of Capital

F. SMALL SCALE ENTREPRENEURS RELATIONS WITH BANKS

Considering the kind of credit facilities these banks offer, it came out clear there was no facility for these small scale entrepreneurs from these banks in Akwapim North Municipal Assembly. Most of these banks branded these small scale entrepreneurs and the kind of operation they were into as a no go area; and the reason was simple it was a high- risk career. Banks like any other businesses are in business to make many and wouldn’t consider helping socially these small scale entrepreneurs where there is a strong indication that they may be at a loss.

Majority of the small scale entrepreneurs are people who have not had access to any formal education or one way or the drop out of school due to poverty. So with such manner of persons, most of them are not even aware there is such a facility like credit form. The banks themselves have not made any effort to educate these poor entrepreneurs of such a facility. The other group of small scale entrepreneurs who said they had made attempts to these banks for such a facility said they were astonished by the payback period and the interest rate.

V. CONCLUSION

Reference drawn from the analysis revealed that the educational level of the entrepreneurs in small scale business within the study area were generally low. This was made clear by the 35% of the respondents having attained the basic level in education.

The study also revealed that most of the entrepreneur in this area of business acquired their source of capital from personal savings. This revealed that the government of Ghana is not assisting them financially enough to expand their operations in the assembly. The study also revealed that 100% of the respondents saved some of their income. Out of those who saved their income 12.5% saved in bank as "KUDI NKOSO", 45% saved with micro finance operators, 25% saved with susu collectors, 7.5% saved with credit union and 10% of them saved personally. The reason was that it is easy to acquire loan from susu collectors and micro finance operators.

With regards to budget preparation, it was revealed that 45% of the respondents did not prepare budgets before beginning the business operation. As to who prepare the budget, many said they did it themselves. Furthermore it was that 20% of the respondents do not keep record of their income and expenditure. The 80% that keeps records said they record their income and expenditure daily.

Finally, the study revealed that the problem facing the small scale industries in the Furniture works, dressmaking (Garment) and Metal works were ,financial problem ,managerial problem, high transportation, rampant changes in prices of goods and services and limited market share. Predominant among these were financial problem followed by rampant changes in prices and goods.

The small scale industries and for that matter the entrepreneurs were aware of their importance to the growth of the Ghanaian economy but they were deprived of financial problems and land to operate. Most of these entrepreneurs did not prepare well despite all the importance associated with preparations. Some also did not keep records to know their actual cost and profit attained in that particular year. There was also lack of managerial skills among some small scale industry operators in supervision, controlling, planning and coordinating. These problems hinder their success in their field.

The study was successfully carried out and has greatly enhanced and given the researcher more insight into the operation of Furniture works, dressmaking (Garments) and metal works business. Users will find the document very beneficial.

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