PRINT: ISSN 0971-8923 ONLINE: ISSN 2456-6756
J Soc Sci, 49(1,2): 67-69 (2016)
DOI: 10.31901/24566756.2016/49.1,2.09

# Access to Debt Finance by Young Entrepreneurs in Polokwane, South Africa

**Moliwa Rector, Olawale Fatoki and Olabanji Oni**

*Department of Business Management, University of Limpopo, Private Bag X1106, Sovenga, 0727, Limpopo Province South Africa*
*E-mail: [1]<moliwarector@yahoo.com>, [2]<olawale.fatoki@ul.ac.za>, [3]<olabanji.oni@ul.ac.za>*
*Telephone: [1,2]<00927 15 268 3897>, [3]<00927 15 268 2646>*

**KEYWORDS** Access. Debt Finance. Entrepreneur. Need. Obstacles. Young

**ABSTRACT** The paper investigated the need for and access to debt finance by young entrepreneurs. In addition, the study examined the obstacles to access to debt finance by young entrepreneurs. This study was conducted at Polokwane, South Africa. Forty nine young SME owners participated in the study. Convenience and snowball methods were used to select the study participants. The self-administered questionnaire method was used for data collection. Descriptive statistics was used for data analysis. The results indicated that although there is a strong need for external debt finance by young entrepreneurs, however, access to debt finance is limited. Obstacles to debt finance by young entrepreneurs include lack of collateral and bad credit history. Recommendations to improve access to debt finance by young entrepreneurs are suggested.

## INTRODUCTION

Small and medium enterprises (SMEs) play an important role in the economy of many countries. SMEs contribute to job creation, poverty reduction and economic growth of many countries (Subhan et al. 2013). South Africa's current unemployment rate is 26.7 percent. Youth unemployment is much higher at 54.5 percent (Statistics South Africa 2016). SMEs are expected to be one of the solutions to the high levels of youth poverty and unemployment in South Africa (FinMark 2010). The SME sector contributes sixty-one percent of employment and fifty-two to fifty-seven percent of South Africa's gross domestic product (Abor and Quartey 2010).

According to De Clercq and Honig (2011) and Sharma and Madan (2014), one of the solutions to the high levels of youth unemployment in many countries is the entrepreneurship. However, the failure rate of SMEs including those owned by young entrepreneurs is very high in South Africa (Scheers 2010). Many factors affect the performance of SMEs. Inaccessibility to external debt is one of the principal causes of SME failure in South Africa (Cant and Wiid 2013).

### Objectives of the Study

The objectives of the study are:

- To investigate if SMEs owned by young entrepreneurs need external debt finance from trade creditors and commercial banks.
- To examine if SMEs owned by young entrepreneurs have access to external debt finance from trade creditors and commercial banks.
- To explore the obstacles to demand and access to external debt finance by young entrepreneurs.

### Literature Review

#### *Definition of Youth Entrepreneurship*

The National Youth Policy 2015 of South Africa defined youth development as: "*an intentional comprehensive approach that provides space, opportunities and support for young people to maximise their individual and collective creative energies for personal development as well as development of the broader society of which they are an integral part.*" *Youth refers to "young people falling within the age group of 14 to 35 years"* (National Youth Commission Act 1996). Chigunta (2006) defined youth entrepreneurship as *"the practical application (by youths) of enterprising qualities, such as initiative, innovation, creativity, and risk-taking into the work environment (either in self-employment or employment in small start-up firms), using the appropriate skills necessary for success in that environment and culture."* Young people become entrepreneurs because of necessity factors such as lack of jobs or opportunity factors such as the desire to provide innovative products and services (Riahi 2010). The benefits of youth entrepreneurship include employment creation, provision of goods and services, improving business competition, innovation and the revitalising of communities. The challenges facing young entrepreneurs include, lack of experience, lack of extensive network and lack of capital (Riahi 2010; Uddin et al. 2015). Funding constraint for small businesses may cause low productivity and poor performance. This can lead to close down or exit from the market (Faulkender and Peterson 2006). Inadequate internal finance is one of the reasons why SMEs need external finance (Blumberg and Letterie 2008).

## RESEARCH METHODOLOGY

The study was conducted at the Polokwane Central Business District in the Limpopo province of South Africa. The survey method was adopted for data collection. Self-administered questionnaire was used to collect data from the study participants. According to Cooper and Schindler (2006), self-administered questionnaires are research questions directed to respondents to complete with no external involvement of any party. There is no list of young entrepreneurs in the study area, therefore, convenience and snowball sampling methods were used to identify the study participants. Young entrepreneurs were selected based on their convenient accessibility and proximity for the purpose of their participation in the study. Reliability is concerned with the consistency of measures. The Cronbach's alpha was used to measure reliability. Descriptive statistics was used for data analysis.

## RESULTS AND DISCUSSION

### Response Rate and Biographical Information

One hundred twenty questionnaires were distributed to young entrepreneurs in the study area and 49 returned. The response rate was forty-one percent. There were 35 male respondents and 14 female respondents. Seventy-one percent of the respondents obtained matric or post-matric qualifications.

### Need and Access to External Finance

Out of 49 respondents, 37 needed bank loans whereas only 12 respondents did not demand debt finance from commercial banks. In addition, 40 respondents needed trade credit and 9 respondents did not need trade credit. However, only 8 young entrepreneurs were able to access commercial bank credit. In addition, fifteen young entrepreneurs were able to access trade credit. Osano and Languitone (2016) found that only about five percent of SMEs are financed by commercial banks. Many SMEs finance their projects through their own funds or contribution from family and friends. Inaccessibility to external debt capital can negatively impact the performance of SMEs.

### Reasons for the Rejection of SMEs' Credit Applications

The most cited and common reasons for inaccessibility to debt finance are lack of collateral. 29 respondents agreed that it is a problem, 27 out of 49 respondents agreed that lack of managerial skills is an obstacle in obtaining external finance. Another important reason for the rejection of credit application by commercial banks is bad credit history. In addition, inability to provide a credible business plan is one of the reasons for the rejection of credit applications of young entrepreneurs by commercial banks. Kwaning et al. (2015) agreed that lack of acceptable collateral is one of the major reasons for inaccessibility to debt finance by SMEs. In addition, banks are very strict in vetting the credit application of SMEs.

## CONCLUSION

Young entrepreneurs are one of the drivers of the South African economy. Access to financial resources is one the major factors that impact on the growth and success of SMEs owned by young entrepreneurs. The primary objective of the study was to investigate if SMEs owned by young entrepreneurs need and have access to external debt finance from trade creditors and commercial banks. In addition, the study investigated the obstacles to access to debt finance by young entrepreneurs. The results indicated that there is a strong need for debt finance by young entrepreneurs. However, access to debt finance is limited. Many applications for debt finance are rejected by commercial banks and trade creditors. Lack of collateral, bad credit record and lack of business plan are the major obstacles to access to debt finance by young entrepreneurs.

## RECOMMENDATIONS

It is highly recommended that government and financial institutions should assist young entrepreneurs with finance. In addition, young entrepreneurs are encouraged to utilise the networking platform as it would improve access to financial resources especially trade credit. Commercial banks and trade credit providers should also provide consistent information about financing procedures and also make the criteria and requirements clear to young entrepreneurs.

Young entrepreneurs should visit financial institutions and find out the requirements needed to obtain external debt finance. The information will help business owners to gather all relevant documents needed to obtain finance. Government agencies that support small business development (that is, Small Enterprise Finance Agency, Small Enterprise Development Agency and the Department of Small Business Development) should include young entrepreneurs as part of their strategic plans. Young entrepreneurs should visit these agencies and find relevant information on how to access finance.

## REFERENCES

Abor J, Quartey P 2010. Issues in SME development in Ghana and South Africa. *Int Res Jou of Fin & Eco,* 39: 218-228.

Blumberg BF, Letterie WA 2008. Business starters and credit rationing in small business. *Small Bus Eco,* 3(1): 187-200.

Cant MC, Wiid JA 2013. Establishing the challenges affecting South African SME's. *Int Bus & Eco Res Jou*, 12(6): 707-716.

Chigunta F 2006. Youth Entrepreneurship: Meeting the Key Policy Challenges. From <http:// yesweb. org/gkr/res/bg.entrep.ta.doc> (Retrieved on 2 May 2016).

Cooper DR, Schindler PS 2006. *Business Research Methods*. USA: McGraw-Hill.

De Clercq D, Honig B 2011. Entrepreneurship as an integrating mechanism for disadvantaged persons. *Ent & Reg Dev,* 23(5): 353-372.

Faulkender M, Petersen MA 2006. Does the source of capital affect capital structure*? Rev of Fin Stu,* 19: 45-79.

Kwaning CO, Nyantakyi K, Kyereh B 2015. The challenges behind SMEs' access to debts financing in the Ghanaian Financial Market. *Int Jou of Small Bus & Entrepreneurship Res*, 3(2): 16-30.

National Youth Commission Act 1996. From <http:// www.gov.za/sites/www.gov.za/files/a19-96.pdf.> (Retrieved on 5 September 2015).

National Youth Policy 2015. The Presidency Republic of South Africa. From <http://www. thepresidency. gov.za/MediaLib/Downloads/Downloads/ NYP%20Policy%202020%20Report.pdf > (Retrieved on 5 September 2015).

Osano HM, Languitone H 2016. Factors Influencing Access to Finance by SME's in Mozambique: Case of SME's In Maputo Central Business District. From <https://innovation-entrepreneurship .springeropen. com/articles/10.1186/s13731-016-0041-0> (Retrieved on 5 September 2015).

Riahi S 2010. Youth Entrepreneurship: Ottawa's Portfolio in Talent Development. From <http://timreview. ca/article/394> (Retrieved on 8 August 2016).

Scheers L 2010. Challenges of small family groceries shops in South Africa. *World Jou of Ent Man & Sus Dev*, 6(3): 221-231.

Sharma L, Madan P 2014. Effect of individual factors on youth entrepreneurship India. *Jou of Glo Ent Res*, 2(3): 1-17.

Subhan QA, Mehmood MR, Sattar A 2013. Innovation in small and medium enterprises and its impact on economic development in Pakistan. *Pakistan Eco & Soc Rev*, 52(2): 159-174.

Uddin M, Chowdhury MM, Ullah MM 2015. Barriers and Incentives for Youth Entrepreneurship Start-Ups: Evidence from Bangladesh. From <https:// globaljournals.org/GJMBR_ Barriers-and-Incentives-for-Youth.pdf.> (Retrieved on 7 September 2015).

**Paper received for publication on July 2016**
**Paper accepted for publication on September 2016**