FINANCE AS A CRITICAL SUCCESS FACTOR IN THE ESTABLISHMENT AND SUSTAINABILITY OF ENTREPRENEURIAL VENTURES.

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Abstract

The establishment and sustainability of entrepreneurial venture is driven by the availability of adequate finance as well as access to the available capital at every stage of the business cycle. However there are other resources needed for the survival of the entrepreneurial venture such as human and material resources. This paper seek to identify various sources of finance for a start-up small business ventures, risk associated with the capital venture, the significance of finance and their implications for the entrepreneurial venture. Challenges that are faced by the providers of finance to the small business ventures in building up the finance gap are also analysed. 25 small business ventures (Poultry) were randomly selected from 5 local governments out of 18 local governments in Ondo State. Hypothesis testing was carried out by adopting a t-test based on the sample size and it was found out that there is a significance difference at 0.05 alpha levels that adequate finance is needed for the establishment and sustainability of entrepreneurial venture at every stage of its cycle.

Keywords:*Entrepreneurial venture, Capital, Sustainability, Finance gap, Risk.*

Introduction

Finance (venture capital) has been identified by many researchers as an important factor for a successful start-up and the sustainability of entrepreneurial ventures (Allen and Hall 2008; Brown, 2005). However, there are other factors such as degree of innovation, human capital, technology and the strength of stakeholders that are important apart from finance that contributing factors to a new business venture in order to be viable and to achieve continuous success as the business life cycle progresses. These inputs allow advice and guidance to be given to new entrepreneurs both on the technical and managerial aspects of running a business (Aernoudt 1999). Venture capital is defined as “financial investment in unquoted companies, which have significant growth potential, with a view of yielding substantial capital gains in line with the additional risk and illiquidity of an investment, which cannot be freely traded during the lifetime of the investor's commitment to the business” (Deakins and Freel 2009). In the recent years, there have been a percentage of business failures involving entrepreneurial ventures in developed and emerging markets like Nigeria that is giving utmost attention to entrepreneurial development, as a result of recent economic downturn with a significant impact on the labour force and economic development (Ervin, Greg and Johnson 2009). This paper seek to critically analyse the problem of inadequate finance in the start-up and sustainability of poultry business ventures in Ondo State, Nigeria, other alternatives sources of finance, the role played by government in supporting entrepreneurial ventures in order to boost the Gross

Domestic Products (GDP) of the economy as well as alleviating problem of unemployment and challenges faced by the external providers of funds to small business ventures by looking into relevant theoretical and empirical review of literature with appropriate research methodology for the collection and analysis of data in order to arrive at reasonable conclusion and recommendations.

Research problem

The establishment and sustainability of entrepreneurial ventures in both developed and emerging markets have suffered a lot of set back as a result of inadequate finance. A new start-up technology- based entrepreneur with good intention of contributing to economic growth and development is posed with the challenge of inadequate capital to run the business. This has resulted in the natural death of many small businesses that do not have access to any other external sources of finance apart from the initial capital raised by the founder, family and friends. However, commercial banks and other business angels that supposed to build up the finance gap are faced with high level of risks and uncertainties as a result of high default rate due to unstable exchange rates, government policies, high interest rates and unacceptable credit history.

More attention is being given to development of entrepreneurial ventures in Nigeria as at moment in order not to rely solely on income generated from the oil industry for the development of Nigeria economy likewise a strategy for in unemployment rate. But this has suffered a lot of set back as a result of inadequate finance to support the establishment and survival of entrepreneurial businesses and this has resulted in the research topic. Therefore this research will critically analyse “finance” as a critical success factor in the establishment and sustainability of entrepreneurial ventures and the roles that government, commercial banks and business angels need to play in ensuring the survival of venture businesses. This will enable the researcher to arrive at policy recommendations on the research topic.

The objective of this research is to identify the significance of finance and their implications for entrepreneurial ventures. While the research will focus on the following objectives; identify various sources of finance for entrepreneurial venture, analyse and evaluate the challenges face the small business ventures owners in building up the finance gap and To identify the significance of external finance for business ventures and the inherent risks.

Review of literature

Several studies have identified factors that lead to venture success and failure, for example, Allen and Hall (2008); Colombatto and Melnik (2007) Brown (2005). The majority of the work related to venture and entrepreneurial firms and their success factors were classified with ones associated with start-ups, early stages ventures and establish ventures. However, the degree of their significant contribution to the success and sustainability was not adequately considered. The financing of the creation of entrepreneurial ventures depends on a large variety finance sources: founder of the business, family, friends, wealthy individuals (business angels), commercial banks, the small business administration and or institutional venture capital (VC) investors Michel (2009). On the other hand, venture capital invests in the seed stages and some of the largest firms, especially in the high-tech industry have obtained funding from these types of investors to support their start-ups. The success of a new business venture often depends on entrepreneur's ability to establish a network of supportive relationships, especially with informal or “angel” investors, who represent a significant source of venture capital (Steier and Royston 2000). Business angel funds are therefore smart funds and essential to the establishment and development of new enterprises.

Furthermore, as formal venture capitalists are moving towards larger deals and shifting their investments to a later stage of development, creating a "second" equity gap, those so-called business angels become more significant in the financing of seed, early stage and second round phases. Hence, any policy to inspire entrepreneurship and development should consider business angel financing as a priority Aernoudt (2005). To achieve a successful and profitable business development, it is necessary to ensure that the right type of capital is matched with the risk involved in the business. For a start-up, with no earnings until the product is fully developed and the first sales are made, debt finance is seldom the best source of external finance and is usually secured on assets. Before seeking external financing, an entrepreneur should initially explore all methods of internal financing, such as using profits, selling unused assets, reducing working capital, obtaining credit from suppliers and prompt collection of account receivables Robert, Miheal and Dean (2009). On the other hand, it is noted by Hellman and Puri (2002) that start-ups ventures funded by institutional venture capital investors usually have a faster growing business, create numerous jobs and have a significant impact on the business environment.

Empirical research on the relationship between the survival of a new small business ventures and bank loan by Astebro and Irwin (2003) using ordinary square regression model found out that there is a negative correlation between having a bank loan and business survival, and a positive correlation between having a non-bank loan and the survival of the business. However, having a bank loan, all things being equal is a positive predictor of the survival of start-up companies. These findings also enable some inferences about the process of loan source selection by start-up business owners and bank's loan granting process. Kutsuna and Nobuyuki (2004) established the activities of small business owner-managers acting as financial and nonfinancial supporters of business start-ups in Japan, by using two data sets (both surveyed in 1999 by the National life Finance Corporation). The empirical results show that owner-managers who are younger, from larger small businesses, or who have received support when their own businesses were starting tend to provide start-up support. It is shown that there is a clear tendency to provide financial support to business types different from the managers' own businesses. One way of increasing the pool of informal investors would be to attract managers in various positions to make informal investments and expand their businesses and entrepreneurial skills. The study of Van and Howard (2001) investigates the familiarity of owners of small technology-based firms with alternative forms of capital by stage of development and in comparison with their ability to price and negotiate external equity and debt investment. The result indicates that owners are most familiar with the traditional sources of capital, somewhat less familiar with capital commonly used to fund business development.

Theoretical framework

Basu and Simon (2001) investigated the theoretical model of family finance and found out that self-finance provided by the entrepreneur's own saving and assets are the largest source of funds in most countries. David (2004) concludes that banks are "special" in that they provide services such as monitoring that are not provided by other debt claimants, while non-bank private debt serves as important role in accommodating the financing needs of firms with low credit quality. As a result of this, provision of funding shifts from capital to debt and so predominance of intermediate over market financing (Modigliani and Enrico 2002). Though, it is difficult to accurately enumerate the cumulative amounts of funds coming from each funding source, different estimates recommend that various sources of funds contribute a significant amount of capital to entrepreneurial ventures (Wong 2002). The existence of multiple sources of financing raises the question of whether the source of funding matters for the entrepreneurial ventures, but rather the survival and sustainability of the business.

Many entrepreneurial ventures have experienced a setback in Nigeria, basically as a result lack of financial support from the government and inability to assess commercial bank's loan as a result of high interest rate and inadequate or absence of security being a start-up ventures. In the developed economies, it was noted by Small Business Association (SBA) that these small business ventures represent 99% of all employers and creates up to two-thirds employment for the labour market (SBA, 2003; 2009). However, the ability of small firms to access finance is hindered by persistent market failures which create funding gaps. These funding gaps are greatest for new ventures seeking external finance for the first time, for firms seeking small amounts finance, for technology-based firms and firms in peripheral regions (Colin 2008).

The establishment and sustainability of entrepreneurial ventures has been narrowed down to existence of finance gap (credit rationing) as a result of demand from small ventures is greater than the willingness of financial institutions to supply the required finance at current market conditions such as prevailing interest rate and exchange rate. For example, various official reports and other researchers have pointed to the continued existence of an equity gap in the United Kingdom and the Enterprise Directorate review of evidence suggested that ' Small businesses find it difficult to obtain modest amounts of private equity finance' (Deakins and Freel 2009).

Methodology

Since this paper focus on the finance as a critical success factor in the establishment and sustainability of entrepreneurial ventures, using twenty five poultry businesses in Ondo State of Nigeria as the sample size. Empirical sources of data were employed in order to do some further exploration, therefore resulting in conclusions as well as recommendations regarding the subject. In addition, the information was a mixture of primary and secondary data in which quantitative measures would usefully supplements and extend the qualitative analysis. The theoretical population of the study consists of the entire entrepreneurial ventures in agricultural businesses with a particular reference to poultry business in the country. However, the study was restricted to Ondo State. The choice of Ondo State stems from the fact that is one of the States in Nigeria that focus on agriculture and that the concentration and predominance of entrepreneurial ventures in Ondo State is easily identifiable. A simple random sampling technique was adopted to select a total of 25 entrepreneurs that constituted the sample size. The study area comprises of 5 Local Government Areas (LGAs) out of 18 LGAs in the state with an average thirty (30) viable poultry businesses. 5 poultry businesses were randomly selected from each local government for administration of questionnaires and in – depth interviews, thereby resulting in a proposed sample size of 25 poultry business ventures. It should be pointed out that limited financial resources at the researcher's disposal could not permit or allow for a greater sample size. The Researcher has a strong link with poultry business operators in the state as a result of past business relationships in the course of my working experience as a business development manager in the financial industry. The initial approach towards the empirical study consisted of in- depth analysis of various related empirical studies done on the research area. Furthermore, published reports, journals and bulletin from Entrepreneurship management, economics, business management and available relevant documents were examined to acquire as much initial information as possible, so that the empirical research is constructed to address previous deficiencies as well as put together to be useful and practical. For the analysis of the primary research data, hypothesis testing (null and alternate) were employed as follows:

Ho: Adequate capital is essential for the establishment and sustainability of business ventures.

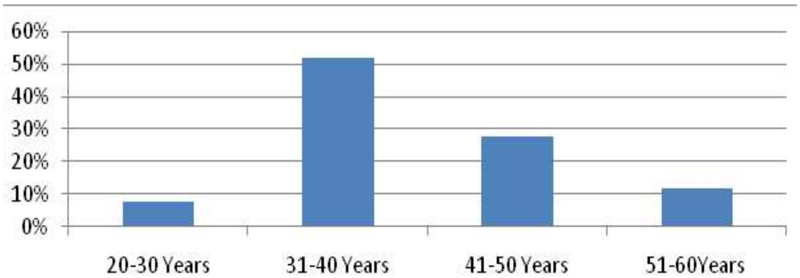
Hi: adequate capital is not needed for establishment of venture capital

We accept Ho at 5% alpha level of significance and reject the alternate hypothesis Hi if t-cal is > t-tab. T-test was adopted since the sample size (n) is = 30. Average means, frequency, mode and standard deviation were also employed in the data analysis.

Analysis of data

It was found out that 84% of the correspondents (Poultry Farmers) were male, while 16% of them were female. This indicated that the nature of the business calls for the attention of male than female as a result of physical and financial stress involved in the business. It was discovered in the course of interview that male have large heart to bear any loss in the case of any unforeseen occurrence as the business is prone to high risk and uncertainty, such as high mortality rate, disease out brake, theft and attack from other animals. 52% of the respondents were between the ages of 31-40 years, while other age categories are shown in the figure below:

Figure I: Age Analysis



Source: Survey March, 2013

In analyzing the literacy level, it was found that 19 of the respondents representing 76% were literate, while 4 of them were semi-illiterate and the remaining 2 representing 8% were illiterate. The high rate of literacy level has assisted many of the respondents to effectively and efficiently manage their resources (financial, material and human) in a harmonious manner in order to achieve their pre-determined goals. This was categorized into three different groups namely; literate, semi-literate and illiterate. Surprisingly, some of them are Masters Degree holders with entrepreneurial traits as a result of rate unemployment and job loss in the many nations of the world. This is represented in the table below:

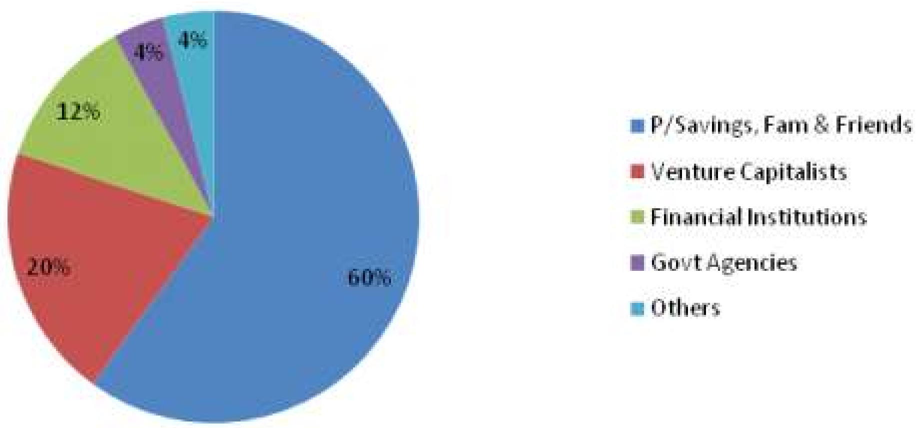
Figure II: Literacy Level of the respondents

Literacy Level	No of Respondents	% of Respondents
Literate	19	76%
Semi- literate	4	16%
Illiterate	2	8%
Total	25	100%

Source: Survey March, 2013

The major sources of funds that are available to the correspondents are personal savings and funds from family, friends and other associates. This constituted 60% of the total sample size, while venture capitalists was 20%, financial institution 12% , government funding and others (Pay-off package) constituted 4 % respectively. This shows that many of the entrepreneurs are not getting adequate financial support either from the government and financial institutions that are supposed to be major sources of funds to bridge the financial gap being experienced by the entrepreneur at the various stages of the business life-cycle. The diagram below illustrates the various sources of finance available to entrepreneurial ventures.

Figure III: Sources of Finance.



Source: Survey 2013

As regards the other sources of finance for entrepreneurs, it was found out from the survey that severance packages for some people that have been laid off from their job and gratuity paid to retirees are other sources of fund for the start-up of new business ventures.

However several challenges are being faced by the owners of small business enterprise in assessing funds from formal financial institution, micro - credits, and venture capitalist. Two most challenging issues are high interest rate and non- availability of collateral. All the respondents gave negative responses on the above issues. The tenor of the available funds from these institutions and other terms and conditions attached are also issue on concern likewise the bureaucratic processes. Almost all the respondents also gave negative comments on the role of government agencies such as Bank of Industry (BOI), Industrial Development Canters (IDCs), National Economic Reconstruction Fund (NERFUND) in the area of the financial support to small business, even many of the micro-credit programmes organised by the governments are just mere propaganda.

The hypothesis testing was also carried out in which the null hypothesis (Ho) was accepted and the alternate hypothesis (Hi) was rejected at 5% alpha level from the initial assumption that adequate capital is essential for development and sustainability of business venture. The t-cal = 0.450 while the t-tab is 1.645 and since t-cal > t-tab at 0.005 significance level, we accept Ho and reject Hi indicating that capital is essential for the new business start-up and its survival.

Entrepreneurial decisions such as the decision to start a new enterprise usually require the investment of money, time and other resources that need a return to make them worthwhile. But there is a risk that the investor will get nothing in return, or even be worse off than before. There is a continuum of possible outcomes ranging from extremely positive with very high return to extremely negative with substantial losses. Entrepreneurial activity is inherently risky, and quantifying the outcome is fraught with difficulties. In the face of an unknown future, and the risks of investment, there are many choices to make, and much may be at stake.

There are various categories of financial risks associated with venture capital namely; credit risk, market risk, interest rate risk, currency risk, equity risk, liquidity risk, refinancing risk, operational risk, legal risk, political risk volatility risk, profit risk and settlement risk.

Types of Fund

There are various types of venture capital that are commonly identified within the framework. These are:

- Institutional Venture Capital: These are investments in entrepreneurial venture by firms of full-time professionals who raise finance from pension funds, banks, insurance companies and other financial institutions.
- Informal Venture Capital: This is also known as Business Angels Finance. Investments by wealthy private individuals who are prepared to use their financial resources to make risk investments based upon their experience and interests. Business Angels are often retired senior executives of large companies, or entrepreneurs who have sold their companies and now wish use the money.
- Corporate Venture Capital: This is otherwise known as Corporate Venturing. These are form of minority investor made by large companies in smaller enterprises for a principally strategic action such as

gaining a window on new technologies rather than exclusively financial motives.

- Public Sector Capital: While government plays a role in encouraging private – sector venture capital through policy investments such as Enterprise Investment Scheme or offering (primarily, capital gain) tax incentives may, occasionally, act more directly as a provider of venture finance.

Conclusion

New entrepreneurial venture a reliable sources of finance to be able to thrive at various stages of entrepreneurial life- cycle. Personal savings being the traditional source of new business venture has been seen as the starting point of the business start-up. External sources of finance are seen as a secondary way out to bridge the financial gaps experienced by the entrepreneur. However, several financial risks are inherent in these external sources of finance. The conditions and terms attached to the external sources serve as a guide for the entrepreneur to take some critical decisions that will affect the business either in the short run or long run, basically because the higher the risk, the higher the returns on investment and vice-versa.

Policy Recommendations

Based on the findings from this research, the following recommendations are made.

- There is need for the government agencies in the area of financial support to small scale business firms by making soft loans available to the small business owners with flexible terms and conditions that will not discourage the beneficiary in order to cushion other sources of finance available to them.
- Terms and conditions attached to fund assessment by the financial institutions should be reviewed to accommodate entrepreneurial businesses particularly in the area of interest rate and collateral.
- Awareness programmes should be organised by the government agencies and financial institutions in order to properly sensitise small business owners in meeting the basic requirement for them to have access to loans. Since there are some risks attached to the loan and to guide against high rate of default.

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