

Owners' Characteristics and the Financial Bootstrapping Strategies Used by Rural Small Businesses in South Africa

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Abstract: The purpose of this study was to examine if there are significant differences in the financial bootstrapping strategies of rural small businesses on the basis of owners' demographic characteristics (level of education and gender). The research followed a quantitative research method with descriptive research design. A sample of 104 rural small businesses participated in the survey. Data was collected through the use of self-administered questionnaires in a survey. The participants in the study were rural small business owners in Fetakgomo Municipality located in the Limpopo Province of South Africa. The study utilised the convenience and snowball sampling techniques to select the study participants. Data analysis included descriptive statistics, factor analysis and the T-test. The Cronbach's alpha was used to measure reliability. The results of the T-test showed significant differences between gender and level of education and the financial bootstrapping methods used by rural small businesses. Recommendations are made to improve the awareness of bootstrapping by small business owners.

Keywords: *Owners' characteristics, financial bootstrapping, small business, rural, South Africa*

1. Introduction and Background

There is no uniform definition of a rural area in South Africa (Gaede & Versteeg, 2011; Jacobs & Hart, 2012). According to the Department of Land Affairs (1997, p1), rural areas can be defined as "sparsely populated areas in which people farm or depend on natural resources, including the villages and small towns that are dispersed through these areas. In addition, rural areas include large settlements in former homelands, created by the apartheid removals, which depend for their survival on migratory labour and remittances". The rural population can be calculated as the difference between total population and urban population (Trading Economics, 2016). The rural areas of South Africa face many development challenges. Armstrong et al. (2007) indicate that the incidence of poverty is much higher in the rural areas of South Africa. The poverty rates of individuals and households in the rural areas more than double the corresponding rates for urban areas. In addition, the level of unemployment in the rural areas is much higher than in urban areas. (de Witte et al., 2011; Tshabalala, 2014). Rural income inequality is much higher than urban inequality (Mahadea & Simson, 2010). Crime is higher in rural areas compared to urban areas (The South African Presidency, 2008). The creation and growth of small and medium enterprises (SMEs) can help to alleviate the challenges faced by rural areas in South Africa (Mugobo & Ukpere, 2012; Lekhanya, 2016). According to Amra et al. (2013), growing and successful SMEs offer a critical contribution to the policy goals of poverty alleviation, employment creation and promotion of economic growth in South Africa. However, the failure rate of SMEs in the rural area is very high in South Africa (Chimucheka & Mandipaka, 2015).

In general, 70% of SMEs in South Africa fail in their first year. The failure rate of rural SMEs is higher than that of urban SMEs (Business Environment Specialist, 2014). This negatively impacts on the ability of SMEs to reduce the high rates of unemployment, poverty and crime in the rural areas of South Africa. The major causes of the failure of rural SMEs include small markets, lack of *business* and technical skills and limited access to external finance (Mugobo & Ukpere, 2012; Arko-Achemfuor, 2012; Agbenyegah, 2013). Lam, (2010) points out that financial bootstrapping is a method for meeting the need for resources by firms without reliance on long-term external finance from equity or debt holders. Financial bootstrapping is used in managing and accessing resources necessary for business development. Financial bootstrapping helps to reduce the need for financial capital or to provide alternative sources of capital. This suggests that financial bootstrapping can be of significance to rural small businesses in two ways. (1) It can reduce the need for external finance and (2) it can provide alternative sources of resources (Padachi et al., 2012). Owners' demographic characteristics such as the level of education and gender can influence the financial decisions and performance of firms (Rauch & Frese, 2007; Neeley & Van Auken, 2010; Isaga, 2015). A review of the empirical literature on rural entrepreneurship in South Africa (Pooe & Mafini, 2012; Mugobo & Ukpere, 2012;

Arko-Achemfuor, 2012) and financial bootstrapping strategies of SMEs (Pretorius, 2007) revealed that no study has investigated the effect of owners' demographic characteristics on the financial bootstrapping methods employed by rural small businesses.

Objectives of the Study

The objectives of the study are: To investigate the financial bootstrapping strategies used by rural SMEs To examine if there is are significant differences in the financial bootstrapping methods used by rural SMEs on the basis of owners' demographic characteristics (level of education and gender).

2. Literature Review

Definition and Contribution of Small businesses in South Africa: This study will make an empirical contribution to the literature on financial bootstrapping from the context of SMEs that are located in the rural areas. The National Small Business Act of South Africa 1996 as amended in 2003 defines a small business as "a separate and distinct entity including cooperative enterprises and non-governmental organizations managed by one owner or more, including its branches or subsidiaries if any is predominantly carried out in any sector or sub-sector of the economy mentioned in the schedule of size standards, and can be classified as an SME by satisfying the criteria mentioned in the schedule of size standards" (Government Gazette of the Republic of South Africa, 2003). The Act also provides for a schedule of size standards to quantitatively define a small business as depicted in table 1.

Table1: Schedule of Size Standards for the Definition of Small businesses in South Africa

Size class	Employees (less)	Turnover less than or equal to (Rand)	Balance sheet less than or equal to (Rand)
Micro	5	0.20m	0.10m
Very small	20	4.00m	0.60m
Small	50	19.00m	3.00m
Medium	200	39.00m	6.00m

Source: Adapted from Government Gazette of the Republic of South Africa (2003).

SMEs are one of the drivers of inclusive economic growth in South Africa. SMEs makeup to 91% of formalized enterprises, provide employment to about 60% of the labor force and contribute about 34% of the gross domestic product of South Africa. One of the major challenges facing SMEs in South Africa is lack of access to resources especially external finance (Agbenyegah, 2013; Banking Association of South Africa, 2017).

Resource Dependency and Capital Structure Theories: According to Pfeffer & Salancik, (1978), the Resource Dependency Theory (RDT) argues that resources are a critical or important part of an organisation's operation. RDT focuses on how the external resources of organisations affect the behaviour of the organisation. Resources include all physical and financial assets, capabilities, and organisational. Resources can help a small business to survive, grow and gain competitive advantage (Kraaijenbrink et al., 2010). The traditional view of bootstrapping coincides with the RDT. Firms do not possess all of the resources they need and must therefore obtain resources from external parties (Ebben & Johnson, 2006).

Capital structure is described as the mix of debt and equity that a firm uses to finance its operations. Capital structure theories (Modigliani & Miller, 1958, 1963; Jensen & Meckling, 1976; Myers, 1984) focus on how firm access and use debt and equity finance. Small businesses in South Africa face difficulties in accessing debt capital. The rejection rate of credit applications by commercial banks is very high (Mahembe, 2011; Andreea & Aiga, 2012; Fin Mark Trust, 2015). In addition, small businesses have difficulty accessing funds from equity providers such as business angels and venture capitalists ((Baldock & North, 2012). Thus, there is both a debt and an equity gap in small business financing (Balogun et al., 2016). The debt and equity gap is most prevalent in rural small businesses because of their low credit rating and weak growth (Coleman & Okyere, 2016). Financial bootstrapping is one of the methods that firms can use to meet the need for resources without reliance on external equity or debt finance (Lam, 2010).

Definition of Financial Bootstrapping: Freear et al. (1995) describe bootstrap financing as highly creative ways of acquiring the use of resources without borrowing money or raising equity financing from traditional sources. Bhide, (1992) refers to bootstrap financing as the financing of ventures with modest personal funds. Bootstrap financing includes all sources of capital used after personal savings and loans from financial institutions are either exhausted or are not available, such as loans from friends and relatives, credit cards, home equity loans, life insurance, supplier credit, leases, and customer financing (Padachi et al., 2012). Bootstrapping finance allows a business to operate with minimum resources. Bootstrapping can be used as a creative financing strategy. In addition, bootstrapping can be used for the acquisition and control of resources (both tangible and intangible), and the efficient uses of those resources to finance the enterprise for growth (Vanacker et al., 2011). Ebben (2009) points out that the bootstrapping method includes a combination of techniques that reduce overall capital requirements, improve cash flow, and take advantage of personal sources of financing. Andreea & Aiga, (2012) identify thirty-two financial bootstrapping method (refer to table). The thirty-two bootstrapping methods can be grouped into the following: (1) owner financing, (2) minimising accounts receivable, (3) joint utilisation of resources, (4) delaying payments of accounts payable, (5) minimising stock, and (6) subsidy financing (Schofield, 2015).

Owners' Demographic Characteristics and Financial Bootstrapping: Hart & Wainwright, (2013) and Isaga, (2015) remark that demographic factors such as education and experience contribute to the success of entrepreneurs. Owners' characteristics affect the financial decisions and performance of small businesses. Owners' characteristics influence business decisions and may shape the bootstrap choices that entrepreneurs make (Neeley et al., 2015).

Level of Education of the Owner and Financial Bootstrapping: According to Neeley & Van Auken (2009), high level of education improves network diversity. This can enhance access to resources apart from debt or equity. The literature about the effect of the education of the owner on firm financial bootstrapping strategies is inconclusive. Schinck & Sarkar, (2012) report that low educated SME owners tend to use bootstrapping finance than their highly educated counterparts. Pretorius, (2007) finds that education does not impact on financial bootstrapping of small businesses. A high level of education can improve the knowledge of bootstrapping methods and networking by small businesses (Neeley & Van Auken, 2009; Irwin & Scott; 2010; Grichnik et al., 2014). It is hypothesised that there is a significant difference in the financial bootstrapping strategies used by rural entrepreneurs on the basis of the level of education of the owner.

Gender and Financial Bootstrapping: Kwong et al. (2012) point out those women entrepreneurs find it more difficult to access finance from commercial banks than male entrepreneurs. This can be attributed to many factors such as supply-side discrimination and debt and risk aversion. Neeley & Van Auken (2010) indicate that women tend to use their own finance and borrow from close relatives and family than men. Consequently, women are likely to use less external financing options than men. Women entrepreneurs suffer from a higher level of discouragement in applying for credit from commercial banks and higher rejection rates. Thus women entrepreneurs will have to source for unconventional sources of finance (Schinck & Sarkar, 2012). This suggests that female entrepreneurs will use bootstrap financing more than male entrepreneurs. It is hypothesised that there is a significant difference in the financial bootstrapping strategies used by rural entrepreneurs on the basis of the gender of the owner.

3. Research Methodology

The survey was conducted in the Fetakgomo Local Municipality in the Limpopo Province of South Africa. The study following the quantitative research method with a descriptive research design data was collected through the use of the self-administered questionnaire in a survey. The population for this study was all SMEs in Fetakgomo municipality. Due to the difficulty in getting a population frame of SMEs in the study area, a sample size of 230 SMEs in Fetakgomo municipality was conveniently taken. This was considered a sufficient sample size for the study to cater for the documented low response rate among SMEs. The questionnaires were given to the owners of SMEs to complete. The questionnaire had three sections (1) biographical information (2) need and access to external finance (3) financial bootstrapping methods employed. Question items included dichotomous questions and Likert scale questions. The part of the questionnaire on financial bootstrapping was adapted from Schinck and Sarkar, (2012) and Fatoki (2014).

The questionnaire contained thirty-one question items. Likert scale questions where the respondents could answer 1-5 representing “1 never use”, “2 rarely use”, “3 occasionally”, “4 moderate amount” “5 a great deal”. The Cronbach’s alpha was used to measure reliability. Data analysis included descriptive statistics, factor analysis and the T-test

Response Rate and Biographical Details: Two hundred and thirty questionnaires were distributed to rural small business owners and one hundred and four questionnaires were returned. The response rate was 45.2%.

4. Results and Discussion

Table 2: Biographical Details of the Participants

Biographical factors	Frequency
Gender	
Male	59
Female	45
Age	
Below 20	5
21- 30 years	22
31- 40 years	41
41- 50 years	16
Above 50 years	20
Level of education	
Below Matric	7
Matric	43
Diploma	25
Degree	15
Post graduate	14
Legal status	
Sole proprietorship	63
Partnership	22
Close corporation	12
Company	7
Sector	
Retail	48
Service	56
Number of employees	
No employees	15
1-4 employees	47
5-10	26
11-20	16
21-50	0
Above 50	0
Length of business operation	
Less than one year	9
1-5 years	63
6-10 years	24
11-15 years	5
Above 15 years	3

The biographical details are depicted in table 2. The results show that the majority of the respondents are males, in the 31-40 age group with matric qualification. The legal status of the majority of the respondents is sole proprietorship. In addition, the majority of the respondents are in the service sector, with one to five employees and operating for between 1 and 5 years. Thus it can be concluded that the majority of the respondents’ business are micro-enterprises. The National Small Business Act of 2003 as amended defines a

microenterprise as a business with less than five employees. In addition, the majority of the respondents' businesses can be classified as young enterprises with the business life of between one and five years.

Need for External Finance

Table 3: Need and Access to External Finance by the Participants

Statement	Yes	No
Is your contribution to your business adequate to finance your business	8%	92%
Do you require finance from commercial banks?	76%	24%
Have you applied for finance from commercial banks	68%	32%
Was your application for commercial bank finance successful?	21%	79%

92% of the respondents agree that internal finance is adequate to run their businesses. The results indicate that internal finance is often inadequate for small businesses to survive and grow. It is increasingly difficult to keep the costs within the constraints of self-financing (Mateev & Anastasov, 2011). The results also indicate that the majority of application for funding by small businesses from commercial banks is unsuccessful. Wehinger, (2014) finds that the acceptance rate of small business credit applications is very low. Thus rural small businesses need to find innovative and creative ways of obtaining resources.

Bootstrapping Methods Used by Rural Small Businesses

Table 4: Bootstrapping Methods Used by Rural Small Business Owners

Bootstrapping technique	Mean	Standard deviation
1. In my business I buy used equipment instead of new	2.50	1.307
2. I borrow equipment from other businesses for shorter periods	2.60	1.178
3. I hire personnel for shorter periods instead of permanently employing personnel	2.37	1.133
4. I coordinate purchases with other businesses	3.00	1.223
5. I lease equipment instead of buying	2.41	1.228
6. I practice barter instead of buying/selling goods	2.42	1.040
7. I offer customer discounts if paying in cash	2.62	1.185
8. I buy on consignment from supplier/s	2.89	1.105
9. I seek out best conditions possible with supplier/s	3.18	1.221
10. I deliberately delay payment to supplier/s	2.24	1.219
11. I withhold manager's salary for some period	4.05	1.109
12. I make use of my own private credit card for business expenses	4.57	1.180
13. I obtain capital via assignments in other businesses	2.39	.999
14. I obtain payment in advance from customers	2.34	1.085
15. I raise capital from a factoring company	2.47	1.004
16. I obtain loans from relatives/friends	4.29	1.121
17. I deliberately delay payment of value-added tax	1.99	.970
18. I obtain a subsidy from the County Administrative Board	2.13	1.103
19. I use routines in order to speed up invoicing	2.75	1.113
20. I use interest on overdue payment from customers	2.51	1.052
21. I cease business relations with customers frequently paying late	2.54	1.051
22. I offer the same conditions to all customers	3.20	1.257
23. I deliberately choose customers who pay quickly	2.85	1.077
24. I use routines in order to minimize capital invested in the stock	3.05	1.046

25. I employ relatives and/or friends at a non-market salary	2.45	1.190
26. I run the business completely at home	4.03	1.242
27. I share premises with others to cut costs	2.61	1.169
28. I share employees with other businesses	2.27	1.159
29. I share equipment with other businesses	2.23	1.168
30. Late payment of wages and salaries for my employees	2.13	1.094
31. I receive free consulting	1.49	.975

Table 4 depicts the results of the bootstrapping methods used by rural small business owners. The findings show that the most frequently used bootstrapping methods by rural small businesses are obtaining loans from family and friends, withholding salaries and running the business from home. The limited use of bootstrapping methods can be due to the fact that rural SMEs are not aware of bootstrapping finance. Schinck and Sarkar, (2012) report that many small business owners are not aware of bootstrapping finance.

Factor Analysis

Table 5: Rotated Component Analysis

Bootstrapping technique	1	2	3	4	5
I withhold manager's salary for some period	0.834				
I make use of my own private credit card for business expenses	0.762				
I obtain loans from relatives/friends	0.654				
I employ relatives and/or friends at a non-market salary	0.776				
In my business I buy used equipment instead of new		0.651			
I share premises with others to cut costs		0.755			
I borrow equipment from other businesses for shorter periods		0.565			
I coordinate purchases with other businesses		0.666			
I practice barter instead of buying/selling goods		0.763			
I lease equipment instead of buying			0.562		
Late payment of wages and salaries for my employees			0.634		
I deliberately delay payment to supplier/s			0.721		
17. I deliberately delay payment of value-added tax			0.543		
I hire personnel for shorter periods instead of permanently employing personnel				0.761	
I buy on consignment from supplier/s				0.631	
I use routines in order to minimize capital invested in the stock				0.853	
I seek out best conditions possible with supplier/s				0.640	
I obtain capital via assignments in other businesses				0.533	
I offer customer discounts if paying in cash					0.774
I obtain payment in advance from customers					0.636
I use routines in order to speed up invoicing					0.863
I use interest on overdue payment from customers					0.622
I cease business relations with customers frequently paying late					0.773
I offer the same conditions to all customers					0.674

I deliberately choose customers who pay quickly					0.776
Eigen value	45.643	9.301	6.211	4.563	2.771
% of variance explained	47.533	20.654	12.774	8.665	4.551
Cronbach's alpha	0.751	0.832	0.744	0.765	0.775

Items with factor loading less than 0.300 removed

Table 5 shows the results of the component analysis. Five factors were identified by the factor analysis. Factor 1 is labelled as owner's finance. Existing literature identify financial resources as one of the most pressing challenges for small businesses. Factor 2 is labelled as joint utilisation and consists of five items. These are innovative measures used by the business to cut costs by sharing the burden of costs. This involves items such as buying used equipment, sharing premises, borrowing equipment, coordinating purchases with others as well as embarking on barter trade. Factor 3 is labelled as identified as delaying payments. This factor consisted of 4 items such as: leasing equipment instead of buying, late payment of wages and salaries for my employees, deliberately delaying payment to supplier/s and delaying payment of value-added tax. Factor 4 is labelled as minimising investment and consists of five items. Cutting down unnecessary costs increases the firm's profitability. Factor five is identified as minimising accounts receivables. Accounts receivables form a crucial part of the working capital of any business. The findings are inconsistent with the results of the study by Schinck & Sarkar, (2012) which reported that low educated SME owners tend to use bootstrapping finance than their educated counterparts. However, a high level of education can improve the knowledge of bootstrapping methods and networking by small businesses (Neeley & Van Auken, 2009; Irwin & Scott; 2010; Grichnik et al., 2014).

Gender Difference

Table 6: Gender Difference in Financial Bootstrapping Strategies

Factor	Female	Male	t- statistic	Sig level
Owner financing	3.453	3.835	1.65	0.01
Joint utilisation	1.665	1.775	1.43	0.03
Delaying payments	1.475	1.133	1.02	0.76
Minimisation of investment	1.236	1.156	0.45	0.01
Minimisation of receivables	0.472	0.761	0.87	0.26

Sig 0.05

Table 6 shows a gender difference in the financial bootstrapping strategies used by rural small businesses. There are significant gender differences for three factors. These are owner financing, joint utilisation and minimisation of investment. Considering each factor, males tend to use more of owner financing than females. In addition, the results indicated gender differences for joint utilisation. However, considering minimisation of investments, females have a higher mean than males. The results are consistent with the findings of Jayawarna et al. (2012). The study found gender differences in some of the measures of financial bootstrapping. Males engage in more payment-related bootstrapping activities than females. Gender differences are significant in the working capital such as obtain payment in advance from customers, delay payments to suppliers and speed up invoicing.

Level of Education Difference

Table 7: Level of Education Difference in Financial Bootstrapping Strategies

Factor	Matric and below	Tertiary qualification	t- statistic	Sig level
Owner financing	2.561	3.754	1.61	0.03
Joint utilisation	1.632	1.754	0.76	0.26
Delaying payments	1.264	1.264	1.43	0.33
Minimisation of investment	0.268	0.257	0.66	0.54
Minimisation of receivables	1.733	1.863	1.63	0.02

Sig 0.05

Table 7 depicts the results of the t-test for the level of education educational difference. The results show that educational level is significant on two factors: owner's financing and minimisation of account receivables. Considering the owner's financing it can be deduced that people with tertiary qualifications tend to use their own funds more than those with Matric and below. Delayed payments and minimisation of investments do not show a significant difference. This is consistent with Pretorius, (2007) finds that the level of education does not impact on financial bootstrapping of small businesses.

5. Conclusion and Recommendations

The rural areas of South Africa face many development challenges. These include high rates of unemployment, poverty and crime. The growth of the small businesses is one of the solutions to the challenges faced by rural areas in South Africa. Rural small businesses have a high failure rate. One of the principal causes of failure is inaccessibility to external finance. Financial bootstrapping is a method for meeting the need for resources by firms without reliance on long-term external finance from equity or debt holders. The study investigated the financial bootstrapping strategies used by rural small businesses. In addition, the study examined if there is a significant difference in the financial bootstrapping methods used by rural small businesses on the basis of owners' demographic characteristics (level of education and gender). The findings show that the most frequently used bootstrapping methods by rural small businesses are obtaining loans from family and friends, withholding salaries and running the business from home. The results indicated a significant gender difference in some of the bootstrapping techniques. Furthermore, the results showed that educational level is significant for two bootstrapping techniques. These are owner's financing and minimisation of account receivables. The findings of the study indicated significant gender differences for some of the bootstrapping techniques. The government has a huge role to play to in providing finance and information to rural small businesses. It is recommended that the government embark on a heavy awareness campaign specifically targeted at rural male and female small business owners. In addition, government agencies such as Small Enterprise Development Agency (SEDA) and Small Enterprise Finance Agency (SEFA) among others should conduct a series of workshops to enlighten both male and female small business owners about financial bootstrapping. The findings of the study indicated that the level of education affects financial bootstrapping. Rural small business owners should improve their knowledge of financial management. Rural small business owners should be proactive and attend training on small business finance organised by universities, government agencies and non-governmental organisations that support entrepreneurship.

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