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Innovative mechanisms to improve access to funding for the black-owned small and medium enterprises in South Africa

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Background: Small and medium enterprises (SMEs) in South Africa and globally struggle to gain access to external funding. The current lending instruments used by the banks are more suitable for large enterprises than for SMEs. Financially constrained SMEs are less likely to contribute to economic growth and job creation. Small and medium enterprises in South Africa are expected to create 90% of the 11 million jobs as per the National Development Plan.

Aim: The objective of this study was to deliver innovatively designed funding mechanisms through which improved access to external funding can be achieved.

Setting: Participating stakeholders in this research were entrepreneurs and suppliers of funding, policymakers and experts.

Methods: The purposive sampling method was used in this study where 24 in-depth interviews were conducted, and 160 survey questionnaires were recorded. Mixed-methods approach was used to incorporate both qualitative and quantitative techniques. A literature review related to entrepreneurship and capital structure theories was conducted. Thematic and statistical graphical data analyses were applied in both the qualitative and quantitative data, respectively.

Results: The critical findings of this study are the blended SME funding model and the SME risk reduction model. Designing the lending instruments in a way that blends both private and public financial resources increases the risk appetite on the side of the private lending institutions.

Conclusion: The proposed model requires more improved public–private partnerships. Furthermore, the findings include the need for supportive regulatory framework and embracing alternative emerging technology-enabled funding options.

Keywords: entrepreneurship; small and medium enterprises (SMEs) funding; blended SME funding model; funding gap; SME financing.

Introduction

The positive relationship between entrepreneurship and economic growth has been confirmed by previous research work (Bowmaker-Falconer & Herrington 2020; Saberi & Hamdan 2018). In recognising the job creation power of a thriving small and medium enterprise (SME) sector, the South African government has established a dedicated national Department of Small Business Development (DSBD) with the aim of fostering sustainability and growth of SMEs. Furthermore, the government has set an ambitious target of creating 11 million jobs by 2030, of which 90% are to be created by the SMEs (National Planning Commission 2011). South Africa records a higher SME discontinuity rate compared to established enterprises (Bowmaker-Falconer & Herrington 2020), casting a doubt on the feasibility of the job target set by the government. According to Statistics South Africa (2021), the unemployment rate is recorded at 34%. Regrettably, SMEs in South Africa face constraints such as highly competitive market environment, insufficient government support, non-supportive government policy and regulatory framework, funding gaps and corruption (Mistra 2020; Mutoko et al. 2017; Trade & Industrial Policy Strategies [TIPS] 2017).

The lack of access to external funding as a constraint hits hard on black-owned SMEs (Mutoko et al. 2017). Bowmaker-Falconer and Herrington (2020) posit that access to funding for start-ups is a global phenomenon. Only well-established older enterprises have a higher bank fundability likelihood (Erdogan 2019). The bank's assessment of the enterprise's financial performance relies heavily on hard information such as the financial statement (Erdogan 2019). The government's plan to address market failure through the establishment of Small Enterprise Finance Agency (SEFA) is yet to make considerable impact. Some of the government-run SME support programmes provided by the National Youth Development Agency (NYDA) are said to be ineffective (Bowmaker-Falconer & Herrington 2020).

The objective of this article was to demonstrate how the blended SME funding model provides options to close the already identified funding gap. The rest of the article is structured as follows: literature review, methodology, findings of the study, analysis and conclusion.

The funding gap

According to Omer (2016), SMEs also fail to access external financing as a result of mismatches between demand and supply. South Africa does not have a shortage of funding instruments, but there is a lack of innovation in the development of lending tools (Visser 2019). According to Visser (2019), the funding gap in South Africa is estimated to be between R86 billion and R346bn. Although funding is available in South Africa (Bowmaker-Falconer & Herrington 2020; Visser 2019), SMEs fail to meet the funder's requirements given their inability to prove creditworthiness, present collateral and high-failure rate associated with start-up infancy stage (Rao et al. 2021). The high prevalence of information asymmetry-related problems in the SMEs exacerbates the situation (Erdogan 2019). Existing empirical evidence proves the existence of correlation between lack of access to external finance and lack of SME growth and development (Rao et al. 2021).

Small Enterprise Finance Agency, NYDA and other governmental institutions employ inefficient models, and hence they are less impactful on the ground (Bowmaker-Falconer & Herrington 2020; Mistra 2020). The lack of access to external funding is said to be the contributor to the high business discontinuity rate in South Africa (Maduku & Kaseeram 2021).

This study's specific objectives were:

1. to identify the factors contributing to SME failure in South Africa,
2. to examine SMEs and entrepreneurship funding models with respect to how the models can address the funding gap in South Africa,
3. to identify the factors enabling SME funding in South Africa,
4. to propose a new SME funding model with a view of closing the funding gap.

Addressing the funding gap has the following benefits, namely, increased participation of black South Africans in the main economy, hence the achievement of economic transformation, and increased SME Gross Domestic Product (GDP) contribution and employment creation. The blended SME funding model is seen as an option to close the funding gap.

Literature review

This section deals with literature review on entrepreneurship and capital structure theories.

Entrepreneurship

According to Hisrich et al. (2019), the word 'entrepreneur' originated from the French language, and it means 'between-taker' or 'go-between'. The advancement in the entrepreneurship concept and theory can be attributed to the work of Schumpeter as cited by O'Boyle (2017). Innovation is placed at the centre of Schumpeterian entrepreneurship (Mehmood et al. 2019). Entrepreneurship bears the characteristics of creativeness, risk-taker and growth-orientated individual (Schermerhorn & Bachrach 2020).

The most recent successful global enterprises that are deemed entrepreneurial and innovative include Google, Apple, Telsa, Facebook, Paypal, Netflix and others. The rise of these innovative disruptors reduced the dominance and market share of the former industry giants such as Microsoft, Nokia, Yahoo, Kodak, print News Papers and others. Scholars have always associated entrepreneurship with uncertainty and risk because entrepreneurial value creation takes place within the context of unknowingness (Townsend et al. 2018).

The association of uncertainty and risk in entrepreneurial endeavours finds true expression in the journey of Steve Jobs of Apple and Mark Zuckerberg, the co-founder of Facebook. Steve Jobs had been previously fired by Apple, and Mark Zuckerberg was young with no previous success history. The products being delivered by both Apple and Facebook were new offerings associated with uncertainty. The situation is characterised as uncertain when the outcomes cannot be calculated or measured (Townsend et al. 2018). According to Townsend et al. (2018), a risk exists when the outcome is uncertain and yet predictable. Entrepreneurial endeavours do result in failure, even when the entrepreneuring enterprise and person in-charge have a good track record in business. Window's Vista, Ford's Edsel, Amazon's Fire Phone, the Apple Newton and many others are some of the unsuccessful entrepreneurial efforts (O'Boyle 2021). A total elimination of risk and uncertainty in entrepreneurial practice and innovations seems impossible.

O'Boyle (2017) associates entrepreneurship with a lively active and spontaneous person who has the eagerness to initiate change. Beyond profit making and achieving any success of economic value, entrepreneurship attains a greater success in improving social welfare and reduction of poverty (Mehmood et al. 2019). Small and medium enterprises are central to economic development globally (Erdogan 2019). Furthermore, Erdogan (2019) associates entrepreneurship with national positive contributions such as economic growth, employment creation and innovation. Entrepreneurship in developing economies is mostly necessity driven.

Opportunity-driven entrepreneurship is associated with market conditions whose circumstances are rich in opportunities, and necessity-driven entrepreneurship prevails in circumstances that are poorer in opportunities (Baker & Welter 2020). Entrepreneurial activity that makes a difference in society is purpose driven (opportunity driven) (Bowmaker-Falconer & Herrington 2020). Resources such as finance, skills and social networks are critical for entrepreneurial opportunity exploitation (Bowmaker-Falconer & Herrington 2020). Resource-based entrepreneurship recognises the importance of resources in detecting and pursuing opportunities. The lack of access to external finance has been described as the most significant factor because it directly influences growth and sustainability (De Prijcker et al. 2019). Financial resources are the most required for sustaining and growing an enterprise (Cummings et al. 2020).

Entrepreneurship in South Africa

South Africa is the birthplace of one of the world's greatest entrepreneurs, Elon Musk. The country has produced many other successful entrepreneurs such as Adrian Gore (Discovery Limited), Christoffel Wiese (Pepkor), Herman Mashaba (Black Lime Me) and others. South Africa's current entrepreneurial performance as reflected by empirical data paints a bleak picture (Swartz et al. 2019). The country's SME discontinuity rate was measured at 4.9% in 2019, and it was found to be higher when compared to 3.5% for established firms (Bowmaker-Falconer & Herrington 2020). Entrepreneurs in South Africa face a high level of constraints such as inadequate support, lack of access to advisory services, high cost of broadband access, skills shortage, electricity supply and unsupportive regulatory frameworks (Swartz et al. 2019).

The constraint of lack of access to external finance has been described as the most significant because it directly influences the firm's growth and sustainability (De Prijcker et al. 2019). Consequently, the SMEs' inability to access external finance regrettably negatively affects the country's productivity (Erdogan 2019). According to Bowmaker-Falconer and Herrington (2020), SMEs are the main employment creators in many societies, and they further contribute to social cohesion within local communities. The South African society has a historical, economical and social character that needs entrepreneurship's contribution in reducing the high unemployment rate and fostering social cohesion. Small and medium enterprises have an edge in employment creation when compared to large firms (Rao et al. 2021).

Within DSBD, there are support entities such as Small Business Development Agency (SEDA) and Small Business Finance Agency (SEFA). Small Business Finance Agency provides non-collateral funding, while SEDA provides non-finance support to start-ups, cooperatives and other small businesses. The SME advisory services offered by public institutions require upskilling to be more impactful (Bowmaker-Falconer & Herrington 2020).

South Africa's ratings on the national entrepreneurship framework conditions are summarised in Table 1.

TABLE 1: South Africa's score on entrepreneurial framework conditions in comparison with the Global Entrepreneurship Monitor (GEM) in 2019.

Entrepreneurial framework conditions	South Africa (2019)	GEM average (2019)
Financial environment and support	4.0	4.5
Concrete government policies related to entrepreneurship	3.5	4.3
Government policies: taxes and bureaucracy	2.7	4.0
Government entrepreneurship programmes	3.1	4.4
Entrepreneurship education (vocational, professional, and tertiary level)	3.5	4.7
Internal market dynamics	4.7	5.2

Source: Authors' compilation from Bowmaker-Falconer, A. & Herrington, M., 2020, *Igniting start-ups for economic growth and social change*, Global Entrepreneurship Monitor South Africa (GEM SA) 2019/2020 report, Stellenbosch University, Cape Town
GEM, Global Entrepreneurship Monitor.

The majority of SMEs in South Africa face survival-threatening challenges such as lack of access to markets, lack of internal recordkeeping skills and lack of competitiveness (Mutoko et al. 2017). The lack of internal recordkeeping and the inability to produce proof of financial performance reduce the SME's fundability chances. According to Erdogan (2019), financial performance is considered more credible by the banks than projected sales and future performance outlook. Mutoko et al. (2017) single out the lack of access to external finance as the major challenge and that lack of it prevents SMEs from pursuing business opportunities.

Black-owned small and medium enterprises in South Africa

Black-owned SMEs in South Africa are outperformed by well-established white-owned multinational companies (Musabayana & Mutambara 2022). According to Musabayana and Mutambara (2022), 90% of the thriving SMEs in South Africa are owned by white people. Black-owned SMEs fail because of constraints such as lack of access to external funding (Mutoko et al. 2017). When seeking funding from programmes based on Broad-Based Black Economic Empowerment (B-BBEE) such as that offered by SEFA, the black-owned SMEs regrettably face cumbersome bureaucratic processes (Musabayana & Mutambara 2022). Black-owned SMEs' failure continues despite the implementation of the B-BBEE Policy in South Africa (Mistra 2020). The B-BBEE is the tool to redress the racial and economic imbalances created by both the apartheid era and the colonial legacies. Before 1948, the then prime minister of the Cape Colony, Cecil John Rhodes, introduced the English Economic Empowerment (EEE) (Meredith 2007). According to Meredith (2007), the Afrikaans Economic Empowerment (AEE) was introduced by the National Party government in 1948. The black people were not only prohibited from operating commercial businesses but also deprived of land ownership rights among others. The failure of the B-BBEE can be attributed to the fact that black-owned businesses are expected to compete with the well-established white-owned multinationals (TIPS 2017) and that the B-BBEE deals are secured by connected politicians (MISTRA 2020).

Access to funding

Access to external funding has been repeatedly highlighted as a challenge for most SMEs (Bowmaker-Falconer &

Herrington 2020; Omer 2016). Financial resources' inadequacy within SMEs reduces their capacity to create employment, contribute to GDP growth, and be sustainable (Mutoko et al. 2017). According to De Prijcker et al. (2019), financially constrained SMEs are weakened in areas of potential growth and sustainability. The inability to provide collateral, present audited financial statements (Erdogan 2019) and information asymmetric problems contribute to SMEs' lack of access to external funding. The information asymmetry-related problems are less prevalent in larger enterprises (Erdogan 2019). Such problems lead to credit rationing, adverse selection and moral hazard-related problems (Mueller & Sensini 2021).

Small and medium enterprises that can demonstrate profitability and growth are likely to access external financing (Erdogan 2019). New and smaller enterprises have a lower fundability likelihood (Erdogan 2019). The financial environment support for the SMEs in South Africa is ranked lower than the GEM average (see Table 1). According to Visser (2019), the current funding channels inhibit even the SMEs that would otherwise qualify for funding.

Commercial banks: Sourcing external finance from the banks remains the most viable option for SMEs in both developed and developing economies (Rao et al. 2021). Dealings between private banks and SMEs confirm that SMEs are considered a riskier investment asset class (Beck 2013). The mechanisms through which banks assess the loan applications are not suitable for small businesses. Banks reject SME loan applications because of lack of credit history, lack of collateral, limited owner's contribution and doubtful loan repayment prospects (cash flow) (Erdogan 2019; Mutoko et al. 2017).

Public funding: As a way of addressing the identified market failures within the SME funding space, the government has both direct and indirect funding programmes. Direct programmes include funding instruments such as SEFA, Industrial Development Corporation (IDC) and Gauteng Entrepreneurship Propeller (GEP). Indirectly, the government has a Credit Guarantee Scheme provided by the Credit Guarantee Insurance Corporation (CDIC), incentivising private firms funding SMEs, and the support of IDC. Small and medium enterprise financial support in South Africa is rated lower compared to the GEM average (Bowmaker-Falconer & Herrington 2020). Institutions such as NYDA, SEFA and SEDA are said to be lacking meaningful impact on the ground and that they employ inefficient models (Mistra 2020).

Alternative funding options: Apart from the traditional funding options, SMEs have alternatives such as equity financing, angel investor, venture capital, crowdfunding, and asset-based and technology-influenced funding.

Equity financing functions by way of exchanging capital with equity (shareholding) for investors (Rao et al. 2021). Equity investor option does not impose monthly loan repayment obligation as it would be expected in the bank loan scenario. According to Rungani and Potgieter (2018), it is the lack of external equity that creates more dependency on debt financing. According to DeAngelo (2022), firms use equity funding for 'dry powder', which is to address future funding needs. The equity funding option and other private lending options are among the least preferred in South Africa (Bowmaker-Falconer & Herrington 2020). Theoretically, the Pecking Order Theory (POT) explains why SMEs prefer the use of internal resources and debt options over equity (Rao et al. 2021). Internal earnings remain the default form of equity within the South African SMEs sector (Omer 2016). More assuring and friendly legal and policy frameworks are required for this option to be embraced (TIPS 2017).

The survey results of a study conducted during 2019 showed the private lender funding (including crowdfunding) option receiving the lowest score (3.3 which is lower than 3.9 awarded to government subsidies) among other sources of funding in South Africa (Bowmaker-Falconer & Herrington 2020). According to Rungani and Potgieter (2018), venture capital option is not accessible to newly established SMEs.

Regulatory framework in South Africa

In a free market economic setup, the government plays a regulatory role. South Africa was ranked 60 out of 141 economies on the Global Competitiveness Report of 2019 (World Bank Doing Business Report 2020). The Report showed South Africa's decline in the burden of government regulations (to 101 out of 141) and the time required to start a business (to 129 out of 141) rankings (Bowmaker-Falconer & Herrington 2020). South Africa scored 2.7 against the GEM average of 4.0 on the entrepreneurial framework conditions measuring government policies: taxes and bureaucracy (see Table 1).

The South African labour laws are not favourable to the SME sector (TIPS 2017). The SMEs must pay the nationally set minimum wage and follow protracted Commission for Conciliation, Mediation and Arbitration (CCMA) processes when firing employees. Furthermore, there are provisions of the *Public Finance Management Act* of 1999 (PFMA) that impede B-BBEE promotion. Section 51 (a) (iii) of the PFMA requires that the organs of the state must run a tender process that is fair, equitable, transparent, competitive and cost-effective. Lastly, SMEs find it difficult to comply with the burdensome tax system (TIPS 2017).

Capital structure

Capital structure is defined as the mix of debt and equity in an enterprise to finance projects and operational requirements (Hirdinis 2019). The Modigliani and Miller theory (also known as the 'MM' theory), Trade-off Theory (TOT), POT and Agency Theory are the dominating theories within the capital structure debate.

Modigliani and Miller ('MM') theory

The 'MM' theory was developed in 1958 by Modigliani and Miller (Simiyu et al. 2019). According to Simiyu et al. (2019), Modigliani and Miller made propositions based on assumptions of an existing perfect market environment wherein firms operate without paying any corporate tax fee. Furthermore, it assumed the non-existence of information asymmetric and agency-related costs (Simiyu et al. 2019). A revision was made during 1963 wherein 'MM' acknowledged the corporate tax advantage associated with the debt financing option. Leveraged firms enjoy tax deductible benefits on the interests (Simiyu et al. 2019).

The 'MM' theory with its imperfections must be credited for stimulating theoretical arguments and debates which produced other theories such as the TOT.

Trade-Off Theory

The origins of the TOT are traced back to the collective theoretical work produced in response to the claims and arguments of 'MM' theory.

The TOT posits that firms in their financing decisions seek to maintain an optimal debt ratio, thereby achieving a balance between debt tax benefits and bankruptcy risk exposure (Mueller & Sensini 2021). According to Siljander (2018), SMEs have higher bankruptcy risk exposure than it is for larger enterprises. On the tax benefit debate, TOT arguments may not apply in the South African context where SMEs already enjoy tax benefits and that the cost of debt is unreasonably high. Still, the reality is that most profitable firms are reluctant to take on debt and use retained earnings for funding (Siljander 2018). It is argued in the TOT theory that a firm in a weaker financial position is likely to opt for bank debt financing (Simiyu et al. 2019). The TOT focused primarily on debt-equity ratio and ignored the funding and hold (DeAngelo 2022). According to DeAngelo (2022), optimisation of debt-equity ratio is a narrow problem compared to access to funding for purposes such as project financing, operating income shortfalls and distributions to bond holders. Furthermore, the TOT failed to address the profit and leverage invasive relationship (DeAngelo 2022). DeAngelo (2022) provides the profit and leverage invasive relationship explanation in the baseline model – stating that firms prefer to self-fund internally the initial investment outlays.

Pecking order

Pecking order theory posits that firms set a hierarchy that follows an order of funding options preference – internal, debt and equity as a last resort (Simiyu et al. 2019). According to Hirdinis (2019), POT argues that profitable enterprises prefer the use of internal financing resources compared to seeking external finance as a way of averting costs associated with information asymmetry. The firm develops a financial policy setting out the preferred option, hence reducing the information asymmetry-related costs (Adair & Adaskou 2015). Pecking order explains a firm's general tendency to prefer internal over external financing and to prioritise debt over equity (DeAngelo 2022). The prioritisation of internal financing is motivated by the need to reduce or avoid information asymmetry-related costs (Simiyu et al. 2019). The applicability of the POT theory within the financially constrained SME is questionable.

Agency theory

Agency theory argues that owners of the firms appoint managers who act as the owner's agents in the day-to-day management of the business (Simiyu et al. 2019). The conflict of interest results in problems referred to as 'agency costs', originating from information asymmetry, moral hazard and adverse selection-related problems (Erdogan 2019; Mueller & Sensini 2021). In SMEs owned by two persons and more, information asymmetry problems are lower compared to a single person-owned firm (Erdogan 2019). Agency-related problems can result in credit rationing.

Methodology

A multi-stakeholder integrated view was deemed necessary to achieve the study objectives; hence, an ethnographic design using mixed-methods research approach was adopted. A purposive sampling strategy was employed to collect data using semi-structured in-depth interviews. There is no institution in South Africa that has a full database of all SMEs. Therefore, a non-probability sampling method was used to sample about 30 participants representing the identified stakeholders listed in Table 2. Marshall et al. (2013) recommend a size of between 20 and 30 for grounded theory development studies. Qualitative studies are associated with a small sample size (Saunders et al. 2016). Table 2 represents the interview participation report.

There were 24 interviews conducted, representing 80% of the targeted sample of 30. Of the interview participants, 75% were men while 25% were women. The participating entities recommended participants based on their expertise on the subject, and gender representativity was a priority importance. Thematic data analysis was applied to the interview transcripts. Interviews were digitally recorded. The interview recordings were converted to text (transcripts). The analysis involved repeated readings of the transcripts in order to identify the codes. Coding identifies and groups data having similar meanings (Saunders et al. 2016). A total of 391 codes were generated, grouped and categorised, which produced the themes presented in the findings section. The themes emerging from the data constituted the elements that were utilised to build the blended SME funding model.

TABLE 2: Interview participation report.

Participating stakeholder group	Number of participants	%
Entrepreneurs/SME owners	6	25
Developmental financing institutions	7	29
Private funding intuitions	4	17
Government and SOEs	6	25
Research and academic	1	4
Total	**24**	**100**

SME, Small and medium enterprises; SOE, state-owned enterprise.

A survey questionnaire was designed and administered for the purpose of validating the emerging model. The questionnaire was electronically sent to both entrepreneurs and non-entrepreneurs. Small Enterprise Finance Agency and GEP distributed the questionnaire to the SMEs on their database. The questionnaire was also sent to non-entrepreneur participants. It was deemed unethical to collect qualitative data from both the entrepreneurs and non-entrepreneur participants and then only ask the non-entrepreneur participants to validate it. About 160 questionnaire responses were received. Statistical analysis was performed on the qualitative data to inform the conclusions of this study (see 'Statistical Analysis' section). This research was conducted in compliance with the conditions set by the UNISA School of Business Leadership Research Ethics Review Committee. For both qualitative and quantitative data collection methods applied in this study, pilot tests were conducted as a way of ensuring validity and reliability.

Ethical considerations

Ethical clearance to conduct the study was obtained from the UNISA Graduate School of Business Leadership Research Ethics Review Committee (GSBL CRERC), reference number: 2020_SBL_DBL_037_FA.

Research findings and discussion

This section presents the results (themes) emerging from the study. The themes are, namely, the causes of SME failure in South Africa, factors enabling SME funding in South Africa and factors enabling SME success in South Africa.

Theme 1: Causes of small and medium enterprises failure in South Africa

The semi-structured interview-collected data revealed the following SME constraints: non-availability or inadequate SME support structures, high dominance of survivalist entrepreneurial culture, entrepreneurial skills shortage, poor public–private partnerships and unsupportive policy regulatory framework. In the extract below, an interview respondent mourns about the unsupportive regulatory framework:

> 'What Preferential Procurement Policy Framework Act (PPPFA) says is that when you want to issue a tender, you need to go to the open market – you need to be fair and transparent … give everyone a fair opportunity. Even those who were not part of the enterprise development programme must be given a fair chance. What happens is that the SMEs do not have a network, a consortium where they can get the goods cheaper. The big companies buy the goods cheaper. SMEs lose out on tenders because the price is used [*as*] a determining factor.' (P15, female, SOE official)

Both public and private institutions provide B-BBEE-inspired support programmes and opportunities to SMEs aimed at addressing the constraints. The respondents viewed the current non-financial support programmes as generic, less impactful and implemented just to fulfil the requirements. Despite being under-resourced and inadequate, the current SME support structures are mainly centred in urban and developed towns and cities. Start-ups and entrepreneurs require access to support and advisory services from the infancy stages and through the entrepreneurial journey. The following excerpt provides evidence regarding this:

> 'The support services must be prescribed and provided on case to case basis. For an example, an entrepreneur from a family that has never had a million rands is likely to require serious financial management support and mentorship in financial decision-making.' (P9, male, private equity and academia)

The support services also include mentorship, advisory services, product licensing and registration, accounting services and access to funding. Currently, the private enterprises implement B-BBEE policies and programmes, such as Enterprise Supplier Development (ESD) programmes just for compliance and not in the spirit of achieving the intended objectives of empowerment and transformation. A lack of real success in implementing support programmes leaves the SME sector dominated by survivalists.

The high dominance of survivalist entrepreneurial culture is associated with non-business formalisation and non-recordkeeping. The study data revealed a low level of entrepreneurial spirit in South Africa. Mainly, skills deficiency is reported in areas such as technology, business management, recordkeeping, market research, marketing, and general operations that require interventions. The entrepreneurial and SME support programmes offered by government and its entities are poorly collaborated. Because of the lack of skills and practical business experience, entrepreneurs are unable to communicate identified profitable business opportunities and exploitation strategies in the business plans when applying for funding.

The rejection of SMEs' funding applications is largely owing to their failure in meeting the funder's requirements, presenting a unbankable business case and high risk associated with the enterprise and/or the owners. Small and medium enterprises find it costly to commission professional firms to produce the enterprise's audited financial statement as well as the business plan. Even when the business plan has been compiled by a professional, some entrepreneurs fail to internalise and articulate the content of the document during the interview with the funding institution investment official. The low level of opportunity-based entrepreneurs contributes to the submission of non-bankable business plans that are rejected by the funding institutions.

Theme 2: Factors impeding small and medium enterprises funding in South Africa

As revealed in the interview data, the three key reasons why suppliers of external funding decline the SME funding applications are failure to meet the requirements, non-bankable business case and high-risk profile. Further, there are underlying factors on both the demand and supply sides. On the demand side, the prevailing survivalist entrepreneurial practice is associated with non-recording of the enterprise's financial and operational information. The entrepreneurs are, therefore, unable to adequately complete the business loan/funding application. On the supplier side, the SME's loan applications are subjected to similar loan assessment measures applied to large enterprises, the government funding institutions lack capacity and employ lengthy loan assessment processes, and the banks are more strict and less flexible when applying the rules:

> 'A practical case is the group of medical doctors in the province of Gauteng who came together and created a warehouse and distribution centre. In this initiative, the group of medical doctors were not satisfied with the transformation happening at their medical suppliers and therefore created their own medical supply warehouse distribution centre. At the time of the application, the warehouse did not meet all requirements to attract funding. Key mandatory requirements included being operations, licensed and meeting cooling (air-conditioning) requirements… A decision to fund the initiative was taken on the bases that the doctors themselves were both the distributors (suppliers) as a group and market (customers) as individual doctors. If strict rules for business loan application were followed without the willingness to analyse the application differently, the opportunity to support transformation would have been missed. Entrepreneurs/SME business loan application come in different shapes and forms, when rules are applied, it is easy to disqualify cases with great potential. SMEs are diverse and require flexibility in handling their loan applications.' (P18, male, bank official)

The participants lack developmental and transformation mindset within the private lending institutions. Public funding institutions lack the capacity to timeously assess loan applications and conduct monitoring and evaluation of contracts:

> 'Government agencies do not only lack practical impact on the ground, they yield characteristics of strategic deficiency. While it is being said that the success of entrepreneurship in the country is negatively affected by lack of entrepreneurial skills within the entrepreneurs, it must be admitted as a reality that the lack and mismatch of skills in the operations of government agency bears equal blame.' (P12, male, DFI official)

The survey results revealed that about 63% of SME funding applications are submitted to public funding institutions, while 37% are submitted to private funding institutions. It must be declared that the numbers may be skewed given the fact that the participation sample was sourced from a government funding institution.

The survey results revealed that 63% of the SMEs applied for 250 000 while 37% applied for R250 000 and less. In terms of processing funding applications, only 13% submitted at public funding institutions are processed within a month. In contrast, the banks complete 56% of the submitted applications within a week. Public funding institutions deal with the bulk applications that are not filtered through a pre-qualification computer system applied by the banks. Further, public funding institutions centralise approval delegation for funding application to the central committee. This is consistent with the survey results of a study conducted in 2019 where respondents with previous dealings with the NYDA rated it as an ineffective method (Bowmaker-Falconer & Herrington 2020).

Theme 3: Factors enabling small and medium enterprises funding in South Africa

Factors that enable SME funding were found to be influential to SME's success. According to Rao et al. (2021), financially leveraged SME's growth translates into the broader societal economic growth. The interview-collected data revealed the SME success factors as being improved access to entrepreneurship and SME value chain support structures, competent entrepreneurs, formalised partnerships between private and public role-players, flexible and accessible business loan application processes, compelling business case documents, blended funding programmes, efficient and capacitated government agencies, better contract conditions, dedicated SME banking services and alternative funding options and effective communication on the side of the agencies.

Access to market and easily accessible SME support services enable SMEs to meet the funder's requirements, thereby presenting contracts with the clients and audited financial statements. Non-financial support services incorporated within the collaborated partnerships between private and public partnerships such as mentorship and business incubation are also very critical success and funding enabling factors. The success of the Credit Guarantee Schemes (CGS) and the proposed blended SME funding model depends on improved public–private collaborations.

On the establishment of SME support structures, the survey results indicate support of 58.8% strongly agree, 36.3% agree and 5% neutral. The support for the establishment of structures is consistent with Bowmaker-Falconer and Herrington (2020). According to them, entrepreneurs in urban, townships and rural areas need improved access to networks, mentorship services and other related advisory services. Most support structures are currently located in urban and developed towns in South Africa, leaving the rural communities isolated. According to Saberi and Hamdan (2018), the Gulf Cooperation Council (GCC) countries established business incubation centres to afford entrepreneurs with new business ideas support to turn ideas into profitable projects. Even as the entrepreneurial skills improve as a result of tailor-made training, mentorship and business incubation services, entrepreneurs need dedicated funding institutions focusing on SMEs.

In their funding application, the SMEs need to clearly demonstrate how they will create and capture value from the identified business opportunity, and the ability to service the loan. The interview extracts below provide evidence:

> 'It is within this "prospective test" that the issue of commercial viability of the business is scrutinised to the detail. Because the first line of defence is unfortunately NOT the precious cash and income generation capacity and asset-base (which can be offered as security), however, it is the prospective "probability" of the business idea that would generate future income and cashflows

which the Funder can rely on for the repayment of loans advanced.' (P10, male, private equity)

The respondents further suggested that government funding institutions should be capacitated and that the loan approval delegation for R250 000 (requested amounts) should be decentralised to the provinces and regions. Central credit database for SMEs should be created for ease of credit rating. Paperwork for small amount loans should be reduced to a 10-page document.

Theme 4: Factors enabling small and medium enterprises success

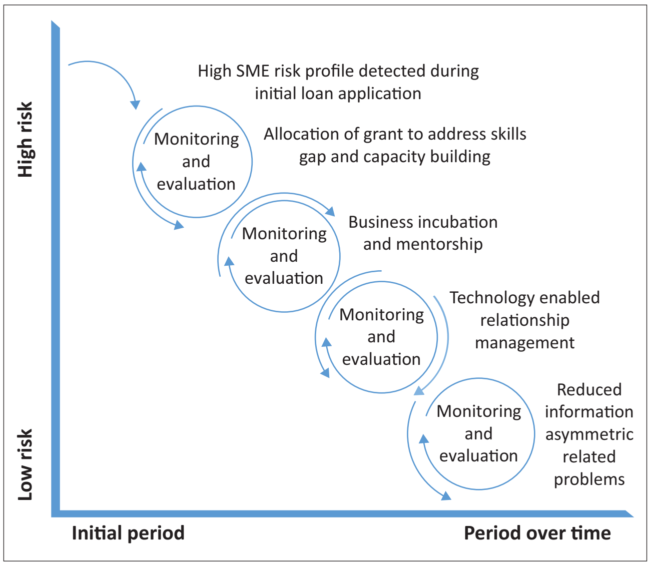
The theme of SME success factors theme highlights the need for improved access to external funding, locally based accessible entrepreneurship/SME value chain ecosystem, formalised collaborative and partnerships, and the supportive policy and regulatory framework. This is evidenced by the following excerpt:

'We need to have structured incubation hubs in every province and every township. The incubators must have a number of pillars that govern and dictate the support of survives that they support to young people. Infrastructure that you would not have access to such as office space, broadband, accounting services and other support services.' (P8, male, private equity expertise)

Data collected in this study exposed how unfriendly the policy and regulatory framework are to the SME community. Other previous research works had similar conclusions about the policy and regulatory framework in South Africa (Domeher et al. 2016; Mistra 2020; TIPS 2017). According to TIPS (2017), the South African labor laws are not favourable to the SME sector, and labour laws and the tax system are burdensome. To create a conducive environment for the alternative funding options discussed earlier in this article, fundamental changes and strengthening of the laws are required, hence embracing crowdfunding, non-fixed assets recognition as collateral and improved collaboration between private and public institutions.

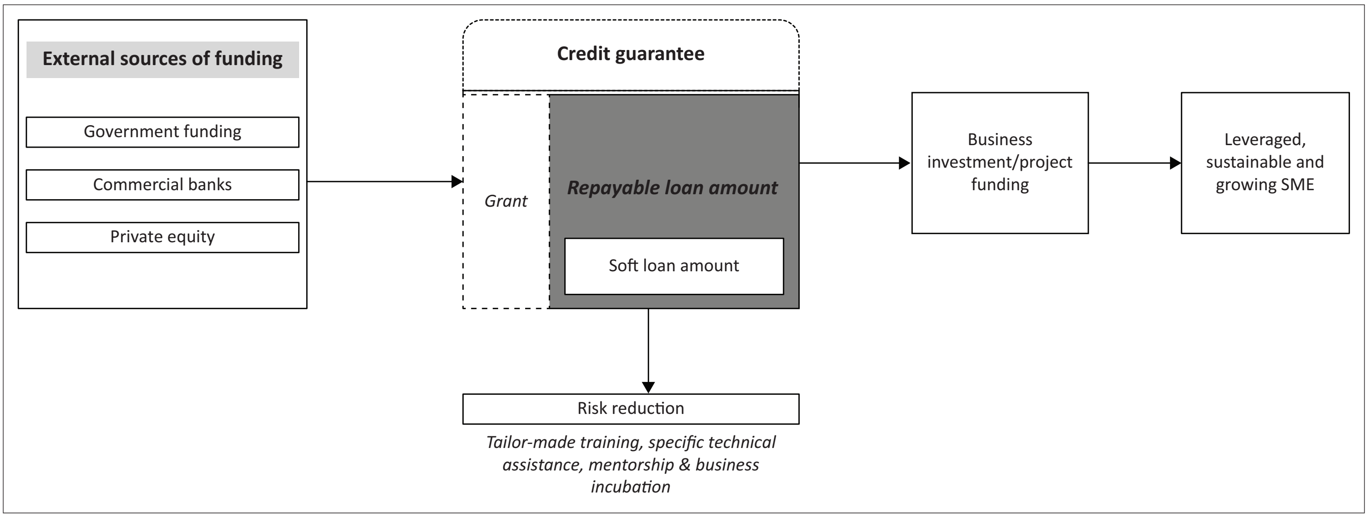
Small and medium enterprises funding risk reduction and mitigation process model

Literature on entrepreneurship associates entrepreneurial practice with uncertainty and risk (Townsend et al. 2018), and a tailor-made risk reduction and mitigation model is proposed. The provision of non-financial support services through private–public partnerships leads to the reduction of SME risk rating and improved skills levels (Saberi & Hamdan 2018). Therefore, risk must be regarded as the ever-present factor in entrepreneurship. This article proposes the SME funding risk reduction and mitigation process (see Figure 1). The SME high-risk proposition emanates from asymmetric information problems, low



SME, Small and medium enterprises.

FIGURE 1: Small and medium enterprises risk reduction process.



SME, Small and medium enterprises.

FIGURE 2: Blended small and medium enterprises funding model.

entrepreneurial skills, previous business history and others.

Flexible funding approach requires that SME funding requests should be assessed differently from the approach applied to large enterprises. This research encountered SME success stories that would have been otherwise not possible if it was not for developmental mindset and flexible and innovative funding approaches. Technology offers the opportunity to monitor the performance of SMEs and business account 24/7. Therefore, traditional agency costs associated with monitoring get reduced significantly. Furthermore, the government's commitment and allocation of CGS budget enable the private sector lending institutions to extend funding to SMEs with a high-risk profile. Working with the broad business community, the grant can be used to provide tailor-made training, business incubation and mentorship programmes. Furthermore, technology enables mentorship engagements to be conducted virtually and reduces costs significantly.

Blended small and medium enterprises funding model

Generally, blended finance is an instrument for attaining developmental objectives through the use of public and private funding (ODI 2019). Through this approach, successes in Asia and sub-Saharan Africa have been realised, where either public or private funding would not have succeeded individually (Convergence 2019). The risk would be too high for private funding to invest and the public (government) would have insufficient budget to achieve the project. According to Havemann et al. (2020), the funds committed by the government overturn risk–return perception and appetite for private funding suppliers. According to ODI (2019), blended finance is only possible where there are compelling measurable developmental goals to be achieved, government-allocated concessionary budget and commercial risk–return-oriented funding. Commercial funding is only attracted to the blended setup by the concessionary capital provided by public funding (ODI 2019)

In this regard, blended funding is the structuring of capital in a way that offers an option to close the funding gap for the purpose of meeting South Africa's developmental goals. Instead of only having the mix of debt and equity in the equation, the model brings in the third element, which is 'grant'. Grant covers funding for technical skills upgrading, mentorship and business incubation. In a traditional blended finance arrangement, it would only be debt and equity in the mix (Havemann et al. 2020). The South African government has already established SEDA to provide non-financial support programmes to SMEs. Small Business Development Agency can be regarded as the 'grant' element of the blended funding model, except that the support services offered by SEDA are not tailor made.

The reasons why SMEs are declined funding have already been reported earlier in this article. The blended funding model presents an opportunity to eliminate and mitigate the risk significantly, hence providing funding access for SMEs. Government-provided CGS can be regarded as the traditional collateral as requested by the banks. Some business ideas are not profitable almost immediately, and government grant will certainly assist with cashflow requirement to sustain the business. Small and medium enterprises doing business with government in South Africa often complain about non-payment of invoices even after 30 days which the government has committed to pay within. Grants will aid SMEs when cashflow streams dry while they wait for payments.

The measurable objectives to be achieved through the blended SME funding model include increased SME fundability, cashflow stability, increased profitability, low-risk profile and improved SME success rate. South Africa needs a thriving SME sector that creates jobs and contributes to both GDP growth and inclusive economic growth. Collaborative partnerships between the government and the private sector are important for the success of the blended SME funding model.

Figure 3 demonstrates the overwhelming support of the blended SME funding model by the survey participants. Combined responses between strongly agree and agree responses make up 87%. Strongly agree responses account for 54% of the responses, while agree responses constitute 33%.

Further analysis on the responses of both entrepreneurs and non-entrepreneur survey respondents is demonstrated in Figure 4.

The combined strongly agree and agree responses for both entrepreneurs and non-entrepreneurs are 85% and 95%, respectively. The survey results show strong support for the blended SME funding model.

Statistical analysis

By design, the data collected in this study would not suit the full statistical analysis. A Likert-scale questionnaire was designed and administered for the purpose of validating the

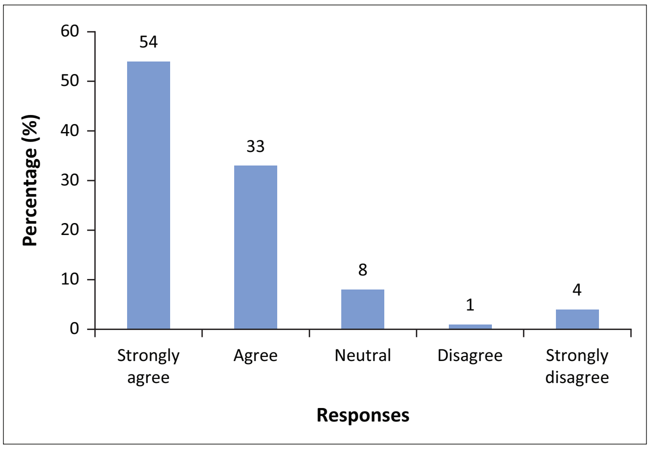
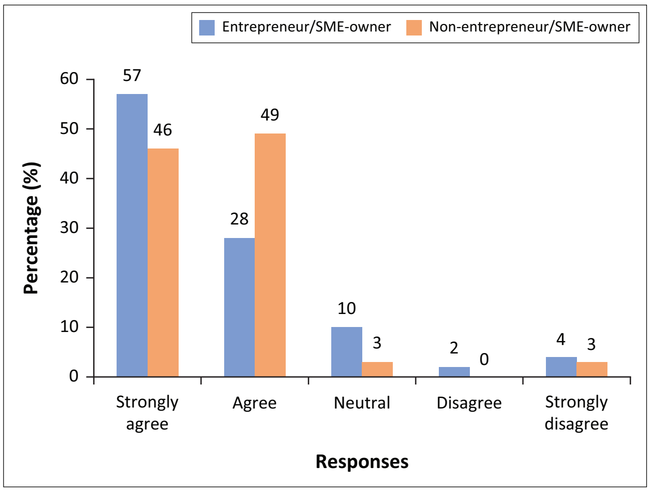


FIGURE 3: Blended small and medium enterprise (SME) **funding model will improve both access to funding and enterprise success.** Survey results – Blended SME funding model support 1.



SME, Small and medium enterprises.

FIGURE 4: Survey results – Blended SME funding model support 2.

results of the qualitative phase of the study. Specific questions targeted certain responses. For example, questions regarding loan application assessment and approval procedures within the government funding institutions would not be responded to by the entrepreneurs.

Three factors emerged from the rotated factor loading Statistical Package for Social Sciences (SPSS) software results depicted in Appendix 2. Factor 1 found relatedness in the instruments measuring the use of contracts with the intention to foster fundability in the absence of collateral and encourage the SME to make monthly savings, confirming that most entrepreneurs require upskilling in financial, operational competency and others, linking collaborative partnerships between private and public sector institutions with the establishment of entrepreneurship support structures in all the nine provinces of South Africa. Furthermore, the need for internal technological capacity building for account monitoring at the public funding institutions is also associated with the instrument measuring the validity of the blended funding model.

Factor 2 found relatedness in the introduction of a common business plan, decentralising the delegation of authority to the regions and provinces for the approval of SME loan applications asking for R250 000 and less at the public funding institutions and the need to introduce virtual training. The final factor comprises instruments measuring the need to reduce paperwork for the SME loan applicants asking for R250 000 and the confirmation that SMEs find it difficult to meet the requirement of submitting audited financial statements during the loan application. Individual Likert scale results for these instruments are covered in Appendix 1. The statistical analysis results further confirm the elements of the blended funding model as proposed in this article.

Limitations and implications for future research

This study was conducted during the time when the government had imposed coronavirus disease 2019 (COVID-19) lockdown restrictions. Twenty-three interview sessions were conducted virtually. Furthermore, the impact of COVID-19 restrictions negatively affected SMEs the most. Therefore, the participation of SMEs may have been influenced. The use of English language in the survey part of the study may have limited or affected the participation level.

This study has both theoretical and practical implications. The funding risk reduction and mitigation model acknowledges the embeddedness of risk and uncertainty in the entrepreneurial process, brings into the equation training, mentorship and other skills development support inputs and technologically enabled monitoring mechanisms. According to Mamabolo et al. (2017), entrepreneurship education and training targeted on certain skills will improve entrepreneurial success. The study recommends for the development of Africa-based SME business school education programmes. Business school education is expensive and mostly has a large enterprise-inspired training content.

The successful implementation of the blended SME funding model depends on the improved public–private partnerships, capacity and skills adequacy within the government SME supporting institution, and the review of certain regulatory provisions impeding SME success as discussed.

Recommendations

Public funding institutions

- Regional and provincial offices of SEFA and IDC should have delegated powers to make decisions on grant and loan applications up to a specific amount as may be determined by these institutions. Based on the observations of this study, such an amount should ideally not be less than R250 000 and could reach a reasonable ceiling of around R2 million.
- The implementation of bank-like information technology systems in order to improve accessibility, efficiencies and monitoring.
- Review orientation and training programmes with the aim of achieving a paradigm shift and embracing a developmental approach for employees recruited from commercial banks.

Private funding institutions

- Commercial banks to adopt a developmental and flexible approach when assessing SME loan applications.
- Support public–private partnership collaborative programmes such as the Credit Guarantee Schemes and others in order to improve SME capitalisation, sustainability and growth.
- Collaboration of Fin-techs and other commercial funding institutions in establishing a central database for SME credit scoring.

Future studies

- The average percentage of the loan amount to be considered as the grant portion for the blended SME model to be objective.

- Standard business plan template to be accepted by both public and private institutions.
- Interest rate to be earned by the SMEs on invoices that remain unpaid after 30 days for the work completed and acknowledged.

Conclusion

South Africa's desired economic development and transformation can be achieved through a thriving SME sector. Entrepreneurship offers a more fair and equitable economic transformative approach where people accumulate wealth as a reward of the value creation contribution as opposed to race, gender or any other orientation. This article has presented a diagnostic report covering the SME success impediment, SME success enablers and the factors enabling SME funding. Finally, the article proposes the blended SME funding model as an option for reducing the funding gap in South Africa. The technological advances witnessed in recent years significantly reduce the costs of monitoring SME performance and enable mass training programmes through virtual platforms.

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Competing interests

The authors declare that they have no financial or personal relationships that may have inappropriately influenced them in writing this article.

Authors' contributions

F.B. who is a doctoral student at the University of South Africa (UNISA) Graduate School of Business Leadership (SBL) wrote this article. M.B.K. supervised the research and the writing of the article.

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Data availability

Interview and survey data used in this study will be made available according to the UNISA research ethics policy.

Disclaimer

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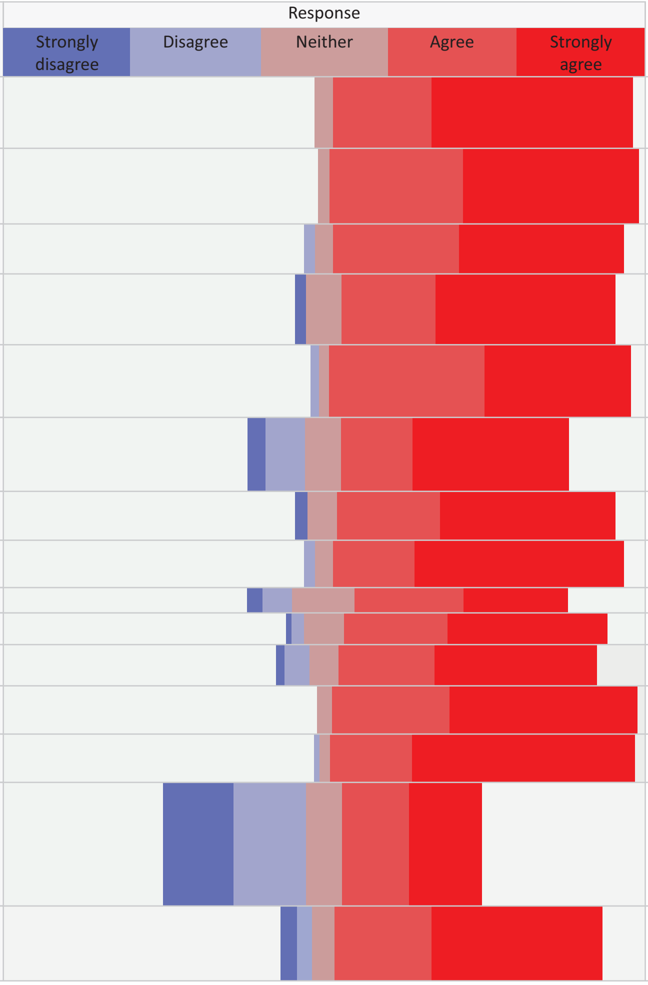
Appendixes start on the next page →

Appendix 1

Questionnaire responses



Response	Share chart	
The paper work supporting the application must be reduced to ten (10) pages.		33
Collaboration and partnerships between public and private sector role players need improvement.		33
Delegated to the regional offices to approve loans for R250 000 and		33
Non-banking institutions must have technology systems similar as the private banks.		34
Better SMEs loan contracts can be used as a way of reducing SME funding risks.		37
SMEs find it difficult to meet the requirement of submitting an audited financial statement		109
Blended finance will improve both access to funding and SMEs		160
Most entrepreneurs require training in financial, operational,		160
Psychometric test		160
Introduction of virtual online training		160
Common standard business plan template		160
Support structures must be established in the provinces		159
Government department and entities fail to pay SMEs within 30-days		159
The current laws and regulations in South Africa make it possible for SMEs to compete fairly with large established businesses (including in government tenders)		157
SMEs should be exempted from submitting TAX returns at least in their first 3 years		159

SME, Small and medium enterprise.

Appendix 2

Rotated Factor Loading

Variable	Factor 1	Factor 2	Factor 3
Better SMEs loan contracts can be used as a way of reducing SME Funding risks.	0.742751	-0.143806	0.219636
Most Entrepreneurs require training in Financial, Operational,	0.735214	-0.183594	-0.037361
Collaboration and partnerships between public and private sector role players need improvement.	0.663650	0.084110	0.359132
Non-banking institutions must have technology systems similar as the private banks	0.523521	0.288825	-0.063293
Blended finance will improve both access to funding and SMEs success.	0.491929	0.010960	0.030687
Support structures must be established in the provinces	0. 424765	0.243015	-0.182538
Psychometric test	0.417475	0.230586	-0.069685
SMEs should be exempted from submitting TAX returns at least in their first 3 years	0.000000	0.000000	0.000000
Common standard Business Plan template	0.043433	0.716528	-0.059592
delegated to the regional offices to approve loans for R250 000 and less.	-0.184643	0.637796	0.349180
Introduction of virtual online training	0.379213	0.465916	0.010847
The current laws and regulations in South Africa make it possible for SMEs to compete fairly with large established businesses (including in government tenders)	0.140758	0.245357	-0.170108
The paper work supporting the application must be reduced to ten (10) pages.	-0.006202	0.046833	**0.618419**
SMEs find it difficult to meet the requirement of submitting an audited financial statement	**0.340204**	-0.124223	**0.419570**
Government department and entities file to pay SMEs within 30-days	0.038365	0.041516	0.287567

SME, Small and medium enterprise.