AN ASSESSMENT OF FINANCIAL FACTORS LEADING TO THE FAILURE OF MICRO AND SMALL ENTERPRISES (MSEs) FUNDED BY MICRO FINANCE INSTITUTIONS IN MALAWI:

THE CASE OF FINCA ZOMBA CLIENTS

MASTER OF BUSINESS ADMINISTRATION

OWEN FARAI CHISUBI MASAULI

UNIVERSITY OF MALAWI

THE POLYTECHNIC

JULY, 2012

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Owen Farai Chisubi Masauli

A Thesis submitted to the Faculty of Commerce, The Malawi Polytechnic, University of Malawi, in partial fulfillment of the requirements for the degree of Master of Business Administration

JULY, 2012

DECLARATION

I declare that this thesis is my own unaided work. It is being submitted in partial fulfillment of the requirements for the degree of MBA in the University of Malawi and has not been submitted before for any degree or examination in any other university.

Candidate's Name: Owen Farai Chisubi Masauli

Signature:…………………………………………………………………………

Date:…………………………………………………………………………..

CERTIFICATE OF APPROVAL

We declare that this thesis is from the candidate's own work and effort. Where he has used other sources of information, it has been acknowledged. This dissertation is submitted with our approval.

First supervisor's Name: Mr. Archie Mwenifumbo

Signature:

Date:

Second supervisor's Name: Mr. Jayi Mlaliki

Signature:

Date:

Head of Department's Name: Dr. E. Sankhulani

Signature:

Date:

DEDICATION

This thesis is dedicated to my beloved father Mr. Chisubi Masauli.

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ABSTRACT

The growing importance of micro and small enterprises in development, poverty reduction and livelihood strategies in developing economies where paid job opportunities are limited cannot be underestimated. One notable development is that most of the Micro and Small Enterprises in Malawi fail due to the impact of financial factors. This study assesses the financial factors that lead to the failure of Micro and Small enterprises funded by Micro Finance Institutions in Malawi using data collected from FINCA Malawi, Zomba Branch clients. The results show that indeed these financial factors have a negative impact on the operations of micro and small enterprises leading to their failing. While there are no significant differences in the impact among the factors, the results, however, show that factors like, unarranged loan repayment period, country's economic elements, and low money supply were among the ones rated highly on their impact. The findings will assist policy makers (Government), development agencies (lending institutions - MFIs) and business organisations (Micro and Small Enterprises) to develop appropriate strategy to improve the MSE sector in terms of failure. As such a call has been made on the Government's intervention on policies and conditions governing the protection of the MSE sector.

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LIST OF ABREVIATIONS AND ACRONYMS

CTA	Chief Technical Advisor
DEMAT	Development of Malawian Enterprises Trust
DFID	Department for International Development
DTI	Department of Trade and Industry
ECI	Ebony Consulting International
FINCA	Foundation for International Community Assistance
GDP	Gross Development Product
GEMINI	Growth and Equity through Microenterprise Investments and Institutions
MBA	Master of Business Administration
MCI	Ministry of Commerce and Industry
MFI	Micro Finance Institutions
MK	Malawi Kwacha
MoGYCS	Ministry of Gender, Youth and Community Services
MRFC	Malawi Rural Finance Company
MRFSP	Malawi Rural Finance Services Programme
MSE	Micro and Small Enterprises
MUSCCO	Malawi Union of Savings and Credit Cooperative
NABW	National Association of Business Women
NGO	Non – Governmental Organisation
NPL	Non Performing Loans
NSO	National Statistical Office
SACCO	Savings and Credit Cooperatives Organisation
SAP	Structural Adjustment Programs
SBA	Small Business Administration

SEDOM	Small Enterprise Development Organisation of Malawi
SHDI	Self-Help Development International
SME	Small and Medium Enterprises
SMME	Small, Micro and Medium Enterprise
SPSS	Statistical Packages for Social Sciences
UNDP	United Nations Development Programme
UWCT	Usiwa Watha Credit Trust
WIP	Work In Progress
WVM	World Vision Malawi

CHAPTER ONE

INTRODUCTION

1.1 Background

Since independence, in 1964, the Government of Malawi concentrated its efforts on the development of the large scale enterprise sector. However, during the late 1970's and early 1980's the government embarked on several initiatives in support of the Micro and Small Enterprise (MSE) sector including the establishment of several support institutions (Ministry of Commerce and Industry, 1999: 3-4). It is now recognized that the potential of the MSE sector has not been fully exploited due to the absence of a concise policy to guide the development and promotion of the sector. Over the last two decades there has been an increased feeling that MSEs should grow and increase their contribution towards employment, poverty alleviation and ownership of productive sectors (Duncan, 1993; Rondinelli, & Kasada, 1993). Sample survey data from Ghana, Malawi, Mali, Senegal, and Tanzania about five years after they launched structural adjustment programs (SAPs), reveal that many MSEs were able to take advantage of the changed environment, while others were constrained by increased competition, financial difficulties, inputs, and the business environment (Office of Advocacy, 2001:9).

1.1.1 Importance of MSEs

In Malawi micro and small enterprises are defined as follows: A micro enterprise is an entity that employs not more than four people including the owner and with an annual turnover of up to MK120, 000.00, a small enterprise employs five to twenty people the owner inclusive and with an annual turnover of MK120,001.00 to MK4 million (Ministry of Commerce and Industry, 1999). A more detailed section on the definition of the MSEs follows in the second chapter.

Micro and small enterprises contribute to the growth and stability of the country's economy in numerous ways (Small Business Administration, 1998). The MSE sector offers a lot of scope for the development of a country. Some of the potential benefits that would accrue to the economy are: the creation of employment at significantly low cost; utilization of raw materials to add value to the agriculture produce; equitable distribution of income; enhancement of balanced development; serving as nurseries for medium and large scale enterprises; and promotion of entrepreneurial development and skills training. Thus, it is central to poverty alleviation in the country, (Ministry of Commerce and Industry, 1999:12). Looking at the overall number of MSEs and owners, according to the GEMINI report (2000:9), the sector contributes income to about 25 percent of Malawian households and by 2000, the sector employed 1.7million people which represented 38 percent of the total Malawian labour force.

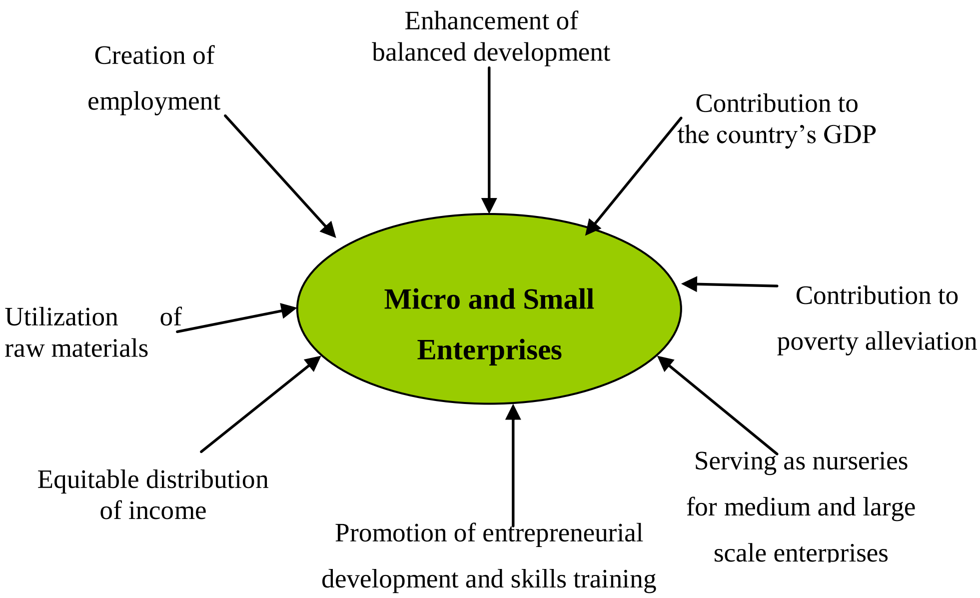

Figure 1.1: Potential benefits accruing to the economy

In addition to the benefits shown in figure 1.1above, it has also been argued that a dynamic and growing MSE sector can contribute to the achievement of a wide range of development objectives, including: the attainment of income distribution and poverty reduction (DFID, 2000); creation of employment (Daniels, 1999); provision of the seedbed of industrialisation (Grosh and Somolekae, 1999; World Bank, 2001); savings mobilisation (Beck, Demirgu, Kunt, Leaven and Levine, 2005); and production of goods and services that meet the basic needs of the poor (Cook and Nixson, 2005).

1.1.2 Performance of MSEs

The micro and small enterprises sector plays an important role in Malawi. According to Chirwa (2004), in 1992 it was estimated that there were 587,283 MSEs generating about 1.07 million self and paid employment opportunities compared to 557,848 MSEs generating 1.01 million employment opportunities in 2000. The GEMINI report (2000:8-

10) further says that the MSE sector contributes more than 15.6 percent to the Malawi Gross Domestic Product (GDP). In Malawi, on average MSEs together generate an annual gross sales value of K47 billion (US$790 million using 2000 exchange rates) which is substantial for a relatively poor country. MSEs have a total annual profit (more equivalent to GDP) of MK 16.7 billion amounting to about 15.6 percent of Malawi's GDP, adjusted to 2000 prices. This is a substantial contribution to the economy by a sector that has largely been ignored in the past. However, the relative performance of micro and small enterprises operated by women and men has not been studied in Malawi, (Chirwa, 2004). Table 1.1 below gives comparative data on the enterprise structure of Malawi.

Table 1.1: Enterprise structure of Malawi

Enterprise Size	Percentage in terms of Numbers
Micro	96.36%
Small & Medium	3.6%
Large	0.04%

Source: CTA Private Sector Development Study, Ministry of Commerce and Industry (2004)

1.1.3 Micro Finance Institutions in Malawi

In 1995 the Malawi Government produced a policy framework for addressing poverty at a national scale against a background of poverty that was estimated at 54 percent of the population by the World Bank (1995). As a result of the policy emphasis on poverty, there has been a substantial growth in the number of microfinance institutions in Malawi offering financial services to the poor on various scales. Most of these microfinance institutions are operating within geographic areas, thereby making financial services not accessible to the poor universally. However, The World Bank (2001) notes that access to credit may help the poor avoid distress sales of assets and replace productive assets destroyed in a natural disaster. Thus, microfinance programmes help the poor households diversify their sources of income and reduce their vulnerability to income shocks. World Bank (2001) further observes that most micro-credit programmes reach clients just above or just below the poverty line and expanding the client base to poorer households remains a challenge.

The growth of the microfinance sector and the central role it is playing in the development of the micro and small scale enterprises in Malawi had prompted the government to address the questions about a conducive environment for promoting microfinance institutions and the regulatory framework to promote best practice approaches in the provision of financial services to the poor (Chirwa, 2002). The Ministry of Commerce and Industry (MCI), which is responsible for the development of micro and small scale enterprises sector, with financial assistance from the United Nations Development Programme (UNDP) through the Enterprise Development and Employment Creation Programme embarked on a consultative process of developing a microfinance policy and the regulatory framework (Makoza, Magai and Chirwa, 2002). According to Chirwa (2002) the following were the Micro Finance Institutions operating in Malawi: Development of Malawian Enterprises Trust (DEMAT), Small Enterprise Development Organization (SEDOM), Foundation for International Community Assistance (FINCA), Malawi Rural Finance Company/ Mudzi Rural Financial Services Programme (MRFC/MRFSP), Usiwa Watha Credit Trust (UWCT), Malawi Union of Savings and Credit Cooperative Organisation/Savings and Credit Cooperative Organisations (MUSCCO/SACCOs), Ministry of Gender, Youth and Community Services (MoGYCS), Chikondano Community Savings and Lending Organisation (Chikondano), National Association of Business Women (NABW), Self-Help Development International (SHDI), World Vision Malawi (WVM), Project Hope, Concern Universal, CARE International, Pride Africa, Small Enterprise Development of Malawi (SEDOM). Currently Malawi has more than 20 MFIs, maintaining some of the ones listed above and registered even new more. While positive developments have taken place in the micro finance sector in the postdemocratisation era, the existing institutions are far from satisfying the demand for such services and lack of financial resources remains a major constraint in the expansion of micro and small business enterprises in Malawi. This is illustrated in table 1.2 below. In addition, the existing micro finance institutions are grossly wanting in terms of human, physical and financial resources to enable them operate national programmes.

Table 1.2: Access to micro credit on selected MFIs by Micro and Small Enterprises by district, 2000

	Microfinance Institutions			*Credit Granting NGOs*					
District	MRFC	FINCA	PRIDE Malawi	NABW	WWB	Concern Universal	Other Org(s)	Total	Total MSEs
North									
Mzimba	5	4	0	2	0	0	0	11	**370**
Nkhatabay	0	1	0	0	0	0	0	1	**134**
Central									
Kasungu	5	0	0	0	0	0	6	11	**264**
Salima	1	0	0	0	0	0	0	1	**185**
Dowa	1	0	0	0	0	0	3	4	**86**
Lilongwe	6	30	0	0	2	0	3	41	**1040**
Mchinji	1	0	0	0	0	0	7	8	**175**
Dedza	0	5	0	0	0	7	0	12	**218**
Ntcheu	1	8	0	1	0	0	0	10	**280**
South									
Balaka	1	0	0	0	0	0	0	1	**68**
Machinga	2	4	0	0	1	0	4	11	**312**
Zomba	**5**	**5**	**0**	**0**	**0**	**0**	**0**	**10**	**280**
Blantyre	2	44	7	0	0	0	5	58	**1479**
Mwanza	0	2	0	3	0	0	0	5	**106**
Mulanje	3	5	0	0	0	0	3	11	**142**
Total	**33**	**108**	**7**	**6**	**3**	**7**	**31**	**197**	**5139**

Source: Computed from ECI/NSO (2000) data

1.1.4 Factors contributing to failure of MSEs in Malawi

The main reasons for failure of micro and small enterprises in Malawi reflect the problems that enterprises experience on an on-going basis. According to the Gemini Report (2000) financial problems account for 36 percent of micro and small enterprises failures with lack of operating funds posing the biggest constraint. Markets problems, including lack of demand, and too many competitors cause 13 percent of failures and unavailable and expensive inputs account for the majority of failures due to input problems (12 percent). A closer look at the data also reveals that household responsibilities account for eight percent of all failures and personal health a further seven percent. The Report adds that 38 percent of micro and small enterprises in rural areas of Malawi fail primarily due to financial problems compared to 24 percent of those in urban areas. Input problems were, however, greater in urban areas with 18 percent failing compared to 11 percent in the rural. While enterprises in both locations cited market problems as the cause of 13 percent of failures. Miscellaneous reasons including household responsibilities and personal health reasons were significant in both urban low income areas registered 33 percent and 27 percent in rural areas. Financial problems remain the single most important factor in MSE failure across ownership by gender although they feature much more prominently for multiple owners than for others. Table 1.3 presents these along with the most commonly cited problems within a category

Table 1.3: Why businesses fail: Percentage of MSEs

Problem Category	*Overall (%)*	*Most common problems within category*
Financial Problems	35.69	lack of operating funds (75%) lack of investment (10%)
Market problems	12.73	not enough demand (38%) too many competitors (26%)
Transport problems	2.81	Expensive public transport (62%) other (20%)
Tools/Machinery	0.44	Unavailability of machinery/ spare parts (44%) expensive spare parts (25%)
Input problems	12.20	Expensive inputs (63%) unavailability (26%)
Govt/Regulatory	0.49	Government involvement harassment (53%) Other (24%)
Shop/rental space	0.42	space unavailable (32%) lack of shelter (20%)
Labor problems	0.78	other (56%) unskilled labour unavailable (21%)
Utilities problems	0.12	Unavailability (64%) unreliability (36%)
Technical problems	0.59	Management problems (78%) access to training + other (22%)
Miscellaneous problems	27.91	Household responsibilities (32%) personal health (26%)
Other closure codes	5.81	started another business (61%) other positive reason (28%)
Total	**100**	

Source: Malawi Micro and Small Enterprise Survey, 2000

1.2 Reseach problem

One of the fundamental questions in strategic management and entrepreneurship research is why some firms fail and others do not. The vast majority of organizational research has concentrated on successful enterprises. Yet, despite evidence that a failure is a more likely fate than survival for micro and small enterprises, failures remain an understudied population (Thornhill and Amit, 2003; Baldwin, Gray, Johnson, Proctor, Rafiquzzaman and Sabourin, 1997; Bruderl, Preisendorfer and Ziegler, 1992). In Malawi the failure of micro and small enterprises is evident by the increasing poverty by the rural masses (Malawi Poverty and Growth Strategy Paper, 2003). Most reports such as the GEMINI report, (2000), Malawi Poverty and Growth Strategy Paper (2003), and Malawi Growth and Development Strategy Paper (2006), just indicate that the sector is not growing. However, there has been little empirical assessment of factors leading to retarded growth of the sector. As such, this research attempted to fill this vacuum by carrying out an assessment of financial factors amongst the factors leading to the failure of most micro and small enterprises.

1.3 Research objectives

The research intended to achieve the following objectives.

Main Objectives:

-To identify and assess financial factors that lead to the failure of Micro and Small Enterprises in Malawi.

Specific Objectives:

- To identify the most significant elements, within the financial factors that lead to the failure of MSE's in Malawi.
- To provide a practical guidance to Micro and Small Enterprise owners and recommend the most appropriate preventive measures that would help to avoid business failure.

1.4 Research questions

The study attempted to answer the following research questions in order to achieve its purpose.

- What financial factors lead to the failure of MSEs in Malawi?
- Which financial factor contributes the greatest to the failure of MSEs?

1.5 Methodology

The research adopted investigative research design to address the research questions in order to achieve the objectives. In addition to desk research where secondary data was reviewed, a sample of 280 respondents was selected with a view of collecting primary data. Face-to-face interviews facilitated by a structured questionnaire were conducted by the researcher with the help of two well trained research assistants. This method was chosen because it had the dimension and capability to accommodate a wider range of primary data. The methods and applications used in the study included sampling, questionnaire design, pre-test and administration. The data was analysed using SPSS and Microsoft Excel packages.

1.6 Limitations

The main limitation to this study was financial resource and as such the study was restricted to a sizable sample that was accommodated by the available funds.

False information from respondents also limited the reliability of the study, this can be deliberate or by hiding, ignorance or through over-enthusiasm.

1.7 Organisation of the study

The dissertation is organized as follows: the first chapter introduces the research and provides a brief background on the importance and performance of MSEs in Malawi. It also highlights some aspects in the research problem, research objectives, research questions, methodology, definition of terms and limitations. The second chapter outlines the literature review on MSEs in Malawi, financial factors leading to the failure of MSEs. These are the views of other authors on the topic. Chapter three gives details of the research methodology and techniques used to gather and analyse data in order to achieve the objectives of the study. Chapter four provides the data analysis and the presentation of the empirical study results. Chapter five discusses the study findings i.e. financial factors that lead to the failure of the MSEs in Malawi are assessed and discussed. Chapter six concludes and summarises the recommendations of the study to provide a practical guidance to Micro and Small Enterprise owners by recommending the most appropriate preventive measures, on the impact of financial factors, to avoid business failure.

1.8 Chapter summary

This dissertation focuses on assessing the financial factors that lead to the failure of Micro and Small Enterprises (MSE's) in Malawi. The background to the performance and importance of MSE's in Malawi has been outlined. The chapter also highlighted the research problem, research objectives, research question and hypothesis, and the methodology. It ended by giving an outline of the rest of the document in terms of the contents of the chapters that follows.

CHAPTER TWO

LITERATURE REVIEW

2.1 Definition of basic terms and concepts

A number of authors have defined the terms used in this report differently, but in this report the researcher has chosen specific definitions to be used throughout the study.

2.1.1 Micro and Small Enterprises

There is no single, uniformly acceptable, definition of a micro or small enterprise worldwide as many authors have given varied definitions. Firms differ in their levels of capital invested, turnover and employment. Hence, definitions which employ measures of size (number of employees, turnover, profitability, net worth, etc.) when applied to one sector could lead to all firms being classified as small, while the same size definition when applied to a different sector could lead to a different result. According to Kayanula and Quartey (in Alabi, Alabi, and Ahiawodzi, 2007) in Ghana the definition for MSEs is based on the number of employees and Total Turnover on Investments. By this classification, Micro-Enterprise employs less than five people with a total turnover of up to $10,000 equivalent, Small Enterprises employ five to 19 people with a total turn over of between $10,000 - $100,000 equivalent and Medium Enterprises employ 20 to 100 people with an annual turn over of above $100,000. In Kenya it is not different from how Ghana defines these enterprises. Botswana, according to Sathyamoorthi (2002), defined micro enterprises as an enterprise which has less than six employees including the owner and an annual turnover of less than P60, 000, and small enterprise has less than 25 paid employees and has an annual turnover of between P60, 000 and P1, 500,000. Referring to the MSEs policy formulated by the Ministry of Commerce and Industry in 1999, in Malawi micro and small enterprises are defined as follows and this study has adopted that definition. A micro enterprise is defined as an entity that employs not more than four people including the owner and with an annual turnover of up to MK120, 000.00. A small enterprise is defined as an enterprise that employ five to 20 people the owner inclusive and with an annual turnover of MK120,001.00 up to MK4 million (Source: Malawi Government – MSE Policy Document, 1999). In this regard, the definition of enterprise size is based on two parameters, namely, employment and turnover as shown in the following table:-

Table 2.1: Tabulated definitions of enterprises

Size	Employment	Turnover (MK)
Micro	1-4	Up to 120,000.00
Small	5-20	120,001 to 4 million
Medium	21-100	Above 4 million to 10 million
Large	Above 100	Above 10 million

Source: Malawi Government – MSE Policy Document, 2000

As noted by Cook and Nixson (2005), although a number of measures have been used to identify and describe MSEs, there is no consensus on any one measure and it is customary to use several metrics, including the value of fixed assets of the enterprise, enterprise turnover and the number of employees. Ryan (2005) pointed out that the term may be used to cover a wide range of economic activities for an indicative number of employees.

2.1.2 Business failure

It means an enterprise not able to achieve its objectives hence no growth experienced and loss of investor capital. This definition allows the assessment to be done by interacting with the business owners. As such, the enterprises in question are not completely closed down as defined by other authors. Dun and Bradstreet (1998) who are considered the primary source of data on business failure, define business failures as those businesses that ceased operation following assignment or bankruptcy. Similarly, Archibald and Baker (1998:221) define business failures as firms that cease to exist and leave unpaid debts. Lane and Schary (1991:95) report that business failures are either the exit of businesses involved in court proceedings or the exit of business by voluntary actions involving losses to creditors.

2.1.3 Business growth

According to Fewell & Parkinson (in Nyirenda, 2005) business growth is defined in terms of the rise of people employed, turnover, size of business and its outlets.

2.1.4 Financial factors

In this study, financial factors are defined as those factors which are financial in nature but goes down to the stem of the business, that if not well managed can lead to the downfall of the enterprise.

2.2 Growth and development of MSEs

During the last 50 years, considerable insight into the characteristics and performance of MSEs has been gained. Early literature, particularly Staley and Morse (in Christopher, et, al, 2006) enhanced the conceptualization of the main characteristics and performances of MSEs and the pattern of growth of these enterprises. However, Anderson (in Christopher, *et*, *al.*, 2006) notes that there was lack of basic data on the management and characteristics of MSEs. Industrial censuses tended to concentrate on large enterprises; censuses of MSEs were often non-existent or quite infrequent or published after a long delay. The lack of data hampered any attempts to undertake serious empirical work on measuring the characteristics and performances of MSEs including explaining the behaviour of these enterprises as well as the constraints that they encountered (Cook and Nixson, 2005).

However, during the 1980s, some efforts were made to collect baseline data on MSEs by, among other tasks, identifying universes, constructing samples and devising methods to deal with incomplete entries. However, due to poor book-keeping by MSEs, the data were often incomplete, unreliable and not repeated across samples. Hence, while the baseline data could be used for measuring the characteristics of MSEs, it was not adequate for testing theoretical propositions about the expected behaviour of the MSEs. Gradual improvements were achieved over the years such that by the early 1990s, some basic databases were available for empirical studies aimed at identifying the constraints facing the growth and development of MSEs in developing countries like Malawi (Levy, 1993). One of the main findings from these studies was that growth and development of MSEs in developing countries were mainly inhibited by access to finance, poor managerial skills, lack of training opportunities and high cost of inputs (Cook and Nixson, 2005).

Further studies conducted in the late 1990s and thereafter suggest that finance is the most important constraint for the MSE sector (Green, Kimuyu, Manos & Murinde, 2002).

2.3 Business establishment

Studies of business development and growth have shown that the early years after establishment are determinant to their future (The business plan, 2004).

O'Neil (2006) is of the opinion that many MSEs remain as small enterprises because the owners are critical to the day to day operations that the business growth is limited to what the owner can personally reach. He further says that a successful and profitable business is one that is not solely dependent on the owner's input. For example a study of Botswana, Kenya, Malawi, Swaziland and Zimbabwe, by Mead (in Christopher, *et, al*., 2006), found that most MSEs started with one to four employees and never expanded; less than 1% grew to exceed 10 employees.

2.4 Non financial factors leading to business failure

There are three main categories of factors that affect the performance of business enterprises with financial being one of them and the others being managerial and market factors (Chirwa, 2004). The poor performance of Micro and Small Enterprises in Malawi is attributed to many factors. These factors include inaccessibility to credit from the formal financial system, lack of capital, poor technical and managerial know-how, poor access to markets and raw material procurement problems, unfavourable legal systems, competition from state and large enterprises, diversion of business capital to medium and large enterprises, poor government policies and inadequate institutional framework (Chirwa, 2004).

Much of the business literature treats business failure as a problem stemming from the manager and the manager's characteristics, especially where the manager is an entrepreneur (Yrle, 2000). It is also argued that between 68 and 80 percent of all businesses fail within the first five years of their existence (Clark, 2000; Monk, 2000). The reasons why businesses fail are numerous; and many of them are predictable. In an attempt to answer the question of why businesses fail, Mason (2000), provides a lists of possible reasons, which included the following: the basic idea was wrong; start-up capital was inadequate; there was wasteful use of capital; a lack of stubborn staying power; a lack of financial know-how; inability to deal with a variety of people - suppliers, customers, employees; bad pricing; ignorance of government restraints; and taking the competition too lightly. Clark (2000) noted that the four most common reasons for business failures are: poor organizational management; unbalanced managerial experience; lack of managerial ability; and lack of market-specific experience.

U.S Government (2001) asserts that the theoretical research in this area is limited but generally, the factors leading to the failure of MSEs funded by micro finance institutions have been financial. These include lack of sound management of working capital/cash flow and other financial problems; technically oriented such as lack of skills e.g. marketing and a lack of managerial experience; Government issues such as tax-related reasons and other general issues such as economic downturn in the economy and increased competition and a lack of raw materials.

2.4.1 Managerial factors

Lack of managerial know-how places significant constraints on SME survival. Even though SMEs tend to attract motivated managers, they can hardly compete with larger firms. According to Daniels & Ngwira (1993), the scarcity of management talent, prevalent in Malawi, has a magnified impact on SMEs.

Management decisions made during the start-up period of a new enterprise can be a key factor in the success or failure of a firm. As noted, much of the discussion in the entrepreneurship literature has focused upon the individual entrepreneur and factors such as managerial inexperience, poor planning, lack of market experience, inadequate cash reserves, and the like (Dun & Bradstreet, 1999; Small Business Administration, 1998). Most factors are under the control of the entrepreneur, and to the extent that they are the primary determinants of business failure, better preparation of the prospective entrepreneur could do a great deal to prevent failure (Lussier, 1996). The recent growth of a flourishing entrepreneurial training and advice-giving industry is the evident result. Supporting arguments of entrepreneurial incompetence is the finding that an increase in business failures follows from an increase in the number of new firm start-ups (Small Business Administration, 1998).

Airman (in Hayward, 2001) concluded that at least 90 percent of business failures were due to internal sources such as incompetence, neglect, and a lack of experience. Likewise, Piatt (in Schaefer, 2006) found that 88 percent of failed enterprises in 1981 could be attributed to insufficient line experience, inadequate managerial expertise, and incompetence and DiBernardo (1999) reported similar findings in a survey conducted in 1999 for Dun and Bradstreet. According to Greenstreet (2004), Dunn and Bradstreet determined that 90 percent of micro and small businesses that fail, do so because of lack of skills and knowledge on the part of the owner. In Jusko (2002) "leadership mistakes" was offered as an important factor leading to business failure. Hayward (2001) indicates that poor management is the cause of one half of all UK Small Business failure.

Lack of experience in a situation that requires handling significant growth was also found to be a factor leading to the failure of micro and small enterprises in several studies (Huang & Brown, 1999; Rovenpor, 2003; Thorton & Marche, 2003). Thornton and Marche (2003) report that of the five failed enterprises they studied, each exhibited a rapid rate of growth. They suggest that the businesses grow quickly that managers have no time for making wise, effective decisions.

Micro and Small Enterprises owners frequently lack relevant business and management expertise in areas such as finance, purchasing, selling, production, and hiring and managing employees. Unless they recognize what they do not do well, and seek help, business owners may soon face disaster (Schaefer 2006). She further asserts that neglect of an enterprise by its manager can also be its downfall. Care must be taken to regularly study, organize, plan and control all activities of its operations. This includes the continuing study of market research and customer data, an area which may be more prone to disregard once a micro and small enterprise is in operation. Pettit (2004) adds that it is critical for Micro and Small Enterprises to have a business plan. Many micro and small enterprises fail because of fundamental shortcomings in their business planning. It must be realistic and based on accurate, current information and known projections for the future.

2.4.2 Market factors

Several factors related to market functions are relevant to enterprise failure. In the micro and small enterprise arena, several studies have concentrated on the market factors influencing business failure (Grossi, Lange, Rebell and Stern, 2000; Honjo, 2000; Porter, 2001). The growth rate of the market being entered into can be a relevant factor for failure. On the one hand, a growing market creates opportunities; on the other hand, it puts strain on resources. A growing market also attracts competitors. Competition has been touted by many studies as a key determinant of failure (Grossi, et al., 2000; Honjo, 2000; Watson, 1999). Consumer loyalty does not just happen; one has to earn it. If one does not take care of customers, then competition will. Competition needs to be watched as closely as can be done with own employees (Small Business Administration, 2005).

2.4.2.1 Lack of market research, consumer and competitor behaviour knowledge

As Shane (2000) comments that amongst micro and small enterprises a frequent cause of business failure is a lack of adequate and appropriate market research. He adds that market research is required to help businesses to identify their customers and inform them of the size of the potential customer base, to determine what price customers might be prepared to pay and to suggest how demand for the product or service will change according to the price charged. Research will also inform about competitors and their likely reaction to a new entrant to the marketplace.

2.4.2.2 Market newness

The degree of a market's newness to a micro and small enterprise determines the complexity involved in the operations as well as marketing of its products or services. The market could be new because the product is new to the enterprise and/or because the chosen market is new. In either case, the newness creates uncertainty and risk. In the case of a micro or a small enterprise just starting out, it may be difficult to determine if there is a sufficient market and if that market is continuing to grow. McGrath (1999) argues that the “liability of newness” can also cause a decline in a business due to its age and/or size because of the roles and tasks that require learning, and the lack of history dealing with suppliers, and clients. If the market is not interpreted correctly due to the newness factor, pressure to engage in destructive practices could result.

2.5 Financial factors leading to business failure

Access to finance remained a dominant constraint to micro and small enterprises in Malawi (Daniels & Ngwira. 1993:30-31). This stems from the fact that SMEs have limited access to capital markets both locally and internationally because of the perception of higher risk, informational barriers, and the higher costs of intermediation for smaller firms. As a result, SMEs often cannot obtain long-term finance in the form of debt and equity. Access to credit has been one of the main bottlenecks to SME development. Most SMEs lack the necessary collateral to obtain bank loans. This fact is supported by the Policy on SMME in Botswana (1999: 4) which says that lack of access to finance has been identified as the main problem confronted by most micro and small enterprises in Botswana.

2.5.1 Insufficient capital

Micro and small enterprises owners underestimate how much capital is needed as such they are forced to close before they even have had a fair chance to succeed (Boardman, at al. 1981). They also have an unrealistic expectation of incoming revenues from sales. Schaefer (2006) adds that a common fatal mistake for many failed small businesses is having insufficient operating funds. Therefore, it is imperative to ascertain how much money an enterprise will require; not only the costs of starting, but the costs of staying in business. It is important to take into consideration that many enterprises take a year or two to get going. This means one will need enough funds to cover all costs until sales can eventually pay for these costs.

2.5.2 Overspending

Many startups spend their seed money before cash has begun to flow in at a positive rate. This often happens because of misconception about how business operates (Schaefer, 2006).

2.5.3 Lack of reserve funds

Micro and Small Enterprises need to ensure that they protect their investment and keep enough reserve cash to carry them through market downtrends and seasonal slowness. According to McGrath (1999), failing to prepare for volatile markets and uncontrollable costs like energy-rate increases, materials, labor, natural disasters, and the like is another top reason many businesses fail.

2.5.4 Lack of credit

Along with markets and managerial issues discussed above, lack of credit is the most commonly cited problem among existing MSEs (Orr & Makawa, 2000). It is likely that, as more micro credit providers come into the market, client needs will be more closely catered for. Both the quantity and type of credit can be a limit to the growth of very small businesses. An alternative view is that successful entrepreneurs often shy away from credit and actually attribute their success to not having to pay prohibitive interest rates (Orr & Makawa, 2000).

According to Paetkau & Finnegan (1999), the then financial crisis made it even more difficult for MSEs to arrange loans because banks had an exceptionally high percentage of non-performing loans (NPLs) which weighed heavily on lending officers. Enterprise owners believe that banks are too focused on collateral. Paetkau & Finnegan (1999) further contend that while bankers agree that the absence of usual collateral is an issue they add others like: the inherent higher risk of business failure among MSEs, a lack of complete and accurate financial information, lack of marketing know-how, and the absence of business plans.

2.5.5 Multiple investments

In a survey conducted by Chirwa (2004), it was found that ownership of multiple enterprises reduces growth of individual enterprises due to lack of proper time planning to pay attention to all the running enterprises. Chirwa further found that ownership of multiple enterprises is statistically significant at the five percent level in the MSE model and has a negative influence on profitability.

2.5.6 Financial management

Poor cash flow management amongst the most common internal causes of business failure implies an imbalance between the payment terms taken by debtors and those given to creditors. The most obvious outcome of defective cash flow management is a significant decline in cash, with the business being unable to cover its repayment obligations, either to banks for loans, or towards suppliers for purchased goods and services. According to Small Business Administration (2005), inadequate management of purchases, inventory and Work In Progress (WIP) can lead to cash flow problems and the ultimate result of poor cash flow management is lack of working capital to run day-to-day activities.

Impeding bad debt is one of the possible causes of business failure that is capable of being predicted in advance (Department of Trade and Industry, 2004). Bad debts may increase significantly, due to the insolvency or disappearance of a customer. This often leads in the long run to insolvency. The main problem for MSEs, though, may be in actually identifying potential bad debts and being able to reduce them. DTI (2004) further notes that in many MSEs, there will not be in-house credit collection personnel who are able to undertake regular credit control activity and follow up matters of going-concern. For this reason, bad debts may have a more dramatic impact on MSEs than on larger enterprises.

2.5.7 Repayment period/arrangement

A current concern is that the credit methodology of the Foundation for International Community Assistance (FINCA), which insists on weekly repayments, limits business growth by not providing sufficient time to make a profit (Orr & Makawa, 2000).

2.5.8 Sources of finance

Lack of access to adequate start-up funds also has a "knock-on" effect of restricting the development and growth of small business by reducing funds available for activities such as advertising, publicity and suitable premises (Fielden, Davidson, and Makin, 2000), Hudson and Beghin (2007) also note that lack of capital and the complexities of obtaining loans from financial institutions and government development agencies are major hindrances to micro and small business development. Inadequate access to credit and other financial services from formal financial institutions has long been recognised as a constraint on the expansion of the MSE sector (Beck *et al*., 2005). Lack of tangible security by MSEs, the limited capacity, outreach and linkages by financial intermediaries and a hostile legal and regulatory framework for financial services are the main constraints (Government of Kenya, 2005).

There have been a number of attempts to explain the limited access to credit by MSEs in most developing countries. These attempts have broadly taken two arguably complimentary perspectives. The first highlights the prevalence of factors external to MSEs including the limited capacity, outreach and linkages by financial intermediaries as the main constraints to MSEs access to credit (Atieno, 2001). A hostile legal and regulatory framework for financial services underlies such constraints (Government of Kenya, 2005). The second perspective also acknowledges the problem of macro level constraints, but emphasizes the greater explanatory powers of the relatively weak MSEs capacities including lack of tangible security and limited human capital (Kimuyu & Omiti, 2000). Arguably, both perspectives have enhanced the understanding of the factors that affect the likelihood of MSEs to access bank credit. However, focusing on either perspective has led to different conclusions on the probable determinants of access to bank credit by MSEs.

2.5.9 Cost of operations

The cost of operations for a micro and small enterprise may have been underestimated in the early days of establishment (Huff & Wade, 1999). The cost of a site today is probably even higher. Micro and small enterprises may have lacked the resources to give them flexibility when it comes to switching gears. Even though many small enterprises had strong initial backing like ever present loans, it was not enough to sustain the business through repeated lack of earnings (Alexander, 2002). Surviving in a turbulent environment such as the micro and small enterprises faced is not an easy task.

2.6 Chapter summary

The chapter highlighted and presented various views of different authors on the factors leading to the failure of micro and small enterprises in general. The literature shows that there are a number of factors that affect the survival of enterprises.

The focus of this study is on financial factors that relate to business failure, especially to establish that financial factors account for a large proportion of the variance in the failure rate. It is maintained that these financial factors, and not primarily managerial factors or market factors, account for the high rate of small business failure (Schaefer, 2006; Government of Kenya, 2005, Beck *et al*., 2005).

In this study, specifically, a somewhat distinctive approach was presented to the process of assessing factors leading to failure of micro and small enterprises. Instead of the more conventional approaches, which tend to concentrate on all other factor categories, the focus is upon the relative strength of key macro-level financial factors - financial management, borrowed amount, sources of finance, repayment period, multiple investments, start up capital, cost of capital, economic growth in the country, cost of operations, insufficient capital, lack of credit, overspending, money supply and lack of reserved funds.

CHAPTER THREE

METHODOLOGY

3.1 Introduction

This chapter describes the methodology that was used when carrying out this study. It outlines a discussion of research design, approach and philosophy; and the research methods used in data collection, analysis and interpretation. The research methods included sampling, questionnaire design and administration. The chapter also outlines the limitations to data collection and the ethical issues. The choice of the methodology was very important because it determined the reliability and validity of the findings.

3.2 Research Philosophy, Approach and Design

3.2.1 Research philosophy

The research philosophy that guided this study was phenomenology. The philosophy is more appropriate in situations where it is necessary to analyse factors under ever-changing business environments. This is so because generalization of facts does not hold true for each situation in the ever-changing world of business. (Saunders, at el, 2003; Cooper & Schindler, 1998). The focus in this study was on the financial factors that lead to the failure of micro and small enterprises. As such, with the constantly changing business environment, the factors might not remain constant in their effect. According to Nyirenda (2005) it may be noted that this philosophy contrasts the positivism which propagates the establishment of a general law that would be used for generalization of facts for future discoveries. In addition, the application of the phenomenology approach was necessary for this study because it had the dimension and capacity to accommodate a large volume of data available for investigation for drawing or establishing possible relationships between two or more variables. It was possible to present and describe respondents' business performance against variables such as financial management, borrowed amount, sources of finance, repayment period, multiple investments, start up capital, cost of capital, economic growth in the country, cost of operations, overspending, lack of reserve funds, lack of credit, insufficient capital, etc.

3.2.2 Research design

The study design adopted was a cross-sectional survey method with three main modalities that sought to assess the effects of financial factors on micro and small enterprises (MSEs) especially on their failure. The modalities included reviews, contacts and field activities. The review was conducted through desk research of online resources, research papers, working documents, conference documents, policy documents and other publications. The contacts were made through one on one discussion, by visiting the respondents in their work places. A self developed instrument was used for the field exercise. This design was appropriate in testing the relationship between the different components and variables of entrepreneurial phenomena (Saunders *et al.* 2003). The survey method is a common design in business and management research because it allows researchers to collect large amounts of data from a sizeable population in an economic way (Saunders *et al.* 2003). As such, the researcher adopted this design because the study focuses on business financial factors with the objective of assessing the effects of those financial factors on micro and small enterprises' failure.

3.2.3 Research approach

The study adopted an inductive approach because it wanted to assess in general terms the effects of financial factors on micro and small enterprises' failure. Both qualitative and quantitative data were sourced in order to effectively assess the financial factors that lead to the failure of micro and small enterprises in Malawi, thus, achieve the study objective. According to Saunders, et al., (2003), in small sample subjects, an inductive approach is appropriate. As shown in the preceding chapter, the study on the financial factors leading to the failure of micro and small enterprises is not widely done (Office of Advocacy, 2001) as such an inductive approach was viewed to be appropriate.

3.3 Research methods and applications

The research process included: identification of the study population and sample frame; sampling; the sampling design, size and procedures and data collection methods.

3.3.1 Study population and sample frame

The targeted population in this study included all the micro and small scale enterprises that are funded by FINCA Malawi in Zomba District. According to Mrs. Salome Nyirenda of

Finca Zomba branch (2008), it was established that there were more than 2000 micro and small enterprises in the district at the time of conducting this study. The sample frame of this study, therefore, consisted of the MSEs that made up FINCA Zomba Village Banks and individual FINCA clients in Zomba district. These constituted only the existing FINCA clients which totaled 1,100 (Finca Zomba monthly return, 2008).

3.3.2 Sample size and design

From the sample frame, simple random sampling procedures were applied to select the required sample. According to Saunders et al. (2003) simple random sampling is best used when the sampling frame which lists the entire population is accurate and easily accessible. Simple random sampling ensures that each member of the population has an equal chance of being selected for the study (Francis, 2004:8-9). Francis further says that the method is viewed to be fair, simple and unbiased. The village banks were grouped into four sections of the district (south, west, east and north). The grouping helped to avoid skewing the sample in one section of the district. A random walk, random sampling technique, was applied to each section of the district to come up with a total of 36 village banks and that represented a sample frame of 1,100 micro and small enterprises. From this sample frame a simple random sampling was applied to select the individual respondents. Following Saunders *et al.* (2003:129) the minimum sample size for this study was taken to be 280 enterprises.

3.3.3 Study area

The study was conducted in Zomba where the targeted population was based. All the four sections of the district were considered when coming up with the respondents (study sample) to the study instrument. These sections were Chingale to the west, Thondwe to the south, Jali to the east and Malosa to the north.

3.4 Data collection

According to Saunders at el. 2003, there are three ways of collecting data when conducting a study namely, through observation, through semi-structured and in-depth interviews and through the use of questionnaires. However, in this study, two forms of data were collected namely, primary data and secondary data. Considering that this study was aimed at assessing the financial factors that lead to the failure of micro and small enterprises in Malawi, both qualitative and quantitative data were used.

3.4.1 Primary data

A structured questionnaire was used to collect primary data. The questionnaire was appropriate in this study because the responses sought were to be selected from a given list. As such closed-questions were used to achieve the research objectives. This research tool was tested for reliability and validity in two ways. First, the factors selected were obtained from previous studies and tested for relevance. Secondly, experts in entrepreneurship were used in the selection of the study variables. The questionnaire was pre-tested and administered as detailed in the subsequent sections 3.4.1.1 and 3.4.1.2.

3.4.1.1 Pilot test

A pilot test was done on the questionnaire in order to detect mistakes so that ambiguities and embarrassments should be avoided; these could attract unnecessary costs once the main data collection phase had been entered. Secondly, the pre–test helped to yield reasonably unbiased data and of course it avoided the second chance of data collection. The conditions for the pilot test were as close as possible to the intended conditions for the real study. One Village Bank was visited and the questions were trial-tested by the interviewer. Data collected in this exercise is not reported but was used to rephrase and reorganize the format of the questionnaire. The necessary corrections were done on the questionnaire and this made it interviewee friendly.

3.4.1.2 Interviewer-administered questionnaire

The questionnaire was administered in a structured interview where the interviewer physically met the respondents. The questionnaire is shown in appendix 1. The choice of this type of questionnaire administration was chosen because the researcher was looking for a higher rate of response since a small sample size was used in the study. Saunders at el. (2003) states that interviewer-administered questionnaire enables the researcher to ensure that the respondent is the person required, hence, the reliability of the data is improved. The data collection exercise lasted four weeks from 2nd to 27th October, 2008. A pre-tested questionnaire was administered by the researcher with the help of two trained research assistants. The research assistants were trained on the handling of the research tools and the topic under study before being allowed to collect data. The research assistants were closely supervised by the researcher during data collection. Data was collected by means of ticking in the box which corresponds to the given response. However, when the response from the respondent was not amongst the predetermined responses, the interviewer had to take note of that particular response.

3.4.2 Secondary data

As indicated in section 3.3.1 above some factors selected for this study were from previous studies hence the need to consult secondary data sources. Secondary data were used with a view to enrich the primary data which is the main source of data for the study. The secondary data were obtained from Government publications, world wide websites (Internet), journals and Books.

3.5 Data processing and analysis

The data was classified into different forms in order to identify the patterns that existed. An inductive approach was used to process and analyse the data. Descriptive analysis complemented by statistical charts and frequency tables were used in the analysis. All the quantitative analyses in the study were conducted using the Statistical Package for the Social Sciences (SPSS) version 13.0 and Microsoft Excel. Qualitative data was subjected to tabulation analysis. In this case, a table was created with columns for the different kinds of respondents and rows for the independent factors.

3.6 Limitations

The collection of data did not go without limitations. The researcher experienced problems during the field work as most respondents were illiterate. The desk research also experienced problems: many vital websites were inaccessible and at times a subscription was demanded for one to access the data. This data access limitation is a common and an on going problem in most of the developing countries like Malawi.

3.7 Ethical considerations

To ensure that the data collection exercise yields reliable and valid data, several ethical issues were considered during the exercise. The respondents were assured that confidentiality, privacy and their anonymity was observed and upheld throughout the exercise. The researcher designed the questionnaire in a way that the data collected did not reflect on specific respondents, instead codes were used. Before conducting the interviews the respondents were first asked for their consent. Upon granting the consent, the interviewees were also assured that the information they were to give will not just be given to people anyhow. This guaranteed their protection. The researcher introduced himself to the respondents in a way of an introductory letter from the University of Malawi – The Polytechnic. (See appendix 2.).

3.8 Chapter summary

The chapter outlines the methodology and techniques employed to address the research questions and the research objectives. Specifically, the following items have been highlighted: the research philosophy, approach and design, research methods and applications, data collection, data analysis and processing, limitations and ethical considerations.

CHAPTER FOUR

RESEARCH RESULTS

4.1 Introduction

This chapter presents the results of the study after analysis of data that was collected. The primary data was collected from a sample of 280 enterprises and the response rate was 100 percent. The data was collected through a structured questionnaire which was administered in a structured interview where the interviewer physically met the respondents hence the attainment of a 100 percent response rate. The data was analysed using SPSS. The secondary data which complemented the primary data were obtained from government publications, world wide websites (internet), journals and books. The findings have been presented in the form of descriptions complemented by statistical charts and frequency tables.

Qualitative methods which have been applied in this study usually research a topic or an idea through several methods. Therefore, it is not unusual to use a combination of documentary analysis, together with non-participant observation and interviews. According to Cano (2002), regardless of the reasons, the use of multiple methods in research in order to corroborate data sources increases the reliability of the research. The use of several data sources and different methods is called triangulation. The idea behind triangulation is that the more agreement of different data sources on a particular issue, the more reliable the interpretation of the data.

4.2 Presentation of findings

4.2.1 Respondents and business general information

The study sample comprised respondents from different categories, namely: age groups; educational qualification; business nature and type; start up capital and business know-how. Figures 4.1a, 4.1b, 4.2a, 4.2b, 4.3a and 4.3b below present the composition of the respondents and their enterprises in terms of age groups and educational qualifications; types and nature of enterprises; and business age and start up capital respectively.

4.2.1.1 Respondents' age group and educational levels

Figure 4.1a shows that 1.8 percent of the respondents were less than 20 years of age while those between 21 and 35 years of age represented 56.4 percent of the total study sample. The remaining 41.8 percent were 36 years of age and above.

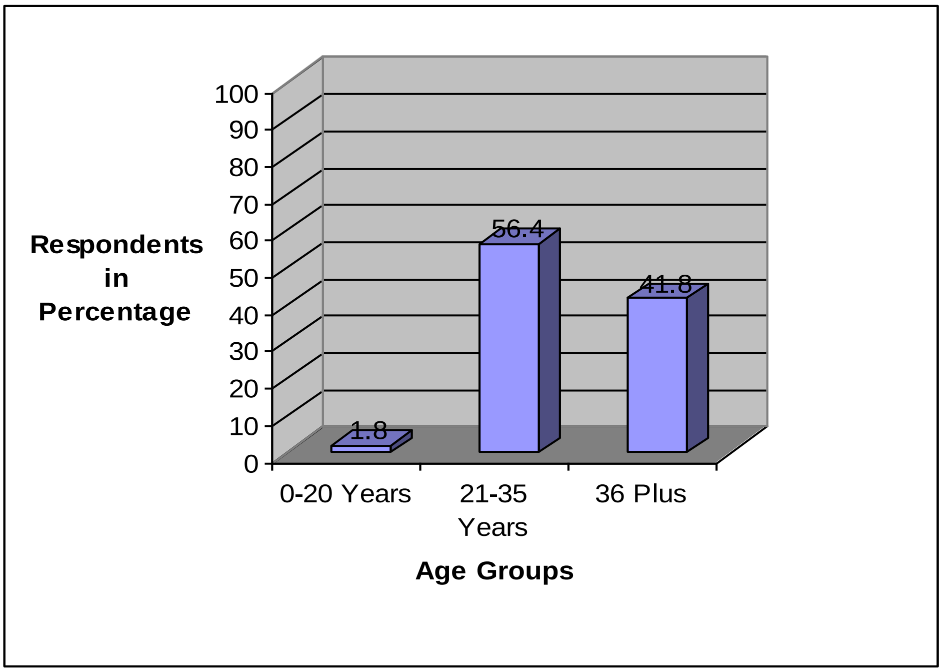

Figure 4.1a: Age levels of the respondents

In terms of educational levels, figure 4.1b below shows that 24.5 percent of the respondents did not attend school, 58.2 percent of the total respondents went up to primary school level while 16.4 percent attended secondary school education. Those that had tertiary education were represented by 0.9 percent of the sample.

Therefore, a total of 98.2 percent of the respondents were above 21 years while 74.8 percent attained education. These were able to understand business issues and be able to articulate issues hence reasonable responses were collected.

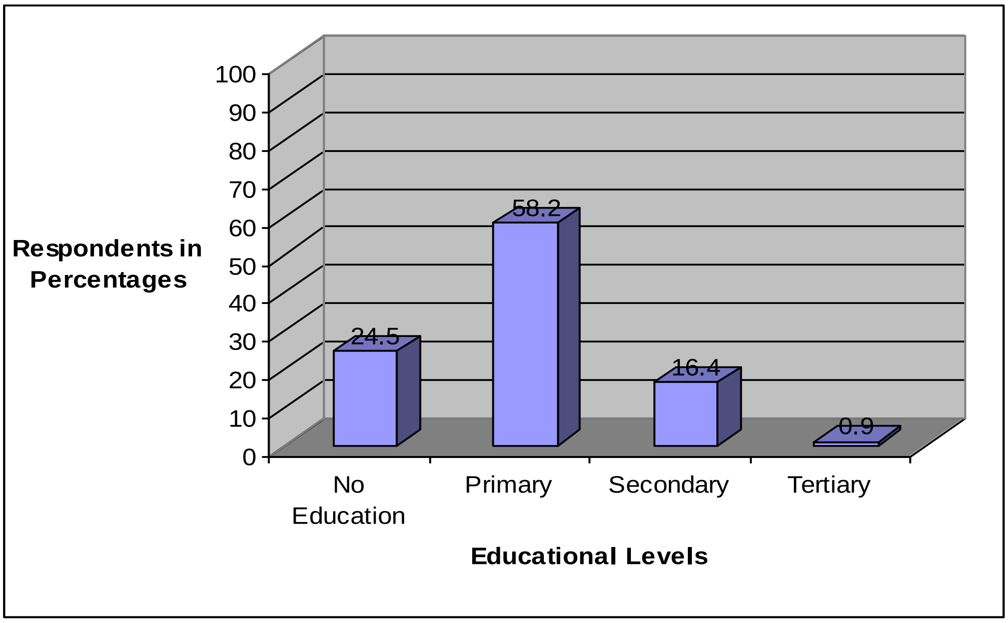

Figure 4.1b: Educational levels of the respondents

4.2.1.2 Types and nature of respondents enterprises

Figure 4.2a below shows that 76.9 percent of the enterprise owners interviewed are in trading businesses while the remaining 10.3 percent and 12.8 percent are in the manufacturing and service businesses respectively.

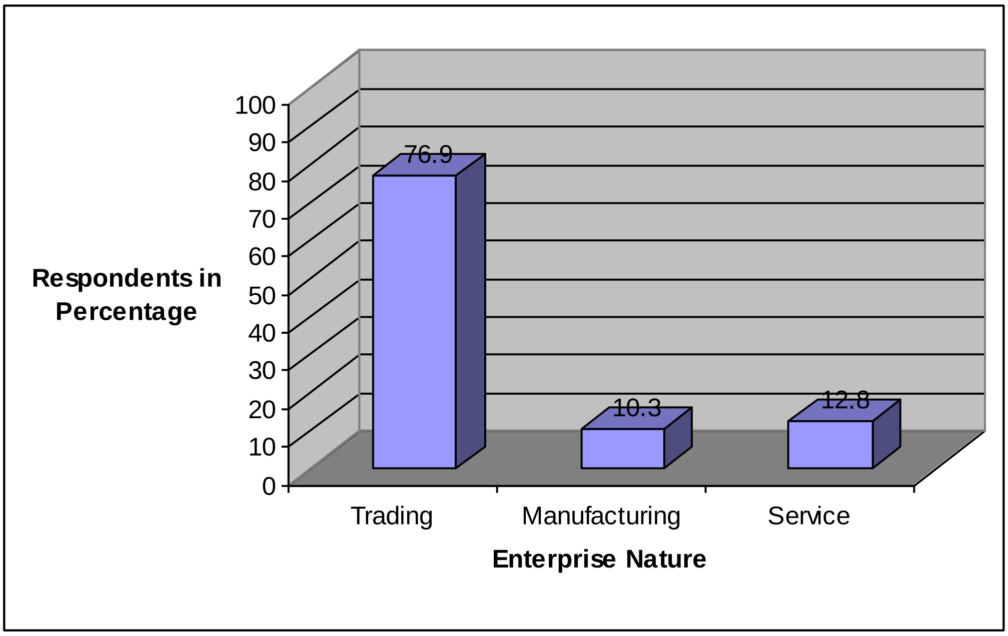

Figure 4.2a: Nature of respondents' enterprises

Figure 4.2b below shows that 99.1 percent of the interviewed respondents are sole proprietors and 0.9 percent are partnerships. Interestingly, there are no franchised enterprises. As can be noted from the results in figure 4.2b 99.1 percent of the respondents are sole proprietors who are directly involved in the enterprise activities and operations so they were able to give out real issues affecting their business operations either negatively or positively.

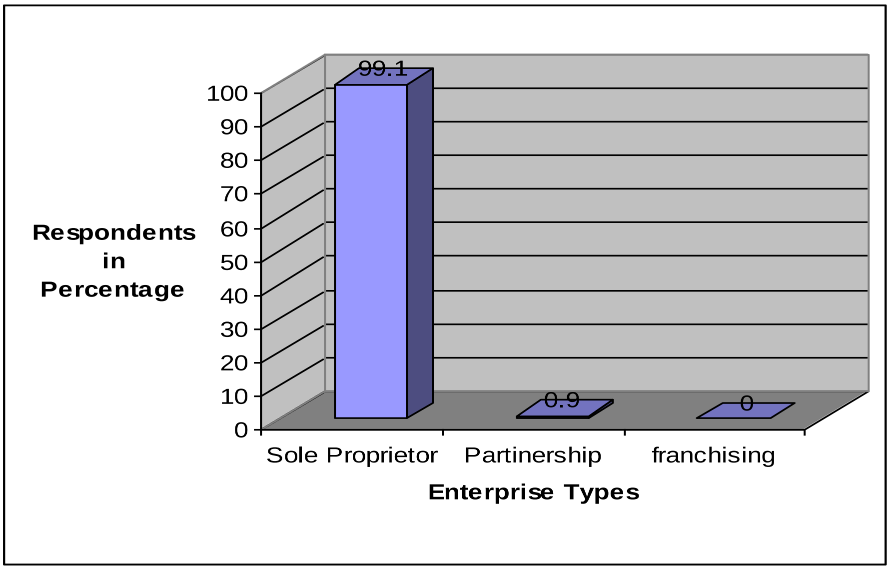

Figure 4.2b: Types of respondents enterprises

4.2.1.3 Business age and start up capital

Figure 4.3a and 4.3b below present the period in which the respondents' enterprises have been operational and the start up capital for the enterprises respectively.

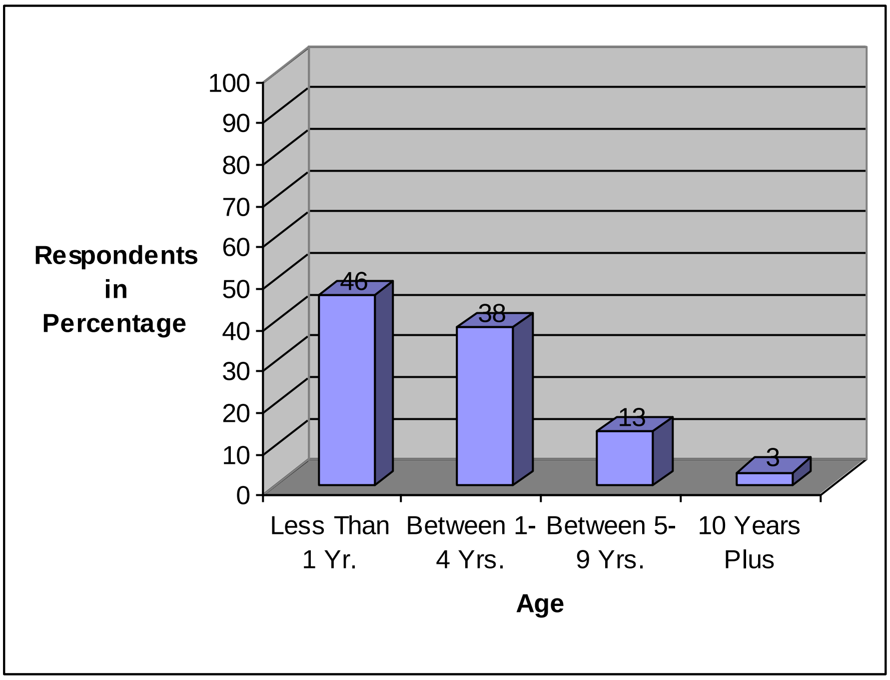

Figure 4.3a: Age of respondents' enterprises

Figure 4.3a above shows that 46 percent of the enterprises have been operational for less than a year, 38 percent have been in business for 1-4 years while those that have been operational for 5-9 years represented 13 percent of the total enterprises. The remaining 3 percent represents enterprises that have operated for more than ten years. This shows that about 84 percent of the enterprises have been operational for less than 4 years.

In terms of start up capital, figure 4.3b below shows that 94.5 percent of the respondents had a start up capital of less than MK50, 000 while those that had a start up capital of between MK51, 000 to MK100, 000 were represented by 4.5 percent. Only 0.9 percent of the respondents had a start up capital of more than MK100, 000. This means that a lot of MSEs operate on very small capital which in most cases does not meet the needs of the enterprises for them to prosper in turbulent market conditions.

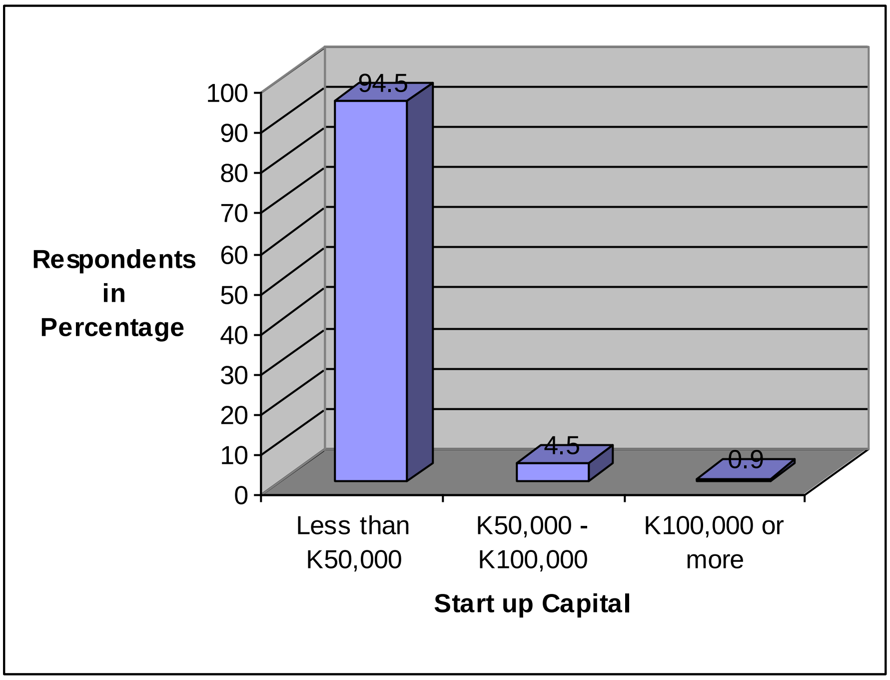

Figure 4.3b: Start up capital of respondents' enterprises

4.2.2 Multiple investments

The study results reveal that there are two ways of investing the funds borrowed from Micro Finance Institutions (MFI's) by Micro and Small Enterprises (MSEs) namely: multiple investment and single investment. Table 4.1 below shows that 173 respondents, representing 61.8 percent of the study sample, did multiple investments when they got the loan while 107 respondents, representing 38.2 percent, invested the loan amount into one enterprise.

As can be seen from Table 4.1 below, 216 respondents, representing 77.3 percent, invested only up to 25 percent of the loan funds into the business registered with the MFIs providing the loan, the other funds were invested in other smaller businesses and other domestic use. Five respondents, representing 1.8 percent, invested 26-50 percent of the loan funds. Those enterprises that invested 51-75 percent of the loan funds were represented by 36 enterprises which translate to 12.7 percent. Only 23 enterprises, which represent 8.2 percent of the total number of respondents, invested 76-100 percent of the loan funds. Whether respondents were successful or not in both or all investments when the funds are diverted from registered business into other businesses, the analysis of the responses shows that 9.1 percent of the respondents succeeded while 90.9 percent did not. (See table 4.1 below).

Table 4.1: Type of investment and usage of funds not invested

Investment Type	***# of Respondents***	***% of Respondents***
Multiple Investment	173	61.8
Single Investment	107	38.2
TOTAL	***280***	***100***
Multiple investment outcome		
Successful	7	9.1
Unsuccessful	66	90.9
TOTAL	***73***	***100***
Loan Portion Invested		
0-25%	216	77.3
26-50%	5	1.8
51-75%	36	12.7
76-100%	23	8.2
TOTAL	***280***	***100***
Usage of Funds not Invested		
Domestic Spending	192	82.4
Banked for Future Use	23	9.9
Pay other Loans	12	5.2
Left Idle	6	2.5
TOTAL	***233***	***100***

According to Schaefer (2006), there are misconceptions about how business operates, many start ups (new businesses) spent their seed money before cash had begun to flow in at a positive rate. As indicated by the "*Usage of funds not invested*" results in Table 4.1, 192 respondents, representing 68.6 percent, used uninvested loan funds for domestic spending while 47respondents, representing 16.7 percent, reinvested the loan funds which were not invested into the business at the time of getting the loan. Twenty three respondents, representing 8.3 percent, banked the loan funds not invested into the business for future use but 12 respondents who represent 4.3 percent used the loan funds, not invested, to pay for other loans. The remaining six respondents representing 2.1 percent just kept the funds idle in their homes. Therefore, 75 percent of the respondents did not invest the whole loan amount into the business registered with the MFI but they used the funds for other purposes or kept the funds idle.

4.2.3 Financial management (working capital/retained profits)

According to Small Business Administration (2005) inadequate management of purchases, inventory and Work In Progress (WIP) can lead to cash flow problems and the ultimate result of poor cash flow management is lack of working capital to run day-to-day activities of the enterprise.

4.2.3.1 Effect of loans provided by the MFIs

Table 4.2 below presents the fluctuation of the working capital of the respondents' enterprises as the result of getting a loan from micro finance institutions. Before getting the loan, 216 respondents, representing 77.3 percent, had a working capital of not more than MK20, 000 while 48 respondents, representing 17.3 percent, were working with a capital of between MK21, 000 to MK50, 000. This concurs with the results in figure 4.3b above. Thirteen respondents who represented 4.5 percent had a working capital ranging from MK51, 000 to MK100, 000. The remaining three respondents, who represented 0.9 percent of study sample, were operating with a working capital of more than MK100, 000. After getting the loan, as shown in Table 4.2, 204 respondents, representing 72.7 percent, operated with a working capital of up to MK50, 000 and sixty four respondents who represented 22.8 percent operated in the range of MK51, 000 to MK100, 000. The remaining twelve respondents representing 4.5 had a working capital of between MK101, 000 to MK150, 000. Despite the ability to access the credit, the enterprises seem not to have experienced a positive change in their working capital.

Table 4.2: Effects of respondents' working capital upon provision of loans

Working capital before getting loan	***# of respondents***	***% of respondents***
Up to Mk 20, 000	216	77.3
Mk 21, 000 – Mk 50, 000	48	17.3
Mk 51, 000 – Mk 100, 000	13	*4.5*
Mk 100, 000 plus	3	0.9
TOTAL	**280**	**100**
Working capital plus loan amount		
Up to Mk 50, 000	204	72.7
Mk 51,000 – Mk 100, 000	64	22.8
Mk101, 000 – Mk 150, 000	12	4.5
TOTAL	**280**	**100**
Working capital six months after getting loan		
Up to Mk 50,000	227	80.9
Mk 51, 000 – Mk 100, 000	41	14.5
Mk 101, 000 – Mk 150, 000	12	4.5
TOTAL	**280**	**100**

Six months after getting the loan, according to Table 4.2 above 227 respondents, representing 80.9 percent, operated with a working capital of up to MK50, 000. Those that operated with a working capital ranging from MK51, 000 to MK100, 000 were 41 representing 14.5 percent. Only 12 respondents making up 4.5 percent had a working capital which exceeded MK100, 000. There is no improvement either after six months of securing the loan. As observed in table 4.2 above, over 80 percent of the respondents' enterprises operate with only up to MK50, 000 as working capital.

4.2.3.2 Investment protection

Micro and Small Enterprises need to ensure that they protect their investment and keep enough reserve cash to carry them through market downtrends and seasonal slowness. According to McGrath (1999), failing to prepare for volatile markets and uncontrollable costs like energy-rate increases, materials, labour, natural disasters, and transport for instance, is another top reason many businesses fail.

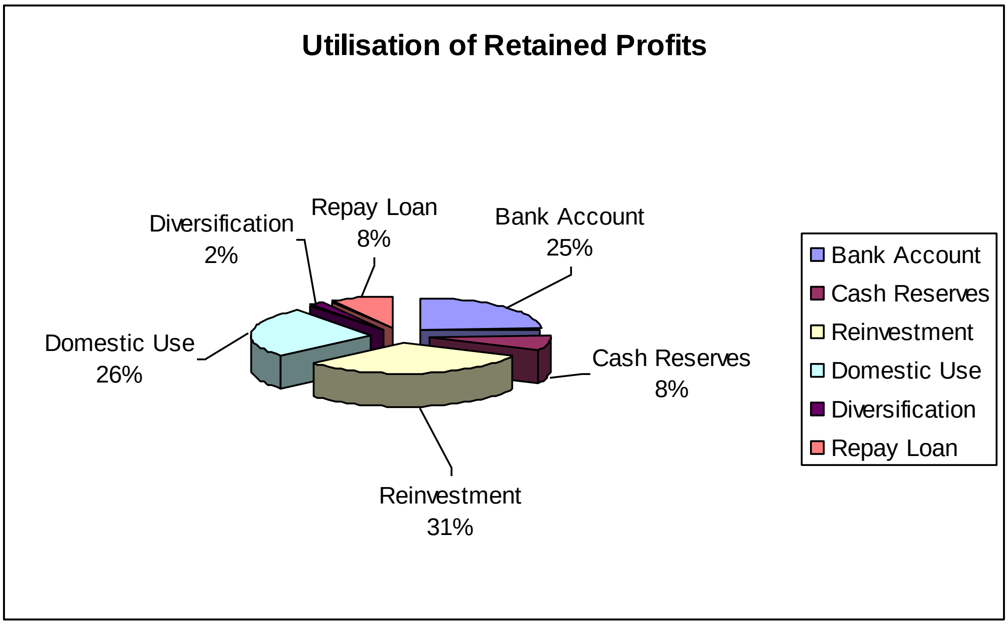

Figure 4.4: MSE's utilization of retained profits

Figure 4.4 above, reveals that 25 percent of the respondents put their retained profits in a bank account, and eight percent had cash reserves from retained profits. Those that managed to reinvest the retained profits were represented by 31 percent. Very few were able to diversify using the retained profits and represented two percent of the entire study sample. Domestic purpose is one of the items that used up the retained profits; 26 percent of the respondents used the retained profits for domestic purposes. However, eight percent of the respondents opted to use the retained profits for repaying the loan. Therefore, only a total of 33 percent of the retained profits (i.e. two percent for diversification and 31 percent for reinvestment) was reinvested into the business and 66 percent (i.e. 25 percent for bank account, 8 percent for cash reserves, 26 percent for domestic use and eight percent for loan repayment) was never retained into the business to boost the enterprise's capital for the adequate support of the enterprise's operations.

4.2.4 Borrowed funds (access to credit)

Lack of access to adequate start-up funds also has a knock-on effect of restricting the development and growth of small business by reducing funds available for activities such as advertising, publicity and suitable premises (Fielden *et al*, 2000). Figure 4.5 below shows that 74respondents, representing 26 percent were able to access the full loan amount applied while 206 respondents representing 74 percent, had their applied loan amount reduced because they did not meet conditions attached to the loan like membership to a group, having a savings account, business experience, and guarantee from the group. This shows that the majority of the MSEs do not access the required credit/finances as per the needs of their enterprises.

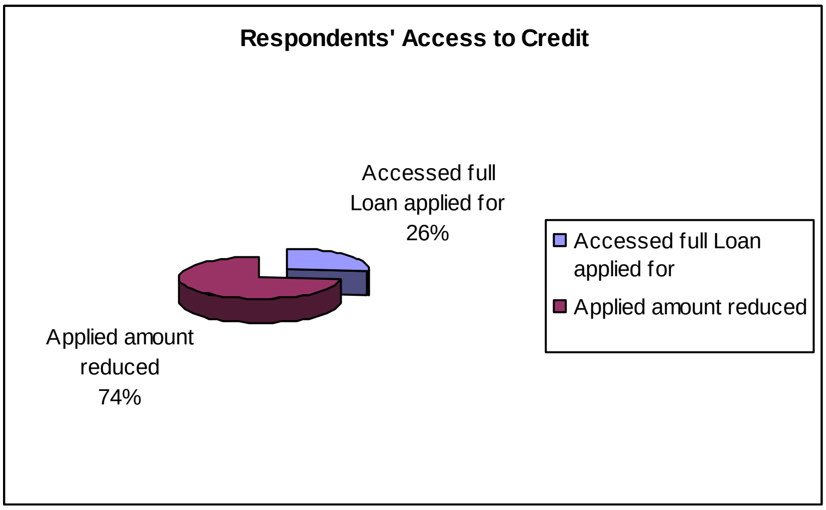

Figure 4.5: Respondents' access to credit

The 26 percent of the respondents who could not get the full amount of credit applied for said it was due to the following reasons: institution policies, creditworthiness of the group to give guarantee, past performance of the enterprise, and inadequate collateral. According to the research findings, 98 percent of the respondents indicated that due to conditions which are attached in order for one to secure a loan from MFIs like, the requirement of operating a savings account results in the following effects to the enterprise: small portion of the profits being reinvested into the business; lack of independent decisions; business expansion restricted; and not able to exploit other viable opportunities. These are detrimental to the success of the enterprise because the enterprise owners are compelled to save just to be in line with the lending institution's policies but this is done at the expense of the enterprise's survival.

4.2.5 Repayment period

The credit methodology of most Micro Finance Institutions like the Foundation for International Community Assistance (FINCA), which insists on weekly repayments, limits business growth by not providing sufficient time to make a profit (Orr & Makawa, 2000). Out of two hundred and eighty respondents, 85.5 percent representing 239 respondents repaid the loan on a weekly basis while only 14.5 percent representing 41 respondents had an opportunity to repay the loan fortnightly.

Due to Micro Finance Institutions' insistence on weekly loan repayments, 97.2 percent of the respondents indicated that they were not given the opportunity to discuss the repayment terms while 2.8 percent indicated that they discussed the repayment terms. Figure 4.6 below shows that two hundred thirty two respondents representing 83 percent had difficulties in raising the repayment amounts due to the weekly repayment arrangement. Only 48 respondents representing 17 percent were able to generate repayment amounts within the week as arranged. This has the effect of taking part of the working capital to repay the loan thereby gradually killing the enterprise in due course.

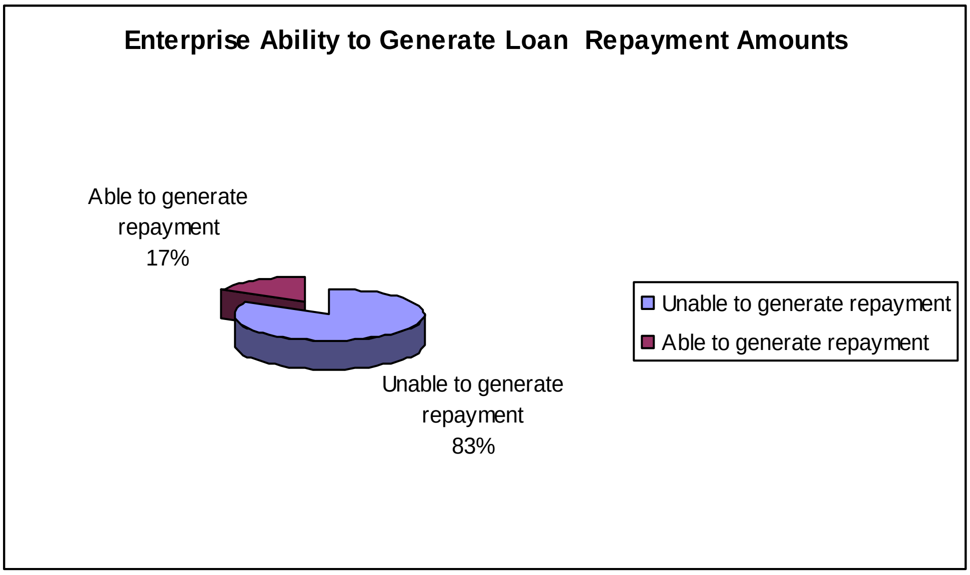

Figure 4.6: Enterprise ability to generate loan repayment amounts

4.2.6 Cost of finance

4.2.6.1 Variation in the elements of cost of finance

Respondents gave mixed reactions because each respondent valued each element of cost of finance differently. This variation is illustrated in Figure 4.7 below.

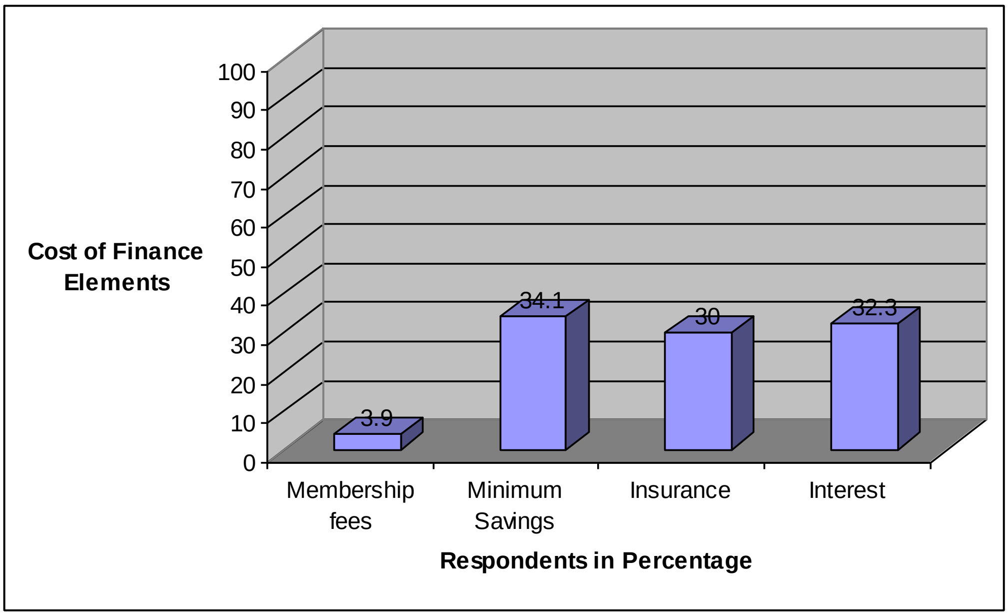

Figure 4.7: Variations in cost of finance elements

As can be seen from figure 4.7 above, 34.1 percent of the respondents viewed the requirement of having a savings book account for one to get a loan as cost to that loan. Those that viewed interest as a cost of capital when one gets a loan were represented by 32.3 percent while 30 percent of the respondents said insurance was the most worrisome cost of finance when one secured a loan from MFIs. Only 3.9 percent alluded to membership fees as cost of finance when one secured a loan from lending institutions. Therefor, 96.4 percent of the respondents concurred that the cost of finance such as minimum savings, interest and insurance have the effect of retarding the operations of the enterprises as well as their working capital.

4.2.6.2 Effects of the cost of finance on the performance of the business

Respondents cited two effects that were brought about by the cost of finance to the business, namely, dwindling capital and reduction of profits. As such, 25.9 percent of the respondents said the cost of finance prevents the capital from growing while 74.1 percent were of the view that it reduces the profits that were supposed to be accruing to the business.

4.2.7 Sources of finance

MSEs received financial assistance from a variety of sources that include both formal and informal sources. These are shown in the Figure 4.8 below.

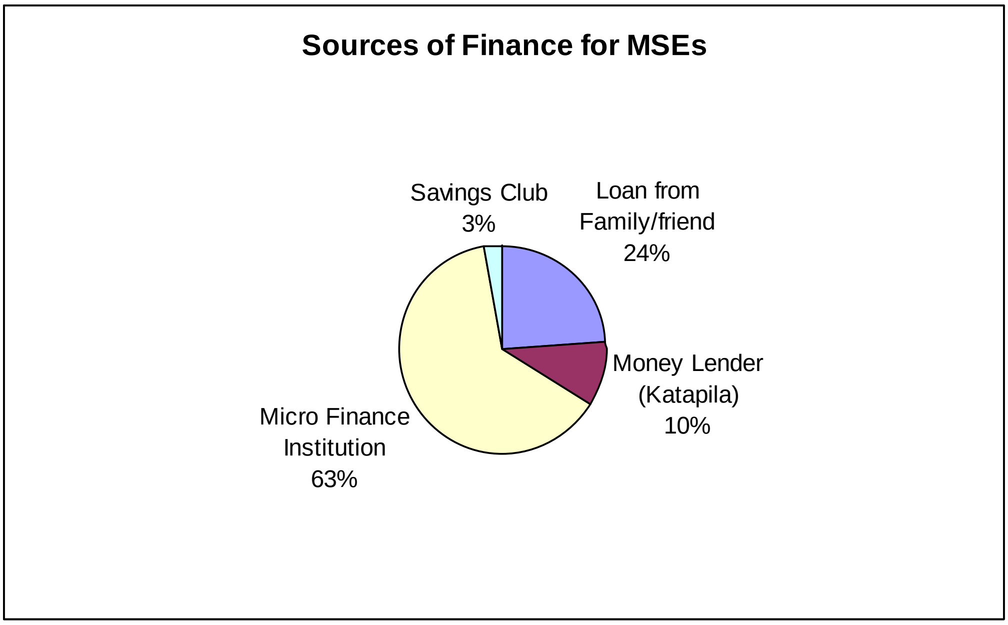

Figure 4.8: MSEs sources of finance

Owners of MSEs were asked if they got financial assistance from other sources apart from the Micro Finance Institutions. There were positive responses from the respondents. Figure 4.8 above shows that 63 percent secured a loan from micro finance institution only, 24 percent got loans from family and friends in addition to what they got from micro finance institution and 10 percent got additional credit from moneylenders (*katapila*). Borrowing from savings clubs (three percent) is relatively small compared to other sources. It is interesting to note that family/friend is an important source of credit in urban as well as rural areas. However, having 37 percent of the respondents securing loans from other sources like family/friend, savings clubs and moneylenders (*katapila*) shows that there is a deficit in terms of proper sources of finance. This has a negative effect on the operations and continuity of MSEs because those other sources are not reliable in that they at times call for their money prematurely or they charge exorbitant interest rate on the borrowed funds.

4.2.8 Cost of operations

According to Huff and Wade (1999) the cost of operations for a micro and small enterprise may be underestimated in the early days of establishment. For instance, the cost of renting premises and mobilization of the initial resources is very high. Figure 4.9 below outlines the outstanding activities that an enterprise engages while in operation.

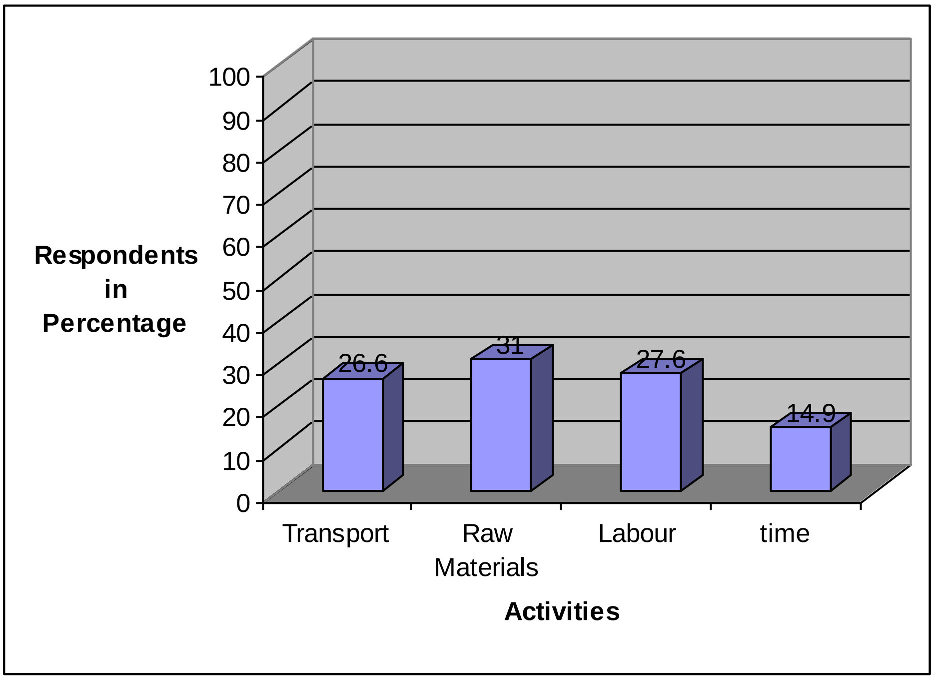

Figure 4.9: Activities taking place in an enterprise

Figure 4.9 above shows that 74 respondents who represented 26.6 percent rated transport costs as the activity which has the highest negative impact of all the operations taking place in the business. The respondents justified this by saying that transport fares are very high and that the respondents incur those expenses almost on a daily basis. Eighty seven respondents representing 31 percent said of all the activities taking place in the business, raw materials costs are negatively impacting on the operations of the enterprise because most of the raw materials are bulky and that they get them from far. So, in addition to the cost of raw materials, they add transport costs thereby making the material cost very high. Labour costs were labeled as highly impacting on the operations of the enterprise by 77 respondents, representing 27.6 percent; they said because it is a fixed cost i.e. regardless of whether the business has performed well or not they had to pay their workers/labourers. Those that viewed time costs as impacting on the operations of the business were represented by 47 respondents which is 14.6 percent of the respondents. Therefore, combining those costs it is seen that the enterprises at the end of the day are paying out far much more than they can realize in profits.

4.2.9 Economic issues in the country

According to the GEMINI report (2000), any business' success depends on the stability and prosperity of the economy in that particular country. From the research findings, 232 respondents representing 82.7 percent indicated that the country's economic elements affected the running of the enterprises while 48 respondents representing 17.3 percent said that they had no problem with the economic elements as they run their business. It has been noted from the study that when the country's economic elements like inflation are very high, exchange rates are not stable, interest rates are not controlled and fluctuate anyhow, money supply is very low, and consumers' incomes are low, leading to extremely low buying power from the locals, Micro and Small Enterprises are the worst hit. Figure 4.10 below further shows how these elements negatively impact on the efforts of Micro and Small Enterprise to succeed.

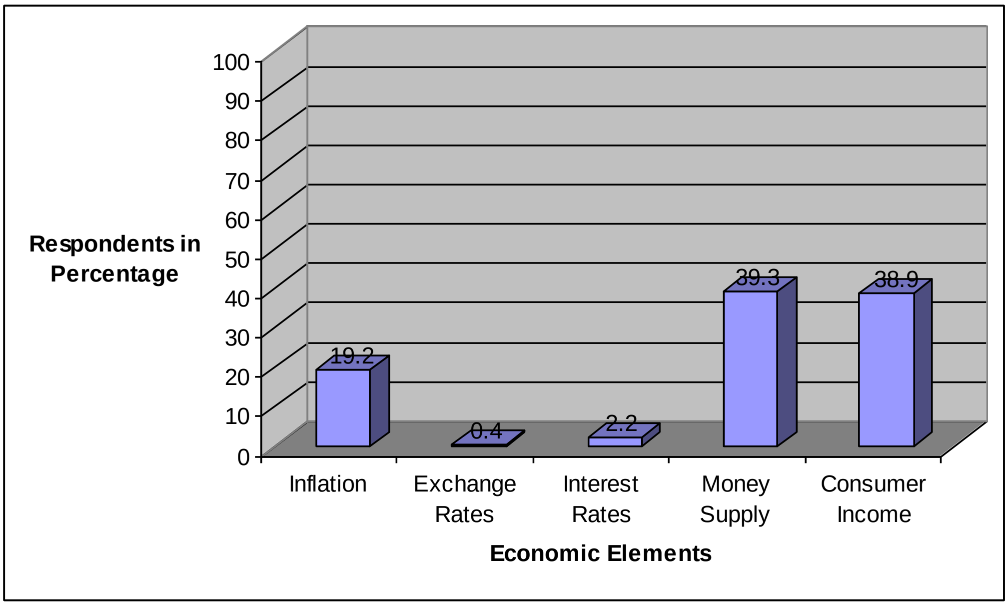

Figure 4.10: Effects of economic elements on MSEs

Figure 4.10 above shows that from the total study sample 19.2 percent of the respondents said that high inflation in the country affects their business prosperity while 39.3 percent cited low money supply as the element with the most economic impact that affect their business. Low consumer income was amongst the frequently noted economic elements affecting the enterprises operations. As in figure 4.10 above, 38.9 percent of the respondents mentioned it as the element hindering business operations. Only 0.4 percent and 2.2 percent of the respondents mentioned exchange rates and interest rates respectively as economic elements effecting their business operations. These results correspond well with the percentage of those who said that the country's economic elements do affect the operations and the viability of their enterprises.

4.3 Chapter summary

This chapter has presented the findings from the data that was collected from the respondents as well as secondary data on the factors that lead to the failure of Micro and Small Enterprises in Malawi. The primary data having been analysed using SPSS and being complemented by the secondary data from Government publications, world wide websites (internet), journals and books clearly show that in addition to other factors there are noticeable financial factors that lead to the failure of Micro and Small Enterprises in Malawi namely, startup capital, usage of retained profits, loan repayment arrangements, country's economic elements, sources of finance, cost of operations, lack of credit, cost of finance, multiple investments, and working capital management.

It has also been noted that the impact brought in by these financial factors is related to the capabilities and level of management of the entrepreneurs themselves.

CHAPTER FIVE

DISCUSSION OF FINDINGS

5.1 Introduction

This chapter presents the discussion of the results obtained in this study as outlined in the preceding chapter. The relevant observations from literature review on the financial factors leading to the failure of MSEs namely, start up capital, multiple investments, working capital/retained profits management, investment protection, access to credit, repayment period, cost of finance, sources of finance, cost of operations, and the country's economic elements are discussed to further justify the study findings.

5.2 Financial factors discussed

5.2.1 Start up capital

The securing of sufficient capital at inception and the maintenance of an appropriate capital structure are critical for the survival of micro and small enterprises (Boardman, at al. 1981). The study results revealed that a lot of Micro and Small Enterprises in the area of study operated with insufficient capital which in most cases did not meet the initial needs to a vibrant start of the business. As can be seen from Figure 4.3b above which shows that over 90 percent of the respondents' enterprises had a start up capital of far less than MK 50, 000 while less than one percent of the respondents' enterprises had a start up capital of more than MK 100, 000. With this trend, it is likely that most MSEs in Malawi do fail at infancy. This can be attributed to the lack of proper insight of the requirements for a particular venture to take off smoothly. According to Honjo (2000), those enterprises that lack sufficient start up capital to sustain their operations are expected to fail.

5.2.2 Multiple investments

Ownership of multiple enterprises reduces growth of the individual enterprises due to lack of proper time planning to pay attention to all the running enterprises (Chirwa, 2004). Chirwa further noted that ownership of multiple enterprises is statistically significant at the five percent level in the MSE model in Malawi and has a negative influence on profitability. This is complemented by the study results in Table 4.1 above which show that 90.9 percent of those enterprises that had multiple investments failed to attain growth, meaning that only 9.1 enterprises managed to do well despite multiple investment. In addition, the results show that most of the MSEs (61.8 percent) in the study area opted for multiple investments, hence many MSEs failed. This can be blamed on the tendency of Micro and Small Enterprises owners in Malawi who venture into other businesses because they have seen a friend or neighbour doing well in a particular venture.

5.2.3 Financial management

Proper management of purchases, inventory, retained profits and Work In Progress (WIP) can help to avert cash flow problems. Therefore, the ultimate result of poor cash flow management is lack of working capital to run the daily enterprise activities. Boardman, et al. (1981) noted that unsuccessful managers also mismanaged those resources that were available and/or failed to determine appropriate policies to finance subsequent growth of the business.

5.2.3.1 Utilisation of retained profits

To avert market downtrends and seasonal slowness which negatively affect the operations of micro and small enterprises, the enterprises need to make sure that their investment is protected and see to it that they have enough cash reserves. According to the study results, this is not the case with most of the Malawian micro and small enterprises. In figure 4.4 above a total of 66.4 percent of the respondents never thought of boosting their business capital by reinvesting the retained profits. The results further show that the retained profits were more prevalently used for meeting basic household needs and other payments which were not business related. The study findings concur with the Gemini Report, (2000) findings that Malawi's MSEs owners tend to focus on meeting basic household needs and not saving in order to reinvest in the business for growth and hedging for unforeseen circumstances from the market. According to McGrath (1999), failing to prepare for volatile markets and uncontrollable costs like energy-rate increases, materials, labour, natural disasters, and the like is a top reason many businesses fail.

5.2.3.2 Effects of loans on working capital

Despite accessing loans from Micro Finance Institutions (MFIs), the enterprises under study seemed not to have improved on their working capital. The number of respondents' enterprises that had a working capital of less than MK 50, 000, according to the study results, kept rising even after getting the loans. In table 4.2 above, over 80 percent of respondents' enterprises operated with far less than MK 50, 000 as working capital despite obtaining the loan six months earlier. In addition to the financial mismanagement by the enterprise owners, the retarded growth of working capital can also be attributed to the small amounts of loans that the enterprises get from the lending institutions. Most of the enterprises do not get the full amounts they applied for. As shown in figure 4.5 above, 74 percent of those enterprises that applied for financial assistance from lending institutions did not get the full amount of the loan requested. As such they did not accomplish the plans put in place to successfully run the enterprise to avoid failure. Even the profit they got out of the small working capital was not enough to sustain the business since from the same profit they paid interest and insurance, and used it to meet basic household needs.

5.2.4 Access to credit

The study found evidence of substantial excess demand for finance from lending institutions by MSEs. However, a higher proportion of respondents who applied for loans received less amounts than applied for. As figure 4.5 above shows, only 26 percent of the respondents were able to get the full loan amounts they applied for. Therefore, the reduced loans received by the remaining 74 percent were less effective to efficiently run the enterprises. Perhaps this is not surprising in light of the magnitude of barriers that the micro and small enterprises face in accessing credit. Lack of tangible security by MSEs, the limited capacity, outreach and linkages by financial intermediaries and a hostile legal and regulatory framework for financial services are the main constraints. According to Botswana Government (1999) lack of access to adequate finance by micro and small enterprises has been identified as the main problem confronting the MSEs. In addition to the small loan amounts the enterprises got from the lending institutions, they were compelled to operate a savings account, as per lending institutions policies. Instead of reinvesting the proceeds from the enterprise operations some funds were deposited just to be idle in the bank. According to this study findings, 98 percent of the respondents cited the following negative effects as a result of the attached conditions to getting the loan: small portion of the profits being reinvested into the business; lack of independent decisions by enterprise owners; business expansion restricted; and not able to exploit other viable opportunities. These effects were very detrimental to the success of the enterprises, not only in Malawi but elsewhere too (Kayanula and Quartey, 2000).

5.2.5 Loan repayment arrangement

According to Chirwa (2004), poor loan repayment arrangements limit enterprise growth by either not providing sufficient time to make profits which can be reinvested into the business for its survival, or by not providing peace of mind to the enterprise owner to have ample time to formulate practical strategies that will see to it that the objectives of the enterprise are achieved. The study results revealed that most micro finance institutions preferred very short repayment period for the loan they extended to their clients (MSEs). Out of 280 respondents, 85.5 percent repay the secured loans on a weekly basis. That was not out of their will and results in the collected data indicate that 97.2 percent of all the respondents were not given an opportunity to discuss the repayment terms with the lending institution. As asserted by Orr & Makawa (2000), repayment periods which are very short and not arranged by both parties do limit enterprise expansion since there is no time to generate profits which at times are used as source of finance to the enterprise by retention. Results in Figure 4.6 above show that 83 percent of the respondents had difficulties in raising revenues from which to pay the loans. This confirms what Orr & Makawa (2000) observed in their study. Upon probing what happens when the repayments amounts are not available when due, the respondents said that they had no choice but to use part of the working capital to repay the loans. That had an effect of reducing the working capital resulting in business failure. At times they were forced to go to informal moneylenders to get funds for loan repayment. The moneylenders charge very high interest rates which the MSE owners are not able to pay back. In other words it meant servicing two loans at the same time, thus putting financial pressure on the enterprises.

5.2.6 Cost of finance

If the cost of finance is too high it creates unnecessary burden to the enterprise in that it has to generate enough revenue to cover those costs but at the same time should remain viable. There are a number of elements that make up the cost of finance but the study looked at the following: membership fees, minimum savings, insurance, and interest. The results of the study as shown in Figure 4.7 above indicate that a total of 96.4 percent of the respondents were of the opinion that the above mentioned elements retard operations of the enterprises more especially on the retained profits.

From the little profits that the enterprises realized from the businesses, they were compelled to pay insurance and interest to the lending institutions. In addition to that they were asked to make deposits in their savings accounts. They did all that at the expense of the enterprises' operations. This has an effect of diminishing the working capital and in turn reducing the profits. In addition to that, 25.9 percent of the respondents mentioned that cost of finance retards the growth of capital and 74.1 percent were of the view that cost of finance reduces the profits that were to be reinvested nto the business.

5.2.7 Sources of finance

Analysed data as shown in figure 4.8 indicate that most MSEs perceived borrowing as necessary for business and the impact of borrowing on business performance as positive. However, this has not been what the enterprises have experienced.

While it was obvious that the respondents to the study questionnaire were clients of a micro finance institution, still a question on other sources of finance was included in the questionnaire. Interestingly, the response to this question was so positive that the study gathered that despite having secured a loan from a micro finance institution, the respondents still had to source finance from elsewhere. Three other sources of finance came out and these were; savings clubs, family/friend, and informal moneylenders (*katapila*). In figure 4.8 above it is shown that a total of 37 percent of the respondents seek additional financial assistance from other sources to top up whatever they sourced from the micro finance institution. This proved to have a negative effect on the profitability of the MSEs and their continuity because instead of servicing one loan from the MFI they had several loans to service. Considering that loans from other sources, for instance, informal moneylenders, are highly priced in terms of interest rates, most of the profits that the enterprises realised were drained into paying back to the other sources. At times those other sources call for their money prematurely causing the enterprise to panic. So if they do not have reserved cash, which they usually do not, as seen in Figure 4.4 above, that most of the funds are used for meeting basic household needs, then they lose out the capital to the moneylenders and this results in the closure of the enterprise.

5.2.8 Cost of operations

The financial strength of a firm as well as the cost of operations were factors to consider in the failure of a business in several studies (Grossi, et al., 1987; Honjo, 2000; Huff & Wade, 1999; Watson, 1999). In this study too, cost of operations was one of the financial factors considered for assessment in the failure of Micro and Small Enterprises in Malawi. The elements of the cost of operations that were considered in the study were, transport costs, materials costs, and labour costs. In figure 4.9 above, a total of 85.2 percent of the respondents agreed that transport costs, materials costs and labour costs are the cost of operations' elements that highly impact negatively on the operations of the enterprises. The enterprises get their trading materials from far; because of the rise in the prices of the commodities, they spend more on both the commodities themselves as well the transport to ferry them to their working stations. The respondents also rated labour as another cost of operation element that impact negatively on the enterprises operations. Because labour is a fixed cost, regardless of whether the business has done well or not, the enterprise owners has to pay their labourers. Therefore, the combination of these costs is so big that the enterprises can not stand, as such they fall out of the business.

5.2.9 Effects of economic elements

The study restricted itself to the following as economic elements that can affect the operations of the enterprises: inflation, exchange rates, interest rates, money supply, and consumer income. The analysed data in figure 4.10 above shows that a total of 82.7 percent of the respondents representing 232 respondents agreed that the country's economic elements negatively affect the operations of the enterprises. When the inflation is very high, pricing decisions are very difficult to come by. Where exchange rates are not stable and interest rates not controlled thereby fluctuating anyhow, financing options/decisions become problematic, when the money supply is very low resulting in no buying power from the consumers, realizing revenues for the enterprises is very difficult. Therefore, in such situations, the Micro and Small Enterprises are the ones that are hit the most. Therefore, from the results in figure 4.10 above, it is shown that low money supply and low consumer buying power are frequently mentioned by almost 78.2 percent of the respondents as the factors slowing down the growth of the enterprises. With the current fiscal measures that the country is experiencing, the common person does not have substantial amounts of money in the pocket as such no buying power at all to boost the revenues of the enterprises to avoid failure. Considering the percentage of the respondents agreeing that money supply and consumer incomes negatively affect the operations of the enterprises, the study confirms that indeed economic elements in the country are, to a considerable extent, leading to the failure of MSEs in the country.

5.3 Chapter summary

This chapter discussed and evaluated the study findings as outlined in the preceding chapter. What is clear is that there are substantial financial factors that complement other factors in negatively affecting the operations of the MSEs in Malawi leading to their failure. However, the effect is magnified by the lack of capabilities and management skills by the enterprise owners themselves.

CHAPTER SIX

CONCLUSIONS AND RECOMMENDATIONS

6.1 Introduction

The findings of the present study contribute to the practice and theory of Micro and Small Enterprises failure in Malawi in several ways. First, the study reveals the influence of key financial factors to the failure in Micro and Small Enterprise business. Second, the study results are based on the opinion of venture capitalists and Micro and Small Enterprises operators who are involved in the planning, executing, financing, and day to day activities of running the enterprises. Third, the study provides guidance to those who will focus on the key financial factors leading to business failure. Fourth, some of these factors are under the control of the entrepreneurs themselves, as such they can be acted upon. Consequently, the study results will benefit those who would like to improve the sustainability of their enterprises. It is important to note that the same kind of factors play a role in both large and small businesses. These findings will help entrepreneurs when starting up their enterprises, they will be able to study successful models and hopefully avoid the pitfalls many entrepreneurs fell into.

6.2 Conclusions

The analysis of the primary and secondary data collected by the study has shown that there are some financial factors associated with Micro and Small Enterprises failure. This is evidenced by the larger percentages of the respondents who cited the financial factors as playing a bigger role in down grading the enterprises operations. However, there is a variation in the influence among the factors. Some factors like, unarranged loan repayment period, country’s economic elements, and low money supply have been rated highly on the influence they have on the operations of the enterprises. This suggests that the failure of Micro and Small Enterprises is contributed by financial factors alongside the other factors.

The results also reveal that a good number of enterprise owners do lack financial expertise in such areas as controlling expenses, cash-flow planning and forecasting, and capital maintenance. Such skill deficits are particularly problematic during start-up, although they tend to be perceived as obstacles even after a business has begun to thrive, largely because it is so difficult to make up for early drawbacks.

The finding in this study that a lack of financial management competencies is implicated in the financial factors contributing to enterprise failure is consistent with the perspective in the literature review above that firms' performance is a function of intangible processes that need special attention.

Further to the lack of financial management competencies by enterprises owners, it is also observed that lack of access to full amount of loan applied by MSEs limits business expansion therefore suggesting in part, the MSE's concentration in the trading business as shown in Figure 4.2 on page 34 above, where less start up capital is required.

Finally, this study adds credence to the view that there is value to be gained from the study of failed organizations. Just as medical scientists would be unlikely to progress by studying only healthy individuals, likewise, micro and small enterprise database may be limited in the knowledge attainable from the study of successful firms hence the justification of the study on the failed enterprises.. While these findings shed some light on why micro and small enterprises fail due to financial factors, the study from which these findings have been drawn is not without limitations as already indicated in chapter one above. Perhaps the most obvious is the lack of financial resources that limited the researcher from drawing the study sample from a larger population. However, post-mortem analysis is not without precedent, nor is it without value, and the influences of the financial factors on the MSEs operations that have emerged represent a meaningful contribution to a clearer understanding of Micro and Small Enterprises failure.

What is important to note is that the study of business failure can be undertaken under a more information rich environment if an effort is made to examine the general factors that lead to failure of Micro and Small Enterprises instead. An extension of the work here could involve examining a much larger data base of MSEs that have undergone a near-death experience and tabulating the major factors that led to each enterprise's crisis and then comparing those to the ones cited in the literature that lead to business failure.

6.3 Recommendations

This study has discussed several factors which have a direct negative impact on the operations of the micro and small enterprises in Malawi. The recommendations in this section are made for micro and small enterprise owners to take note and focus on the key financial factors that lead to the failure of the enterprises if they are to be sustained. The recommendations are also made for other stakeholders like the micro finance institutions to encourage the entrepreneurs that they deal with to seriously give attention to the financial factors leading to business failure once they notice their negative impact. In addition to that, the recommendations are made for the micro finance institutions to provide the financial assistance to the MSEs with moderate conditions which will benefit both parties.

6.3.1 Start up capital

There is a tendency by micro and small enterprises owners to venture into a business with insufficient capital. This means that they do not satisfy the needs of the enterprise as such failure results. Therefore, there is need for the micro and small enterprise owners to be guided by meaningful business plans that will outline the activities and financial requirements before fully engaging into any business.

6.3.2 Multiple investments

The study reveals that ownership of multiple enterprises reduces growth of the individual enterprises due to lack of proper time planning to pay attention to all the running businesses. This finding concurs with what Chirwa (2004) found in his study of Gender and Performance of Micro and Small Enterprises in Malawi. So there is need for micro and small enterprises owners to concentrate on one enterprise in order to have enough time for proper planning and overseeing the enterprise activities. Therefore, apart from sparing enough time to nurse the affairs of the enterprise, the concentration on one enterprise will enable the only enterprise to have sufficient capital to satisfy its needs.

6.3.3 Financial management

With the escalating issues of financial mismanagement as revealed by the analysis of data, MSEs owners have failed to fruitfully manage the retained profits and the working capital which resulted in the enterprises failing. Therefore, there must be a joint effort by the government and the lending institutions to organize seminars or sessions on financial and business management for the MSE's owners to prepare them before they get the loans. The government should also ensure that this requirement is included in the MSEs Policy Statement which safeguards the existence of Micro and Small Enterprises in Malawi. This will benefit both the lending institutions as well as the enterprise owners in that the enterprise owners will be equipped with financial management skills and therefore ably repay the loans as required by the MFIs.

6.3.4 Sources of finance (access to credit and cost of finance)

The study reveals that there are very stiff conditions attached to securing a loan with the MFIs and high cost of finance too which result in pulling backwards the operations of the micro and small enterprises. As such, there is need for devoted intervention by government to regulate the MFIs policies and conditions so that MFIs apply uniform and amicable policies and conditions to the MSEs. This intervention if implemented will ease access to credit and improve on the MSEs' working capital. This will enable the enterprises to have adequate start up requirements, as such, there will be a smooth take off hence avoiding failure at an early stage. In addition to the MSEs having easy access to loans hence improving on working capital, with the amicable and uniform policies and conditions, the MSEs owners will be able to discuss flexible terms with the lending institutions on issues like the repayment periods for the loans acquired.

6.3.5 Country's economic elements

There is need for the government to revisit its monetary policies so that the money supply in the country is at a reasonable level. The government should strive to strike a balance on money supply, that is, the common man should have adequate money supply to boost the buying power but at the same time the money supply should not be inflationary. This will ensure that the enterprises will be able to turn over its supplies in the shortest time possible.

6.3.6 Further research

Given that it is difficult to reach all the districts in the country and address all the financial factors leading to the failure of Micro and Small Enterprises in one single study, future studies may benefit by investigating the influence of additional factors not addressed in the current study, such as the financial viability of the product or service offered by the enterprises and the financial expertise of the entrepreneurs in terms of marketing and promotion.

6.4 Chapter summary

This chapter provides the conclusion and recommendations from the study findings. The chapter has concluded that indeed there are key financial factors that lead to the failure of Micro and Small Enterprises in Malawi. It has also recommended several remedies to the effects of observed financial factors.

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APPENDIX A: Student's Questionnaire

AN ASSESSMENT OF FINANCIAL FACTORS LEADING TO THE FAILURE OF MSE'S FUNDED BY MICRO FINANCE INSTITUTIONS IN MALAWI.

THE CASE OF FINCA ZOMBA CLIENTS.

QUESTIONNAIRE REFERENCE NUMBER …………………..

UNIVERSITY OF MALAWI – THE POLYTECHNIC.

EXECUTIVE MASTER OF BUSINESS ADMINISTRATION

DEGREE PROGRAMME –

RESEARCH QUESTIONNAIRE.

Date of Interview	
Name of Enumerator	

A.	GENERAL INFORMATION	
A1.	Name and address of the respondent/business	
A2.	Age of the respondent	**Tick** (a) Up to 20 years ☐ (b) 21 to 35 years ☐ (c) 36 and above ☐
A3.	Highest educational qualification of the respondent How about no formal education?	**Tick** (a) Not at all ☐ (b) Primary ☐ (c) Secondary ☐ (d) Tertiary ☐

A4.	Area of the business in Zomba	**Tick** (a) Songani/Malosa Cluster ☐ (b) Thondwe Cluster ☐ (c) Jali/Kachulu Cluster ☐ (d) Zomba Central Cluster ☐ (e) Chingale Cluster ☐
A5.	Have you ever been interviewed on business matters before? *(If NO go to A8)*	Yes ☐ No ☐
A6	If Yes, How many times	**Tick** Once ☐ twice ☐ Thrice ☐ Other *(please specify)* ☐
A7	What was it about?	**Tick** (a) Business ☐ (b) Financial institution ☐ (c) Products ☐ (d) Other *(please specify)* ☐
A8.	Is the business female-led or male-led?	Female ☐ Male ☐

B	BUSINESS INFORMATION	
B1	What is the nature of your business?	**Tick** (a) Trading ☐ (b) Manufacturing ☐ (c) Service ☐ (d) Other (please specify) ☐
B2.	Date business started?	
B3.	How long have you been in this business?	**Tick** (a) Less than one year ☐ (b) Between 1-4 years ☐ (c) Between 5 -9 years ☐ (d) 10 years and over ☐
B4	How much was the starting capital?	**Tick** (a) Less than K50,000 ☐ (b) K50,000 - K100,000 ☐ (c) K100,00 or more ☐
B5	Is the business registered?	Yes ☐ No ☐
B6.	What type of business is it?	**Tick** (a) Sole proprietor ☐ (b) Partnership ☐ (c) Franchise ☐ (d) Other (*please specify*) ☐

B7.	What led you start this business	**<u>Tick</u>** (a) Own idea ☐ (b) Encouraged ☐
		(c) Availability of capital ☐ (d) Other (*please specify*) ☐
C	**MULTIPLE INVESTMENTS.**	
C1	Did you use the funds (borrowed) according to the registered business plan? *(If YES go to Section D).*	Yes ☐ No ☐
C2	If not, how much of the acquired loan was used in the presented/stated business plan?	%
C3	How did you use the other funds?*(Multiple response)*	**<u>Tick</u>** (a) Domestic spending ☐ (b) Reinvestment ☐ (c) Banked for future use ☐ (d) Pay other loans ☐ (e) Other *(please specify)* ☐
C4	What motivated the multiple investments?	**<u>Tick.</u>** a. Viable business at that Particular time ☐ b. Excitement (not sticking to ☐ business plan) c. Fear of low return from one business to ensure weekly or monthly ☐ d. instalments ☐ e. Dual business in the family. ☐
		Other *(please specify)*

C5	If you diverted the funds into other businesses, did you succeed in both/all businesses? (If YES go to section D)	Yes ☐ No ☐
C6	If NO, why	**Tick** (a) Under funding ☐ (b) Preferential bias ☐ (c) Viability ☐ (d) Other *(please specify)* ☐
D	**FINANCIAL MANAGEMENT**	
D1	How did you acquire skills on how to manage your finances	**Tick** (a) Experience from past activities ☐ (b) Financial manegement advice (formal or informal) ☐
		(c) Just handle as they come (no skills) ☐ (d) Other *(please specify)* ☐
D2	How do you manage or monitor your finances	**Tick** (a) Record keeping ☐ (b) Availability working capital ☐ (c) Other *(please specify)* ☐

D3	How do you manage the retained profits?	**Tick** (a) Bank account ☐ (b) Cash reserve ☐ (c) Re-investment ☐ *(In the same business)* (d) Domestic use ☐ (e) Diversificastion ☐
D4	What was your working capital before you got the loan?	**Tick** (a) 0 -20,000 ☐ (b) 20,000 – 50,000 ☐ (c) 51,000 – 100,000 ☐ (d) 100,000 - more ☐ (e) Other (*please specify*) ☐
D5	When did you first acquire loan?	
D6	What was the working capital after the loan was acquired	
D7	What is your working capital now?	
E	**BORROWED FUNDS.**	
E1	Were you able to get the working capital you required? (*If YES go to E2 and E3, if NO go to E4 and E5*).	Yes ☐ No ☐
E2	What were the conditions attached for you to get the working capital?	**Tick** (a) Membership to a group ☐ (b) Savings account ☐ (c) Business experience ☐ (d) Guarantee from the group ☐ (e) Other (*please specify*) ☐

E3	How did the conditions in E2 above affect the performance of the business after getting the working capital?	**Tick** (a) Little profit retained to the business ☐ (b) No independent decisions at times ☐ (c) Other (*please specify*) ☐
E4	What led to the reduction of the working capital applied for?	**Tick** (a) Business plan not viable. ☐ (b) Institution policies ☐ (c) Creditworthiness of the Group. ☐ (d) Past performance ☐ (e) Other *(please specify)* ☐
E5	How did this affect the success of your business	**Tick** (a) Operated on low capital. ☐ (b) Business expansion Restricted. ☐ (c) Exploitation of other opportunities impossible ☐ (d) Other *(please specify)* ☐

F	REPAYMENT PERIOD	
F1	What has been the repayment period for your working capital loan?	**Tick** (a) Weekly ☐ (b) Fortighty ☐ (c) Monthly ☐ (d) Other (*please specify*) ☐
F2	Is this in line with your business ability to generate repayments units? *(If Yes go to F5)*	Yes ☐ No ☐
F3	Are you given an opportunity to discuss the repayment period with your financier or it is imposed? (if discussed go to A5)	Can discuss ☐ Imposed ☐
F4	If imposed, give three advantages or disadvantages of this repayment period arrangement?	**Adv:** (a) You work hard to repay ☐ (b) You repay within the specified period ☐ (c) You plan well ☐
		Disadv: (a) You are given tough time ☐ (b) You risk repaying the ☐ (c) Working capital ☐
F5	Are you always making repayments in time?*(If YES go F7)*	Yes ☐ No ☐
F6	If NO why?	(a) Poor returns from sales ☐ (b) The repaymwent frequance short. ☐ (c) Stock turnover too long. ☐ (d) Other *(please specify)* ☐

F7	Are you able to repay the working capital from the revenues generated by the business? *(If Yes go to F9)*	Yes No
F8	If NO, state the other sources	(a) Spouse's salary ☐ (b)borrow from other people ☐ (c) From other institutions ☐
F9	Why the business is unable to repay the working capital on its own? *(give three reasons)*	(a) business not viable. ☐ (b) interest too high ☐ (c) repayment period too short ☐
F10	What is the cost of capital if borrowed from the micro-finance institutions? *(Multiple response expected)*	**<u>Tick</u>**
		(a) Interest ☐ (b) Membership ☐ (c) Minimum savings ☐ (d) Requirements ☐
		(e) Other charges ☐ *(please specify)*
F11	Which one of the factors in F10 affects your business the most?	
F12	How do the factor in F10 affect the performance of the business	(a) ☐ (b) ☐ (c) ☐
F13	How do you compensate the repayment from other sources *(answer this question and F14 if F8 is answered)*	(a) Use the next loan (b) Use the working capital (c) squeeze the returns.

		(d) Other (*please specify*)
F14	(e) How does this affect your business financially?	(a) No rentetion of profits. ☐ (b) Expansion not possible. ☐ (c) Financial planning a problem. ☐ (e) Other (*please specify*) ☐
G	**SOURCES OF FINANCE**	
G1	Apart from financial institutions, where else did you get the funds for your business?	**<u>Tick</u>** (a) Family members ☐ (b) Friends ☐ (c) Other *(please specify)* ☐
G2	What is the composition of your working capital	(a) % own capital/family member ☐ (b) % from friends ☐ (c) % from other (loans) ☐
G3	If you got loans from other financial institutions, do you ably service all the loans(if YES don't answer G4 & G5)	Yes No
G4	If NO why?	(a) Funds generated not enough ☐ (b) High cost of capital ☐ (c) Preferential bias. ☐ (d) Other *(please specify)* ☐

G5	What impact do the reasons in G4 above have on the operation of your business?	(a) Not able to get another loan ☐ (b) No impact ☐ (c) Other *(please specify)* ☐
H	**COST OF OPERATIONS.**	
H1	What activities make up your business?	**<u>Tick</u>** (a) Transportation ☐ (b) Raw materials ☐ (c) Labour ☐ (d) Time ☐ (e) Other *(please specify)* ☐
H2	What activity consumes much of your working capital?	
	Why?	(a)
		(b)
		(c)
		(d)
J	**GENERAL**	
J1	Has the economic issues in the country affected your business? *(IF No skip to J3)*	Yes ☐ No ☐

J2	Which one has significantly affected the business?	**Tick**
		(a) Inflation ☐ (b) Exchange rates ☐ (c) Interest rates ☐ (d) Money supply ☐ (e) Consumer income ☐
J3	Apart from the above financial factors, what other factors affect your business?	
J4.	Apart from extending loans to you, what other services did financial institutions (FINCA) provide?	**Tick.** (a) Financial advice ☐ (b) Security ☐ (c) Business management ☐ (d) Other *(please specify)* ☐
J5	How can you rate the quality of financial institutions (FINCA) services in terms of loans?	**Tick**
		(a) Much worse than I expected ☐ (b) About what I expected ☐ (c) Better than I expected ☐ (d) Much better than I expected ☐
J6	How can you rate the quality of financial institutions (FINCA) services in terms of financial advice	**Tick** (a) Much worse than I expected ☐ (b) About what I expected ☐ (c) Better than I expected ☐ (d) Much better than I expected ☐

		(e)
J7	Would you recommend a friend to join FINCA (finance institutions) *(if YES answer J8)if NO go J9)*	Yes ☐ No ☐
J8	Why (If YES)?	**<u>Tick</u>** (a) Interest rates are low ☐ (b) Interest rates well spread ☐ (c) Willingness to assist ☐ (d) No pressure on repayment of the loan ☐ (e) The group is the security hence no collaterals requires ☐ (f) Other services are Provided ☐
J9	Why (If NO)?	(a) Interest rates are high ☐ (b) Interest rates not well spread ☐ (c) Unwilling to assist ☐ (d) Pressure onrepayment of the loan ☐ (e) Within the group there are problem. ☐ (f) Other services are not provided ☐

APPENDIX B: Student's Letter of Introduction

UNIVERSITY OF MALAWI

PRINCIPAL
Charles Mataya, Ph.D., MS Ag Econ, BSc. Agric, Dip. Econ

Our Ref.:

Your Ref:

Date: 11th February, 2008

Please address all correspondence to the Principal
The Malawi Polytechnic
Private Bag 303
Chichiri
Blantyre 3
MALAWI

Tel: (265) 1 870 411
Fax: (265) 1 870 578
E-Mail: principal@poly.ac.mw

TO WHOM IT MAY CONCERN

ASSISTANCE TO CARRY OUT AN ACADEMIC RESEARCH FOR MBA DISSERTATION: MR. OWEN MASAULI

I write to certify that Mr. Owen Masauli is a University of Malawi Postgraduate student who is pursuing a Master of Business Administration Degree course at the Polytechnic.

One of the important requirements of this degree programme is that students carry out research project known as dissertation in the final semester. This introduces the student to the methodology of research, the systematic analysis of ideas, the problems of data collection and the presentation of ideas in a clear and coherent way. Mr. Owen Masauli is currently working on his MBA dissertation titled "An Assessment of Major Factors leading to the Failure of SME's in Malawi, funded by Microfinance Institutions in Malawi: The Case of FINCA Zomba Village Banks ".

I am therefore writing to ask for your kind assistance in allowing Mr. Owen Masauli access to carry out his research in your organisation and help him with any information/literature that your organisation may have on the topic of his dissertation.

Your assistance in this matter will be of greatest importance and highly appreciated and any information that may be provided will be treated with utmost confidentiality.

J. M. BULIANI, PhD
ACTING HEAD OF MANAGEMENT STUDIES DEPARTMENT