SMES Performance and Venture Capital Financing in Benue State: The Essence

Benson Emmanuel PhD
Department of Banking and Finance, Federal University Otuoke, Bayelsa State
Corresponding author: besonemmanuel2014@gmail.com

Ogaga, Timiepere Cornelius
Department of Banking and Finance, Federal University Otuoke, Bayelsa State
timiepereo@gmail.com

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Abstract

This work investigate SMES Performance and Venture Capital Financing in Benue State. the researchers employed a survey research design to ascertain the effect of venture capital financing and annual sales of SMEs in Benue State and also determine the effect of venture capital financing and profitability of SMEs in Benue State. The study population was drawn from three major towns of the state and amounted to a total of 1640 with a sample size of 328 which was gotten using Yaro Yamane formula to arrive at the sample size of the study. Regression analysis was used to analysis the data and the findings shows that venture capital financing and performance of small and medium enterprise is significantly positive and concludes that Venture capital financing is a proven and influential factor in the survival and sustenance of small and medium enterprise performance across Benue State. The study recommends among others that Small and medium scale enterprises need to recognize the numerous benefits and potential advantages of seeking external equity finance for corporate sources.

1.0 INTRODUCTION

1.1 Background to the study

Without proper finance, SMEs can neither expand to compete globally nor can they acquire technology or meet their fixed and working capital requirements (Warijohi and Muguro, 2008). SMEs face significant challenges, which includes access to finance (Iwisi et al., 2003) and financial management skills and support (Gem Report, 2003). This has contributed to the slow and staggering development and high rate of mortality of small business in Nigeria. The role of finance has been viewed as a critical element for the development of SMEs (Cook and Nikson, 2000). Venture capital is an investment in a startup or growing SME that is perceived to have excellent growth performance prospects. Venture capital assist investors to access equity capital to finance expansion of business while maintaining control.

The expertise and extensive relationships of the venture capitalists through its network add value to the company and increase credibility with customers, and finally, the company gain access to the venture capitalist knowledge in accounting, budgeting, computer systems, and back office operations (Amisseh, 2009). In venture capital financing agreement, the venture capital firm will provide financing to enable a business to undertake a project and in return the venture capital company gets an ownership stake in the business (Boateng, 2010). Thus, improving some measures of an enterprise success is achievable either by boosting revenue of business with greater product sales or service income, or by increasing profit of operation simply by minimizing cost. Banney (2002) noted that growth of a firm has been based upon the idea that an organization is a voluntary association of productive assets, including human, physical, technological and capital resources, in order to achieve a common purpose. Baeyens and Manigart (2003) assert that venture capitalists screens potential investments in regards to collecting information about the business, its market approach, management team or entrepreneur, all in order to reduce the initial information asymmetry and potential problems with entrepreneurs. In other words, before final contracting, venture capitalists spends much of his time and efforts in assessing and observing the opportunity, in terms of its market size, strategies, customer adoption etc (Kaplan and Stromberg, 2001).

Reynolds (2000 as cited in Njama, 2013) asserts that venture capitalists needed to trigger, maintain and to speed up the small enterprise's growth and its performance, and therefore to result in improved profitability. Thus, its primary role, it is the main contributor in getting rid of the most financial impediments that occur in the establishing phase of a new business. Baeyens and Maringart (2003) asserts that venture capital has another attribute so important, that is providing credibility thus attracting new funding. This they explained by the fact that through screening, observing and value of adding, venture capitalists reduce the information asymmetries and financial risks, and therefore adjoin legitimacy to the venture backed company and consequently influence further financing. This in turn spurs growth and performance development of SMEs in the national economy in general.

Nonetheless, it is important to acknowledge that the agency relation between venture capital investor and the entrepreneurs of companies may engender conflicts leading to a deterioration of the performance of these companies. In fact, entrepreneur and external investors may have different strategic visions; disagreements may absorb the entrepreneurs' efforts and attention to the detriment of the pursuit of business opportunities (Njama, 2013). Even if no conflict arises, the need of venture capitalist to monitor managerial decisions may increase bureaucracy and formalization of decision processes, hampering flexibility and the ability of the firms to timely grasp business opportunities; furthermore, as venture capitalist are competent investors, they might be able to expropriate entrepreneurs of their innovative business ideas and exploit them also in their absence (Ueda, 2004).

In line with the above, the following hypotheses are stated;

H_{01}: There is no relationship between venture capital financing and annual sales of SMEs in Benue State

H_{02}: There is no significant relationship between venture capital financing and profitability of SMEs in Benue State

2.0 Literature Review

2.1 Theoretical Framework

Economic Entrepreneurship theory

Richard Cantillon in 1755 provided one of the earliest contributions regarding the economic strand of thought about entrepreneurship. Richard described an entrepreneur as a speculator who conducts all exchanges, and bears risks as a result of buying at certain prices and further selling them at uncertain prices. Centillion named it the risk theory of profit where anyone who receives an uncertain income can be regarded as an entrepreneur.

Furthermore, the theory stated the importance of entrepreneurs as people who play a key role in the economy by relieving the paralysis engendered by uncertainty and along with it allowing the exchange and production of goods and services so that market equilibrium can be attained. Cantillon further stated that an entrepreneur is not an innovator. They cannot change the demand and supply trends. Rather, they are perceptive, intelligent and willing to take risks. Their main role in the process is to bring two sides of the market together (Parker, 2018).

This theory was proposed by Richard Cantillon who considered the economy as one of the fields affected by entrepreneurship. According to Cantillon, an entrepreneur acts as both 'producers' and 'exchangers'. An entrepreneur's action greatly affects the supply chain of raw products being collected, to become an end product for consumers. Cantillon included everyone as an entrepreneur from their little actions starting from a beggar to restaurant owners as they also have their source of unfixed income; this counts as a unique factor and made his theory stand out from other entrepreneurship theories.

SMEs are vital for economic growth and development in both industrialized and developing countries, by playing a key role in creating new jobs. Financing is necessary to help them set up and expand their operations, develop new products, and invest in new staff or production facilities. Many small business start out as an idea from one or two people, who invest their own money and probably turn to family and friends for financial help in return for a share in the business. But if they are successful, there comes a time for all developing SMEs when they need investment to expand or innovate further. That is where they often run into problems, because they find it much harder than larger business to obtain financing from banks, capital market or other suppliers of credit. The financing gap is all the more important in a fast changing knowledge based economy because of the speed of innovation. If SMEs cannot find the financing they need, brilliant ideas may fall by the way side and this represents a loss in potential growth for an economy.

2.2 Conceptual Framework

Entrepreneurial Finance

Janet K. Smith and Richard L. S (2019), Just as corporate finance is concerned with financial decision- making by managers of public corporations entrepreneurial finance is concerned with financial decision- making by entrepreneurs who are undertaking new ventures. If the venture needs further infusion of funds, the entrepreneur will tap the banks and Non- Banking Financial Companies (NBFCs) for debt financing. Most entrepreneurs prefer debt financing equity

financing. The main disadvantages of equity financing that are overcome in debt financing are as follows:
1) Dilution of Shareholding: After taking on venture capital, the entrepreneur owns less of the firm and even the profits have to be shared.
2) Increased Third- Party Governance: Few entrepreneurs are happy with having to comply to a large number of norms and regulations.
3) Increased External Controls: In debt financing the entrepreneur has to incorporate the views of other investors before taking a decision.
4) Increased Commitment to stated strategy: While taking on external equity, the entrepreneur may have committed to a specific strategy. Changes in long-term strategy may be restricted by the agreement signed by the entrepreneur and the equity investors.
Entrepreneurial finance draws its basic principles from both entrepreneurship and finance. The seven principles are :
1) Real, human and financial capital must be rented from owners,
2) Risk and expected reward go hand in hand,
3) While accounting is the language of business, cash is the currency,
4) New venture financing involves search, negotiation and privacy,
5) A venture's financial objective is to increase value,
6) It is dangerous to assume that people act against their own self-interests, and
7) Venture character and reputation can be assets or liabilities.

Role of Entrepreneurial Finance

Entrepreneurial finance is the application of financial tools and techniques to the planning, funding, operations and valuation of an entrepreneurial venture (Smith & Richard,2019). Entrepreneurial finance focuses on the financial management of a venture as it moves through its lifecycle, beginning with its development stages and continuing through to when the entrepreneur exists or harvests the venture. Nearly every entrepreneurial firm will face major operating and financial problems during its early years, making entrepreneurial finance and the practice of sound financial management critical to the survival and success of the venture. Most entrepreneurial firms will need to re-group and re-structure one or more times in order to succeed. Financial distress occurs when cash flow is insufficient to meet current liability obligations. Alleviating financial distress usually requires r-structuring operations and assets or re-structuring loan interest and scheduled principal payments. Anticipating and avoiding financial distress is one of the main reasons to study and apply entrepreneurial finance. Generating Cash flows is the responsibility of all areas of the venture- marketing, production/engineering, research and development, distribution, human resources and finance/ accounting. However, the entrepreneur and financial manager must help other members of the entrepreneurial team relate their actions to the growth of cash flow and value. The financial manager is normally responsible for keeping the venture's financial records, preparing its financial statements forward for one to two years. The venture needs adequate cash to survive the short-run. Financial plans indicate whether the venture is expecting a cash shortage .If so, the entrepreneur should seek additional financing to avert the shortage. Long-term financial planning typically involves projecting annual statements five years forward. While the reliability of longer- term projections may be lower, it is still important to anticipate large financial needs as soon as possible. Meeting those needs may dictate several rounds of financing in the first few years of operations. The financial manager is responsible for monitoring the firm's operating efficiency and financial performance over time. Every successful venture must eventually produce operating profits and free cash flows. While it is common for a new venture to operate at a loss and deplete its cash reserves, it cannot continue indefinitely in that state. In summary, financial management in an entrepreneurial venture involves record keeping, financial planning monitoring the venture's us of assets and arranging for any necessary financing. Of course, the bottom line of all these efforts is increasing the venture's value.

2.3 Empirical Review

Capizzi et al. (2011), investigated the effects of PE/VC financing on the growth of 160 funded small companies in Italy, they found that PE/VC enhances value added per employee but only in the first year of VC funding. Memba, (2011) who concluded that VC-backed firms in Kenya easily attracted external debt financing. (Paglia & Harjoto, 2014) argued that the participation of the VCs in the funded companies, positively influences their growth in terms of increased number of jobs, nonetheless, they explained that the impact is rather short lived for the VC backed firms. This submission was persistent with the findings of Capizzi et al. (2011). It is therefore obvious that the accepted influence of VC contribution on firm performance remains inaccurate.

In an unlike dimension, Manigart and Van Hyfte (2012) studied 187 Belgian VC-backed firms but the results disclosed insignificant growth in employment matched to non-VC-backed firms of identical size and comparable lifetime. In the same way, Guo & Jiang, (2013) did not establish any evidence of progress in sales growth or R&D investment of the VC-backed firms after receiving VC funding. Instead, Gompers, (1996) encapsulated that VCs have resilient motivations to attract attention, by compelling VC-backed firms to prematurely go public, to allow them exit and acquire returns on investment timely. Metrick & Yasuda, (2011) is in agreement with the foregoing statement, divulging that the principal purpose of the VC firms is to reap high financial returns from their investments. In a different forum, Kelly, (2011) indicated that VC-backed firms provide derogatory returns on investment for VC firms. These results concur with Gompers, (1996) verdicts. Several studies have been conducted largely on measuring the impact of VC on firm performance, however, they present conflicting conclusions and have not reached a consensus.

3.0 METHODOLOGY

3.1 Research Design

The researcher adopted the survey research design (descriptive). Descriptive research design was chosen because it enable the researcher to generalize the findings to a larger population.

The population of the study is made up of all owners/managers/staff of registered SMEs from Makurdi, Gboko and Otukpo Local Government Areas, which are considered to have the highest concentration of SMEs in the state, and are the three major towns in Benue State.

Available statistics show the distribution as follows:

Makurdi	-	740
Gboko	-	480
Otukpo	-	420

Total	-	1640

Source: Benue State Ministry of Commerce and Industry, 2022

3.2 Sample Size Determination

The researcher used the Yaro Yamene (as cited in Olotu and Olopete, 2012) in determining the sample size, since the population is known. The formula is given as

$$n = \frac{N}{1+N(e)^2}$$

Where

n = sample size
N = population
e = level of significance (For this study – 0.05)

$$\therefore \quad n = \frac{1640}{1+1640(0.05)^2}$$

$$= \frac{1640}{5} = 328$$

$$= \underline{328}$$

The individual town sampling size for the 3 local governments is given as

SF = sample size ÷ population

Makurdi SF x 740 = 0.2 x 740 = 148
Gboko SF x 480 = 0.2 x 480 = 96
Otukpo SF x 420 = 0.2 x 420 = 84
Total 1640 328

3.3 Sampling Technique and Data Collection

Simple random sampling was adopted so as to give each item in the population equal opportunity of being selected. While purposive sampling was used to choose the firm based on the basis that they have used venture capital financing. The primary data were collected through questionnaire administration.

3.4 Validation and Reliability of Instrument

That the research instrument (questionnaire) measured what it was intended to measure (validity) and that the result was consistent over several administrations (Reliability), the instrument was validated by three lecturers in the department of Business Administration and management in the areas of Financial Management, Entrepreneurial Studies and Human Resource Management. Thus issues raised were effected appropriately. A pilot study was done to ascertain the sampling adequacy (Kaiser-Meyer-Olin measure of sampling adequacy-KMO = 0.801) indicating the appropriateness of the factor analysis.

The reliability, which Hair et al (2006) views as how well the instrument (questionnaire) consistently yields similar results. And accordingly, opined that the Crombach alpha for determining how relevant the set of items are for a study should be more than 0.7 for the overall items tested. Thus our values surpassed 0.7, (0.792, 0.788, 0.854) which means the items have satisfied the need for inclusion in this study.

SPSS Version 21.0 for Windows Output Printout was used to test for the validity and reliability of the data.

3.5 Variable Specification

The regression model used to establish the form of relationship between dependent and the independent variable.

Thus, the model for this research is given as:

SMEP = F(SV+PR)

Where

SMEP = Small and Medium Enterprise Performance

SV = Sales Volume

PR = Profitability

Y = $a+\beta_1X_1+\beta_2X_2+e$

Where

Y = Depended Variable (Performance-measured through financial that is sale volume and, profitability).

χ_1 = Sales volume (improved technology, strategy, finance/credit from financial institutions and other affiliated institutions).

χ_2 = Profitability (returns on investment, expansion).

3.6 Data Analysis Technique

Questionnaire responses were gleaned, grouped into various categories and entered in the SPSS software to facilitate for analysis. Inferential statistics were employed to analyse the data using a regression model.

4.0 RESULTS AND DISCUSSIONS

4.1 Distribution and Collection of Questionnaire

A total of 328 copies of questionnaire were administered to the selected respondents of the study, out of which 242 were returned in analyzable form, thus representing 73% response rate.

4.2 Respondents view on annual sales

The data collected to substantiate this proposition is presented in Table 1.

Table 1: Summary of Respondents view on annual sales volume

S/No	Item Statement	SA	A	U	D	SD
1.	I am aware of the existence and benefits of venture capital financing	128(52.9%)	102(42.1%)	12(5.0%)		
2.	We have increased our network of distribution through use of VCF	164(67.8%)	40(16.5%)	28(11.6%)	10(4.1%)	
3	Use of venture capital financing has helped us achieve greater sales volume	181(74.8%)	45(18.6%)	16(6.6%)		

4.	Presence of venture capitalists has improved our technology base	160(66.1%)	62(25.6%)	20(8.3%)		

Source: Field survey, 2023

The Table 1 shows that 128(52.9%) of respondents strongly agreed to be aware of existence of venture capital financing, 102(42.1%) agrees while 12(5.0%) were undecided. 181(74.8%) of respondents strongly agreed that use of venture capital financing has helped them achieve greater sales volume, 45(18.6%) agreed while 16(6.6%) were undecided.

The findings from here clearly shows that majority are aware of venture capital financing, and have benefited from the use of it which has helped them in improving their business.

4.3 Respondents view on profitability

The data to substantiate this proposition is presented in Table 2.

Table 2: Summary of Respondents View on Annual Profits

S/No	Item Statement	SA	A	U	D	SD
1.	Use of venture capital financing has increased our profitability base.	132(54.5%)	70(29.0%)	40(16.5%)		
2.	Increase in profitability has been significant in our business performance.	181(74.8%)	55(22.7%)	6(2.5%)		
3.	Venture capitalist has provided value creation and improved returns on investment.	105(43.3%)	91(37.6%)	48(19.1%)		
4.	Our performance in terms of annual profits has improved upon use of venture capital financing.	82(33.9%)	102(42.1%)	20(8.3%)	38(15.7%)	

Source: Field survey, 2023

The Table 2 shows that 132(54.5%) of surveyed respondents strongly agree that the use of venture capital financing has increased their profitability base, 70(29%) agrees while 40(16.5%) where undecided. 181(94.8%) strongly agrees that their increase in profitability has been significant in their business growth and performance, 55(22.7%) agrees, while 6(2.5%) where undecided.

Findings from here depicts that use of venture capital financing has increased their profitability base, and thereby significantly increasing their business growth/performance, thus creating value creation and performance.

4.4 Test of Hypothesis

The hypotheses formulated at the beginning of this study were tested using Statistical Package for Social Science (SPSS) version 21.0 for windows output and is shown bellow;

H_{01}: There is no relationship between venture capital financing and annual sales of SMEs in Benue State

Table 3(a): Model Summary for Annual Sales

Model	R	R Square	Adjusted R Square	Std Error of Estimate
1	0.824	0.679	0.652	3.001

Source: SPSS Printout, 2023

Table 3(b): Coefficients for Annual Sales

	Unstandardised Coefficient		Standardized Coefficient		
Model	B	Std Error	Beta	T	Sig.
1(Constant)	4.457	2.154		2.845	0.000
AS	.484	.067	.294	.294	0.000

Source: SPSS Printout, 2023

Adjusted R^2 is called the coefficient of determination and tells us how close the data are to the fitted regression line. Adjusted R^2 is 0.652, that is 65.2% of the variation in performance of SMEs are explained by annual sales. The Table 3(b) further reveals that the relationship between AS and SMEsP is significant ($\beta = .294$, $t = .294$, $P<0.05$). Thus, we reject hypothesis one and conclude that there is a positive significant relationship between venture capital financing and annual sales of SMEs.

H_{02}: There is no significant relationship between venture capital financing and profitability of SMEs in Benue State

Table 4(a): Model Summary for Profitability

Model	R	R Square	Adjusted R Square	Std Error of Estimate
1	0.884	0.782	0.762	2.864

Source: SPSS Printout, 2023

Table 4(b): Coefficients for Profitability

	Unstandardised Coefficient		Standardized Coefficient		
Model	B	Std Error	Beta	T	Sig.
1(Constant)	3.988	2.041		2.724	0.000
PR	0.418	.062	.488	1.041	0.001

Source: SPSS Printout, 2023

Adjusted R^2 is 0.762, that is 76.2% of the variation in performance of SMEs are explained by profitability. The Table 14b further reveals that the relationship between PR and SMEP is significant ($b=.488$, $t=1.041$, $p=<0.05$). Thus, we reject hypothesis two and conclude that there is a relationship between venture capital financing and profitability of SMEs.

4.5 Discussion and Implications

Evidence abound from this study that the relationship between venture capital financing and performance of small and medium enterprise is significantly positive. That annual sales (AS), profitability (PR), as composition of venture capital financing attributes have impact on performance of small and medium enterprise.

From this study, it shows that increased venture capital financing improves annual sales of small and medium enterprise performance, both for the interviews and the test of hypothesis. The study aggress with that of Memba et al. (2012) which found a positive and significant relationship between annual sales and venture capital financing, in that they discovered that the annual sales of companies that had used venture capital financing over a period of 5years outperformed those that did not use venture capital financing (because they experienced dwindling sales volume). This study also is in line with that of Chermmamur et al. (2008). As such improved managerial and technical expertise improves.
From the study, profitability of firms that have used/are using venture capital financing enjoys robust profits as a result of continuous business expansion, restrategizing, technical and managerial expertise as well as efficiency, are watchword to sustain the profit base of these firms in continually realizing their profit base. This study agrees with Memba et al. (2012), Bertoni et al. (2011) & Bertoni et al. (2010) who all found positive and significant relationship between profitability in venture capital financing and firms performance. This also agrees with Puri & Zarutseie (2008). This could have been related to cost saving and increased efficiency in the use of resources and cross monitoring by venture capitalists. With this growth in profit experienced by these firms that use venture capital financing indicates that venture capital has an influence on performance of small and medium enterprise.
The study also reveals that value of assets of these companies in use of venture capital

5.0 CONCLUSION AND RECOMMENDATION

5.1 Conclusion

Venture capital financing is a proven and influential factor in the survival and sustenance of small and medium enterprise performance across the globe, even as this research has found out. The positive and significant relationship between performance in small and medium enterprise (SMEs) and venture capital financing, is to say that increased venture capital financing means increased benefits such as increase in sales volume, increased in profitability ultimately increasing GDP.
The small and medium enterprise development framework hinges on financial supplies and outlays, and the SMEs have been constrained by lack of skilled human, physical, technological resources as well as capital resources. But with the availability of adequate funding, improving the human capital resources in terms of skills and competencies and improving research and development goes a long way in improving sales volumes and profitability and reducing unemployment. The social impact from venture capital financing perspective include employment opportunities created, which has improved lives and alleviated poverty among employees. The increased profits implies revenue collection for government as tax. The funds released to SMEs and acquired by them improve or adds value to the SME, that is, it spurs entrepreneuring spirit in them thereby improving economic growth and development.
Venture capital financing has helped in the provision of funds that has helped in the internal operations of business especially in policy formulation and investment strategy. Nurturing SMEs at crucial junctures in the developmental stages through growth thereby laying the foundation for an emerging generation of locally owned enterprise capable of self sustenance through development.

5.2 Recommendations

In relation to the findings of this study and in light of the above conclusions, the following recommendations are put forward to enhance venture capital funding impact on performance of SMEs.

1. Small and medium scale enterprises need to recognize the numerous benefits and potential advantages of seeking external equity finance for corporate sources. These corporate investors can therefore become very important asset for the SMEs both financially and strategically as they provide tangible and intangible value added resources which can play a valuable role in SMEs performance.
2. The government should serve as both facilitation and educators in encouraging the venture capital process and provide tax incentives to companies prepared to make venture capital investments. This would be an important method for initially stimulating interest in an activity that many corporate executives are possibly not currently considering.

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