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VENTURE CAPITAL and INITIAL PUBLIC OFFERINGS: THE PROSPECTS and IMPEDIMENTS IN AFRICAN MARKETS

by

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Thesis submitted in fulfilment of the requirements for the degree of

Master of Management in Finance & Investment

in the

FACULTY OF COMMERCE, LAW AND MANAGEMENT

WITS BUSINESS SCHOOL

at the

UNIVERSITY OF THE WITWATERSRAND

SUPERVISOR: Professor Kalu Ojah

DECLARATION

I, ---------- declare that the research work reported in this dissertation is my own, except where otherwise indicated and acknowledged. It is submitted for the degree of Master of Management in Finance & Investment at the University of the Witwatersrand, Johannesburg. This thesis has not, either in whole or in part, been submitted for a degree or diploma to any other universities.

Signature of candidate…… Date……

ABSTRACT

The aim of this study is to present venture creation as an alternative form of alleviating poverty and contributing positively to the economic growth of every African government. This study draws to the attention of policy-makers, the importance of venture creation in emerging economies. The author goes on further to highlights the challenges with the current models used for financing/funding new ventures, in an emerging African economy.

The objective of this paper is to also highlight what needs to be done by policy-makers, to create a thriving economic environment for emerging entrepreneurs. This study seeks to highlight some of the prospects, as well as some of the impediments, experienced by the venture capital industry and start-up enterprises.

The environment in which the creation of new ventures operates under in emerging African markets is reviewed, and the exit of those enterprises when they mature and graduate from a small, private company, to a publicly held company - through an Initial Public Offering (IPO) process, is examined. The benefits of exiting these ventures through an IPO, versus the more aptly applied private placement exit method, are also discussed.

The impact that the behaviour and psychology of investing have on the investment trends in African economies is also discussed.

The author used the qualitative research methodology to achieve the results presented in this paper. The outcomes of the study are outlined in chapter four of this paper. The respondents to the survey indicated the importance of the venture capital sector and the critical role that policy makers should be playing. There were no clear responses around the human behaviour in determining the suitable exit platform. What came out clearly in this study; was that each region in the African economy will use a different exit platform driven mainly by the economic environment.

The author goes on further to conclude on the outcomes of the study and suggest further research on the topic on venture capital and initial public offerings. The participants who responded to the survey agreed with the literature reviewed, in particular around the adequate form of financing for starting up new enterprises.

Key words: Angel Finance, Convertible Securities, Credit Default Risk, Economies, Initial Public Offerings, Venture Capital, Small Medium and Micro-Enterprises, Private Placements, Probability of Default, Entrepreneurship, Qualitative, Sampling, Psychology of Investing.

DEDICATION

To my lovely daughter Keamogetswe "Kea" Nage - you are the shining light in mine and your mother's lives, a constant reminder of what a true miracle is.

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CHAPTER 1

INTRODUCTION

1.1.Problem statement

African economies face challenges of unemployment and poverty, and starting new ventures is one of many ways of trying to alleviate some of these problems. However, there are challenges relating to the creation and sustainability of those ventures - namely access to capital (including effective venture capital finance). The current economic environment in African economies is also not conducive for growth in this sector, with business regulations hampering the establishment of new businesses. These regulations often see the stifling of innovative ideas that would have translated into a real product ready for consumption by consumers, and ultimately the creation of a sustainable enterprise (Ojah, 2009).

Empirical research on the impediments facing venture capital finance-backed initiatives, and also their performance before and after their exit through an initial public offering, has largely been conducted in developed markets (Timmons and Bygrave, 1986). Extensive research has not been conducted in African economies.

Venture capital/angel finance platforms in African economies operate on different levels of economic development, under differing circumstances, and with varying levels of inadequate financial infrastructure. This ultimately impacts on the sector's performance and its prospects for making a meaningful, sustainable and measurable contribution to the gross domestic product (GDP) of African economies.

Other challenges facing Africa's economies include the lack of effective business regulations that lower the entry rates (this is regulations that allow for businesses to be registered faster), for entrepreneurs or start-up enterprises. Lack of access to financing with flexible repayment terms to accommodate start-up businesses, remains a major impediment for entrepreneurs. When the funds are finally made available, government agencies use commercial banks to distribute these funds. This method is ill-advised, because the financial institutions apply credit-worthiness checks that are not appropriate for young start-up enterprises. The other challenge facing Africa's economies is a

lack of a developed Angel Finance Network[1]. Other impediments facing entrepreneurs include financial markets that are both illiquid and hampered by corruption, poor legislation, and inadequate infrastructure (with the exception of the Johannesburg Stock Exchange and the Cairo Stock Exchange to a large extent). This hampers the exit platform for the IPO (Initial Public Offering)**.**

African markets are dominated by active private equity investments of funds that are focused on management buy-out platforms (Ojah, 2009). These markets need appropriate private equity funds, such as venture capital/angel finance. This is equity investment funding provided to privately-held entrepreneurial firms or start-ups that possess attractive products or concepts that are yet to attain consumer acceptance (Ojah, 2009). Governments in Africa, need to facilitate the availability of financing for those entrepreneurs that possess innovative and sustainable ideas (Bigsten and Collier, 2003; Egeln and Licht, 1997).

Less desirable financing is that which is focused on a management buy-out strategy. This is a private equity scheme designed to foster efficiency of production in an existing corporation, by administering that business entity as a private firm (Cumming and Siegel, 2007). That form of private equity is better suited to developed countries such as the USA, Japan, Germany and the United Kingdom. These countries are characterised by well-functioning capital markets with adequate institutional infrastructure, both of which are indispensable for corporate control. These two private equity platforms (i.e. the management or leveraged buy-outs and venture capital/private equity), are both useful, but each serves a distinctly different economic purpose (Ojah, 2009).

The study's results (i.e. venture capital and initial public offerings: the prospects and impediments in African markets) should provide guidance and assistance to both policy-makers and private financers on how to address the challenges that the venture capital finance sector faces, and to fully appreciate the important role that this sector plays in economies.

1.2. Purpose of the study

The purpose of the study is to investigate the prospects and impediments facing venture capital finance and IPO in African economies, particularly South Africa.

[1]Website: http://www.herebedragon.co.za for full details regarding the Angel Finance Network.

The study will evaluate whether a thriving and sustainable sector of new venture capital creation requires the following needs to be in place:

1: Support from governments through business legislation that speeds up the administrative process required to start business.

2: Access to finance. Even when there is access to finance, certain challenges remain. For example, the method government agencies use to disburse funds is not appropriate, because it involves commercial banks. These financial institutions apply credit worthiness checks that are not appropriate for start-up companies. The repayment terms are also not tailor-made for start-up enterprises.

From the foregoing statements, it is clear that private sector financiers need to create new financing models, or tailor-make venture capital financing private equity funds, which are aimed at making finance easily accessible to prospective entrepreneurs. This can take place whilst also addressing the related problems of capital rationing, and the negative impact that high interest rates have on young entrepreneurs seeking capital for starting a new venture (Stiglitz and Weiss, 1981).

Sahlman (1990) found that venture capital-supported enterprises perform better, on average, than non-venture capital supported enterprises, as they not only provide equity capital, but also provide mentorship by experienced professionals, thus reflecting the efficiency of the resources deployed in creating the resultant public enterprise**.**

Furthermore, this study will also investigate the prospects and impediments facing the exit of these investments, (i.e. mature enterprises) through an IPO, versus the private placement exit platforms. The advantage of publicly-listed firms is that the existence and survival of a firm is decoupled from the longevity of the firm's owner(s). It expands the firm's access to external finance enormously, and subjects the firm to the kind of scrutiny that fosters best practice in corporate governance (Ojah, 2009). There are also disadvantages linked to this exit platform though, for example other investors may be looking for short-term gains. This has the potential to affect these enterprises' innovation and creativity negatively, thus leading to the potential demise of the entity.

1.3. Research questions and sub-questions

The study seeks to answer the following questions:

- What needs to be done by both the government (policy makers) and private sector financiers (i.e. banks and third party funds) in African markets, to create a stimulating platform for venture capital finance backed initiatives, and to address the challenges the financing sector faces?

- Are the current funding models appropriate for addressing the challenges faced by start-up enterprises?

- Why is the venture capital backed-IPO not the most viable investment exit strategy for investors in Africa's markets (as opposed to the more popular private sale exit method)?

In answering these questions, a number of sub-questions are likely to arise:

- Does the behaviour and the psychology of investing have anything to do with the investors in African economies and does it ultimately lead to fewer venture-backed IPO's?
- Does the fact that most security exchanges in African countries are experiencing challenges, have anything to do with the behaviour of existing investors and those wishing to invest in these economies?

1.4. Aims and significance of the study

The study aims to demonstrate that venture capital finance-backed initiatives and the way they are structured play a role in addressing the issue of job creation, addressing alleviation of poverty, and reducing reliance on government social grants. The study also aims to demonstrate that these initiatives can also contribute to economic growth in African economies (Wennekers and Thurik, 1999).

Research conducted by Manigart et al. (1999), has shown that investment by private equity funds into companies holds great benefits other than the initial cash injection - to develop the businesses. For example, investors, or their representatives, can provide valuable knowledge through their occupation of a board seat in the company. A study by the Development Bank of Southern African

from 2005/6 to 2008/9, illustrated the performance of private venture backed-enterprises and how financing of these small enterprises positively contributed to the South African economic market[2]. It led to the employment of 5% of South African formal sector employees, which equates to around 427 000 jobs. In the survey respondents reported that private equity funding had made positive contributions to their businesses, and 64% felt the investment(s) allowed their businesses to grow faster.

It is also the intention of this study to try and provide guidance to policy makers and private sector financial institutions. This is because for venture capital finance-backed initiatives to be successful and to continue to contribute to the economic growth of the country, the following points need to be addressed:

- Policy-makers in African economies need to create an economic environment that encourages entrepreneurship by lowering the costs of starting up a business, and to introduce flexible regulations that allow businesses to be established faster (Van Stel and Storey, 2007).

- African governments need to consider the benefit of having financial support agencies in African economies, designed with mechanisms in place that provide easy access to finance for young or start-up entrepreneurs (Bigsten and Collier, 2003).

- The creation of a new venture fund supported by a Public Private Partnership between government and private sector financiers, will add value to this sector.

- The benefits of having a developed Angel Finance Network in African economies to assist with financing new ventures should be considered.

- African countries need to consider what benefit a new venture creation bank, supported by government, will have on their economies. These banks would be specifically focused on providing tailor-made financing for young start-up businesses with no performance track record.

African governments need to consider building efficient legislative environments and institutional infrastructure, which is a prerequisite for creating and running well-functioning capital markets. These capital markets must then be developed enough to spawn active and liquid secondary capital markets, which are capable of sustaining 'market for corporate control' activities (Ojah, 2009).

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[2] Development Bank of Southern Africa, South African Venture Capital Association and I.E. Consulting (2009):*"**The Economic Impact of Venture Capital and Private Equity in South Africa**"* survey.

The study aims to evaluate whether the most profitable method of exiting the maturing enterprise is through the common platform of private sale through investors, or through an IPO listing on the securities exchange platform (Barry and Muscarella, 1990). Evidence shows that venture-backed IPOs perform far better in the long run, as the investors are also advisors or are part of management, and have been with the company for a long time (Jain and Kini, 1995).

Chapter 2 contains a review of the relevant literature published on venture capital, the impediments and prospects facing SMMEs, and the laws and regulations affecting these enterprises and initial public offerings.

Chapter 3 reviews the research methodology - the research design and instruments necessary for achieving the study's objective. This chapter also outlines the limitations of the research methodology, with the author suggesting alternatives to address these limitations.

Chapter 4 discusses and analyses the outcomes of the results from the survey. We go on further to compare those outcomes with the literature reviewed in chapter 3 and draw and inference on the results. The author discusses the demographics of the respondents and also outlines their level of expertise.

Chapter 5 deals with conclusions to the study and suggestions for further research on the topic. The author outlines the gaps identified during the survey and compares those to the literature reviewed in chapter 3.

CHAPTER 2

LITERATURE REVIEW

2.1. Venture capital finance backed initiatives

The literature review seeks to answer the research questions raised in chapter one. The literature review also reviews what other emerging and developed economies have done relating to the venture capital industry.

The literature review is divided into three sections, the first being a review of challenges relating to new enterprises being created. The challenges are in the form of financing, obstructive legislation currently in place, and how to overcome this legislation. The literature review then discusses the exit

of these ventures after they are mature and have graduated from being private to public companies, through a process of listing on a securities exchange. In the discussion the benefits of this method are compared with those of the private placement method. The literature review concludes with a summary of the important lessons learned from previous studies.

The impediments facing venture capital backed initiatives are as follows:

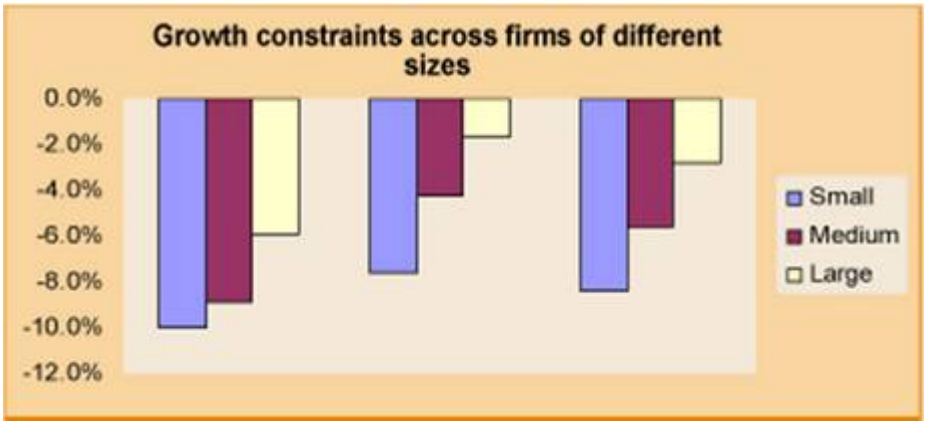
2.2. Challenges facing new ventures being created

There has been no formal empirical research on the impediments facing venture capital finance backed initiatives (access to financing, inflexible repayment terms and the absence of economic environments that encourage entrepreneurship) in African economies. This is despite the performance of ventures having significant benefits for an economy (i.e. contributing to economic development and lowering poverty and unemployment). Research on these problems and performance issues, before and after the exit of new ventures through initial public offering, has largely been conducted in developed markets (Timmons and Bygrave, 1986).

A recent study on African economies (Ojah, 2009) opines that for African economies to thrive and to address poverty and unemployment, the use of the right private equity financing is essential. Appropriate financing is meant to stimulate entrepreneurship, by making capital easily accessible to young entrepreneurs, which would normally not be the case. Continuing with the challenge of obtaining financing, a study by Bigsten and Collier (2003) clearly demonstrated that in African economies, credit constraints are a major impediment, even though there is a great demand for credit. From their analysis of panel data of firms with a demand for credit from six African countries, only a quarter obtained a formal sector loan. The study concludes that while banks allocate credit on the basis of expected profits, micro- or medium enterprises are far less likely to secure loans than larger enterprises. The findings also highlighted the negative impact outstanding debt has, when enterprises attempt to obtain further credit. The authors also observed that the role of outstanding debt is likely to be a reflection of inefficiency in the credit markets (Bigsten and Collier, 2003).

Research by Beck and Deminrquc-Kunt (2006) of the World Bank (‘SMMEs need better access to finance to overcome impediments to growth’), also highlighted the desire of SMMEs to access finance, as a major impediment to SMME growth. SMMEs face greater growth impediments than larger firms - limited access to finance being the greatest impediment. Small firms are also more likely to be constrained by these obstacles than larger firms.

Figure 1: Growth constraints across firms of different sizes'



The graph (above, '*growth constraints across firms of different sizes'*) shows the effect that impediments like financing, legislation and corruption have on a firm's growth. This is based on the regression of a firm's growth as a result of the respective growth impediments, interacted with dummy variables for small, medium and large firms, and controlling for other firm and country characteristics.[3]

Further research by Beck and Deminrquc-Kunt (2006) ('Strengthen access to finance for small & medium-size enterprises while improving business environment for all firms'), identified innovative lending technologies as one of the initiatives that can help in the short term to address impediments in accessing finance. The researchers indicated that in the interim, innovative lending technologies hold promise. These can provide market-friendly ways of relaxing the constraints on SMMEs. Some technologies, like factoring, are particularly promising, since they rely on institutions to a lesser extent. However, other technologies like credit-scoring and leasing can also be useful for relaxing the financing constraints on SMMEs, and their use would improve with development of institutions over time.

The current form of finance available through formal financial intermediaries or banking financial services, doesn't adequately address this challenge (i.e. adequate access to financing). This is illustrated in the finance models that intermediaries use. An example is given in the liner probability model below. The credit scoring models applied by the banks have burdensome requirements (i.e.

[3]Source: Beck, Demirgüç-Kunt (2006): World Bank. ***Strengthen Access to Finance for Small & Medium-size Enterprises while improving business environment for all firms. A finance research Story***. World Bank, Washington D.C. (page 2).

credit history or earnings track records) to determine whether the entity will be able to repay the loan or service the debt on a monthly basis. These credit scoring models are based on quantitative models that use observed borrower characteristics to either calculate a score representing the applicant's probability of default, or to sort borrowers into different default risk classes. One of the popular credit check models used by the banks, is described below:

Linear probability model:[4]

$PD = \sum \beta_j X_{i,j} + \text{error}$

Where:

PD = Probability of default

β_j = *is the estimated importance of the jth variable (e.g. leverage) in explaining past repayment experience.*

$X_{i,j}$=*It reflects quantitative information about the ith borrower, such as leverage or earnings.*

If we take the estimated β_js *and multiply them by the observed* $X_{i,j}$ *for a prospective borrower, we can derive the expected PD for the prospective borrower. The value obtained can be interpreted as the probability of default for the borrower:* $E(PD_i) = (1 - p_i)$ = *expected probability of default, where* p_i *is the probability of repayment on the loan.*

The linear probability model is used by financial intermediaries to predict defaults and use past financial data or the entity's track record - the very information that start-up businesses don't have. The inappropriateness of this model stems from the fact that aspiring entrepreneurs or start-up businesses are excluded from the possibility of accessing financing, due to lack of historical financial information or credit histories.

During a World Bank conference in 2008 ('*Making Finance Work for Africa*'), panellists indicated that some banks use relationship-lending in place of the credit scoring model, when determining whether or not to finance the creation of a new venture.

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[4]*Source:* Saunders and Cornett (2006): ***Financial Management Institutions: A risk Management Approach.*** Sixth Edition. page. 3-17

2.3. Problems and opportunities facing African economies

Apart from access to the appropriate form of financing, African economies face other non-monetary challenges. One of these challenges is lack of clear and understandable information, and this is considered to be the reason for the observed complexity of financial contracts. Flowing from this, other challenges facing aspiring entrepreneurs include business legislation that doesn't facilitate the rapid creation of new ventures. Van Stel et al. (2007) illustrate that Small, Medium and Micro-Enterprises and policy makers seeking to increase the number of new firms created, and subsequent wealth creation, are faced with choices. The primary choice is whether to follow a low-regulation route, or to follow a 'high support' route. The low regulation route focuses on policy in two areas - enabling the establishment of a business as quickly and cheaply as possible, and minimising the compliance burden (i.e. providing technical skills and reduction of tax requirements) on that business while it is trading.

Djankov (2002) showed that countries where legislation governing business was most burdensome are more likely to be undemocratic, characterised by official corruption, and with larger unofficial economies and lower levels of wealth.

A survey done by the African Monitor on African economic freedom, reveals a similar trend. The revealed the following about African countries:[5]

Lesotho:

The overall entrepreneurial environment is hurt by weak property rights, limited access to finance, and bureaucratic red tape. Lesotho has a small and under-developed financial system that is closely tied to South Africa through the Common Monetary Area.

Zimbabwe:

Bureaucracy is non-transparent and corrupt, and the risk of expropriation, which is used to promote 'indigenisation', is high. The weak rule of law, restrictive labour rules ,and inadequate foreign exchange, significantly deter investment.

It is clear that for new ventures to thrive and be sustainable, African economies need to urgently address these challenges. Government intervention in the creation of small businesses is vital, as

[5] Source: 2010 Index *of* Economic Freedom and African Sun News: ***Doing Business in Africa.***

illustrated by the United States government's involvement in encouraging the growth of venture capital through the promulgation of the Small Business Investment Act of 1958, which authorised the formation of Small Business Investment Corporations (SBICs). The legislation was not aimed at venture capital *per se*. It was meant to create funding for small firms of all types. It permitted individuals to form SBICs with private funding, paid in capital. Money is borrowed up to a certain amount that increases over time, with government guarantees. There were also tax benefits such as income and capital gains pass-through (Dossani and Kenny, 2002).

The South African government made a commitment to create an enabling environment for the creation of new ventures, as indicated in the publication issued by the Department of Trade and Industry, that states:

> *"With millions of South Africans unemployed and underemployed, the government has no option but to give its full attention to the fundamental task of job creation, and to generating sustainable and equitable growth. Small, Medium and Micro-Enterprises (SMMEs) represent an important vehicle to address the challenges of job creation, economic growth and equity in our country. Throughout the world, one finds that SMMEs are playing a critical role in absorbing labour, penetrating new markets and generally expanding economies in creative and innovative ways. We are of the view that with the appropriate, enabling environment, SMMEs in this country can follow these examples and make an indelible mark on this economy. The stimulation of SMMEs must be seen as part of an integrated strategy to take this economy onto a higher road, one in which our economy is diversified, productivity is enhanced, investment is stimulated and entrepreneurship flourishes*".[6]

African governments should learn from governments with emerging economies like that of India, which is one of the fastest developing/emerging markets globally. The Indian government has implemented an important policy that directs funding to university research. This investment has funded generations of graduate students in science and engineering. The outcome of this investment has yielded trained personnel and innovations, some of which have resulted in the formation of businesses that have been funded by venture capitalists (Dossani and Kenny, 2002). In South Africa, the University of Witwatersrand's business school has a centre dedicated to the creation of new

[6]Department of Trade and Industry study: ***Integrated Strategy on the Promotion of Entrepreneurship and Small Enterprises.***

ventures and fostering entrepreneurship. This is the Centre for Entrepreneurship and New Venture Creation, which offers a Masters degree in Entrepreneurship and New Venture creation.[7] There is an opportunity for the South African government to partner with the university and provide funding to aspiring entrepreneur students, so that they can learn the technical skills required for new ventures to thrive.

Another effective form of ensuring the sustainability of new ventures created, is through monitoring. Monitoring venture capital-backed initiatives in emerging economies is performed through a creation of networks, as is the case in East Asia (Ahlstrom and Bruton, 2006). The authors argue that while important to venture capitalists everywhere, network connections among entrepreneurs, venture capitalists and enterprises, may play a greater role in helping venture capitalists navigate the challenging environment in emerging economies.

These networks have been found to be particularly important for financing in East Asian economies, and are also useful in the absence of more formal monitoring and control mechanisms that exist in more developed economies. The venture capital industry is also less regulated and less established than mainline financial sectors, in emerging economies.

2.4. Suggested measures for bridging the financing gap for new ventures and for their problems

The World Resources Institute provides some recommendations on how to bridge the financing gap for new ventures in emerging markets. They note that this process encourages and promotes financial innovation.

The Institute argues that both long-term approaches and innovation are needed to overcome systemic barriers. Such innovation could include, for example - financial structuring that increases the security of investments in intermediaries and breaks down large flows of capital into amounts that can be absorbed by intermediaries, or the creation of a new 'social stock exchange' to facilitate exits. A group of financial innovators in London have created an ethical stock exchange to respond to an increasing appetite for direct ethical investment. The exchange's intention is to increase liquidity in the market for ethical investments, by providing new channels for social enterprises to raise capital through share and bond issues, and for equity investors in social enterprises to disinvest

[7]Wits Business School website: www.wbs.ac.za/masters of management in entrepreneurship and new venture creation.

when they need to.[8]

2.4.1. Recommendations for venture capital finance-backed initiatives to succeed

Policy makers have a significant role to play in creating a stimulating environment for the creation of new ventures. Policy makers in developed markets have played a significant role in aiding the venture capital industry through promulgation of laws and legislation, directly aimed at assisting SMMEs.

It is suggested that policy makers in Africa aid venture creation by:

- Amendment of the current SMME legislation to allow flexibility in terms of compliance, (e.g. the payment of tax only after the business has generated a certain amount of revenue).
- Partnership with the private sector and the universities, that have dedicated centres for entrepreneurship and new venture creation.
- African economies dedicating resources to addressing the challenges inherent in their securities exchanges. Venture initiatives need an active stock market in order to thrive and be sustainable.

In order to begin to address the problem of access to adequate forms of financing, African economies reviewed in this study will be well advised to look at other forms of financing, especially micro credit financing, which is being used successfully in other emerging markets such as India. Micro credit financing is supported through Public Private Partnership initiatives between commercial banks and micro financing institutions.

India has come up with creative funding solutions, in order to address the challenges faced by small enterprises. The micro lending institutions that have successfully addressed the financing challenges in India are as follows (see O'Rourke, 2006):

- An Accumulating Savings and Credit Association. All members save the same fixed amount regularly, and can borrow from the group at an interest charge. The interest return is then distributed among the group.

[8] World Resources Institute. On the Frontiers of Finance: ***Scaling up Investments in Sustainable Small, Medium and Micro Enterprises in Developing Countries*.**

- Postal Savings Banks. They operate much like regular banks, but they tend to serve mostly rural communities through local postal offices, and offer more flexible terms than commercial banks.

African economies have a significant role to play in addressing the challenges faced by SMMEs and can learn from their counterparts in adopting and implementing their funding solutions, that have worked. The Public Private Partnership is one of the most effective ways to address some of the funding challenges. In South Africa, institutions like Khula Enterprises partner with other commercial banks to offer financing to start-up enterprises. However, a specific tailor-made financing model should be created and implemented, for this partnership to be successful in addressing problems associated with accessing finance.

An alternative policy involves government providing support to new and small firms, funded by taxpayers. It can be in the form of information, advice, training or finance, to new or existing small firms. An example of how other African governments have intervened to address this challenge is presented below; the Zambian government created a US$ 4 million venture fund to aid small business. Extract from *Times of Zambia*:

> *"The Government is next month expected to issue a Statutory Instrument that will give preference of procurement of Government contracts to Zambian-owned companies, Commerce, Trade and Industry Minister Felix Mutati said. Mr Mutati said the Citizen Economic Empowerment Commission (CEEC) was working with the Zambia Public Procurement Authority (ZPPA) to implement preferential procurement that would support citizen-owned firms. Speaking when he addressed a workshop on Micro, Small and Medium Entrepreneurs (MSMEs) in Lusaka yesterday at Mulungushi International Conference Centre, the minister said the statutory instrument, once effected, would enable the MSMEs to generate employment and help alleviate poverty. 'The Government will issue a statutory instrument to enable the two Government institutions to give preferential procurement on Government contracts and supplies to Zambian companies,' Mr Mutati said. And Government will launch US$4 million Venture Capital Funds in the first quarter of 2011 that will finance start-up capital and expand or restructure an organisation through the use of equity. Mr Mutati said Zambia's venture capital industry was still at an infant stage, and once launched, would assist the SMMEs in terms of accessing finance.*
>
> *The fund would be managed by the Zambia Development Agency (ZDA) and Development Bank of Zambia (DBZ). 'The size of investments will be increased from the initial $4 million*

once the various sectors start accessing the facility, and the ZDA privatisation trust fund will put in some thing as well as the DBZ,' he said. Sectors such as horticulture, manufacturing, pharmaceuticals, hospitality and tourism, property and real estate, financial services, agro-processing, information technology and transportation will benefit from such a scheme. Mr Mutati said SMME policy would be launched on January 27, 2011 and it would further support the growth of the sector which currently accounts for 85 per cent of the total employment in Zambia".[9]

Even after the above initiatives have been implemented, other researchers argue that the one challenge not addressed is the risk of the new enterprises being sustainable - as investing in a fledgling start-up business is extremely risky. They note the high failure rate among new firms as one of the risks. The investors and other scholars rightly argue that making financing available to new businesses that have not proven themselves is also very risky, because they are not aware of how the funds will be managed and whether the venture being supported is sustainable. They also state that venture capital is seen as risky because investors don't know who they're taking a gamble on, and they have to wait at least five years to get returns. Despite the risks highlighted, the yields, however, are generally better than those realised on the general market, which has been patchy since the start of the global financial crisis. Investors can expect a minimum annual return of 20% from a venture capital fund. By comparison, the South African R157 Bond yielded 14, 6% during the period of 1990 to 1995 in a favourable bond market.[10] Sahlman (1999) outlines the structure and governance of venture capital organisations. He declares that the venture capital industry has evolved operating procedures and contracting processes that are well adapted to environments characterised by uncertainty and information asymmetries between principal and agents.

In designing innovative initiatives for alternative forms of financing, the developed world has resorted to extensive use of convertible securities. The most remarkable feature of this financial structure in the North-American venture capital industry, is the unusually broad reliance on convertible securities. Various empirical studies have shown that the percentage of venture capital

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[9]Source: *Times of Zambia,* Zambia. *21 Dec 2010: Forward with the National.*

[10]Larry Claasen. *VC Industry: Fortune favours the bold. Wealthy locals are keen to invest in something new.* Published 11 November 2010 . *Financial Mail*.

deals using some sort of convertible securities, ranges from 20.9 to 94.5 per cent, depending on determinants of financial structure in the venture capital industry, especially with regard to the use of convertible securities (Bascha and Walz, 2001). These instruments require a well-functioning securities exchange. However, securities exchanges in the African economies studied suffer from liquidity problems, adverse selection, and the negative impact of information asymmetry. Countries like Zimbabwe also suffer from weak legislative systems and non-safeguarding of investors' assets.

In Africa there is usually a significant pool of high net worth individuals in local business hub cities (such as professionals and business owners). These groups are, however, not yet considered credible sources of start-up funding. Individual angel investors and small private equity groups are present in many African countries, but this hybrid of structured angel groups deploying funds, appears to be part of the 'missing middle'.

The Angel Network platform - finance that is designed to match angel investments by members of angel group networks, and that can aid the financing of the SMME sector – is now considered. It would seem that the establishment of such groups in business hub cities like Accra, Nairobi and Johannesburg, could help close the SMME funding gap. Furthermore, a model for matching angel investments by members of such angel groups (by local or foreign non-profit or for-profit seed funds), could result in a powerful multiplier effect. There are numerous ways to make such angel groups more effective, from deal-flow sourcing through to due diligence and investment structures. Exploring these options, using best practices from the developed world, may help create a model for such groups to form and operate. If African angel investors organized such groups, they would decrease their own investment risk due to the pooling of resources and insights from other group members, as well as by having access to more deal flow. African entrepreneurs would also benefit from having additional funding sources and business guidance, which start-ups battle to access.

Angel groups have also been successful in the developed world in working with universities and colleges in aiding entrepreneurial students with promising ventures, such as the Angel Investor Forum collaborating with the Yale Entrepreneurial Institute, to fund start-ups. This model could be of interest to Africa's leading educational institutions that seek to encourage entrepreneurship, making it an accessible path for a country's brightest students.

Creating angel groups in key business locations across Africa, could be an effective way to help

fund the 'missing middle' and to drive a new wave of African ventures for lasting economic growth on the continent.[11]

In trying to identify the most suitable form of financing for SMMEs in African economies in the next section, the author introduces other forms of financing that have been successfully used in other emerging markets.

2.4.2. Micro Financing Institutions' structure and their significance for venture creation

O'Rourke (2006) argues that creating structured partnerships between commercial lending institutions and Micro Financing Institutions (MFIs), can provide the best long-term sustainable results and will allow MFI to flourish as independent and vital parts of developing world systems - without threatening the security and stability of the financial systems supporting these innovations.

Micro financing is a vital tool for development because it enables the poor to build assets, increase income and attain self-sufficiency. Additionally, micro credit encourages entrepreneurship and innovation in the rural and consumer goods sectors, which helps to grow and strengthen developing countries' economies. Micro credit also moves small businesses from the informal, to the formal sectors, which then increases stability and security and broadens the tax base. MFIs have a unique role in the financial systems. They provide capital for a borrower, who would otherwise be priced out of the financial market, due to the high transactions costs associated with very small loans, as well as the high-risk nature of small enterprises. MFI loans are usually small and do not require collateral.

2.4.3. Microfinance: Sustainability and outreach

The goal of achieving substantial outreach and sustainability is to drive certain microfinance principles that also mesh well with the modernist perspective of mainstream finance. The financial systems approach to microfinance envisages microfinance institutions converging to financial self-sustainability. This approach sees the subsidies provided, focus on setup and head-office issues, including product development, and not being directly used to subsidise lending interest rates at the margin. This is even when the subsidy is received in the form of a low-interest long-term loan that

[11] Source: Africa Blog. Changing The Way The World Sees Africa: Angel Groups – a **Solution for the Missing Middle in Africa?**

the MFI invests in treasury bills - using the net revenue to cover operating costs. As scale is achieved, such subsidies tend to assume a relatively smaller part of the microfinance business (in a way that, for example, systematically distorting marginal pricing of interest rates would not). Even though the intention is usually to eliminate the microfinance institutions, such foundation subsidies do tend to persist for a very long time. The high interest rates (spread over wholesale rates) seen in unsubsidised microcredit - although much lower than those typically charged by money lenders - result from the costs associated with intermediation of this sort.

Microfinance can be successful in rural areas, but is used more widely in urban and peri-urban settings, which points to the costs associated with remoteness and low density. By the same token, high interest rates mean that much potentially socially beneficial micro-lending simply does not take place. The same applies *mutatis mutandis* with respect to the pricing of deposits and insurance type products (Helms and Reille, 2004; Porteous, 2006; Honohan and Beck, 2007).

Another popular form of financing that is being used extensively in developed markets, is convertible debt instruments, which are discussed extensively in the next section.

2.4.4. The use of convertible debt instruments

The other popular form of financing new ventures is the use of convertible debt instruments. However, for the successful deployment of these instruments, one of the major requirements is the existence of a well-functioning securities exchange. Although not at an advanced stage in terms of securities exchanges and trading of these financial instruments (i.e. the corporate debt market), African economies can consider using this form of financing to facilitate an adequate supply of funding to SMMEs. This form of financing for start-up businesses has been used successfully in developed countries like Germany and the United States. Convertible debt is simply a loan (a debt obligation) that can be turned into equity (stock ownership), generally upon the occurrence of future financing. Investors prefer convertible debt, as their returns may be exponential. It's an excellent way to secure investment funds, without setting a valuation on a company.

This process has a fair amount of uncertainty and is disruptive for an early-stage, pre-revenue company.[12] This form of finance also addresses issues of information asymmetry and moral hazard.

[12]Asheesh Advani is the founder of Circle Lending and Virgin Money USA, and the author of *Investors in Your Backyard.* Entrepreneur: ***Raising Money Using Convertible Debt.***

The IPO exit method is now discussed and evaluated with regard to whether it is suitable for SMMEs enterprises in the context of African economies.

2.5. The investment exit method through an IPO

This section discusses the importance of exiting a mature enterprise from a venture capital fund. It also seeks to highlight the benefits of having venture capital backing a new venture, and outlines the performance of enterprises backed by venture capitalists versus the non-venture backed enterprises. The role of the IPO market in the venture capital industry and the benefits it provides to the sustainability of enterprises is also discussed.

For a successful and profitable exit of a mature private company to be realised through an IPO, African governments need to build sustainable capital market infrastructure, as this is important for corporate control (Ojah, 2009). The impediment such as illiquid and inefficient markets needs to be addressed before a market for exiting mature private companies can be viable. Jain and Kini (1995) argue that markets react favourably to a venture-backed listing, and the involvement of a venture capitalist reduces the risk of the under-pricing of a company being listed on the securities exchange. The factors below determine how under-priced the stock of a new venture can be in an IPO:

- How long the lead venture capitalist has served on the company's board
- The older the lead venture capitalist is
- The larger the fraction of the issuer's equity owned by venture capitalists.

Barclay and Holderness, (2007) show that the initial stock-price reaction to private placements is positive, but in the long run stock returns are negative (why this is the preferred method will be addressed in this study). A private placement scheme involves selling a block of shares to existing managers or other external investors. Private placements are purchased by active investors who are willing, and able, to monitor management to ensure that corporate resources are used more efficiently, and increase the probability of value-increasing takeovers. However, private placements derive more value from the developed markets as (Barclay and Holderness,2007)illustrated through their analyses of over 100 firms in the US.

2.6. The importance of exiting a mature enterprise by the venture capital fund

The first step in appreciating the link between the stock market and the venture capital market, involves understanding the importance of exit by the venture capital fund from its investments.

Black and Gilson (1999) developed an informal theory indicating why exit from successful investments is critical This is both for the relationship between a venture capital fund and its portfolio companies, and for the relationship between the fund and its capital providers

2.7. Benefits of venture capital fund to the business - portfolio company relationship

Venture capitalists provide more than just money for their portfolio companies: They also provide management assistance, intensive performance monitoring, and reputational capital (i.e. the venture capitalists ability to give the portfolio company credibility with third parties.[13]) These are discussed in detail below:

Management assistance: Venture capital fund partners are experienced in developing start-up companies and possess market knowledge based on other portfolio investments in the same and related industries. They can assist a management-thin, early-stage company in locating and recruiting the management and technical personnel it may need, as its business grows. They can also help the company through the predictable problems that firms face in moving from prototype development to production, marketing, and distribution. Venture capitalists' industry knowledge and prior experience with start-up firms, helps them locate managers for new start-ups.

Intensive monitoring and control: Venture capital funds have both strong incentives to monitor entrepreneurs' performance, deriving from equity ownership and strong control levers, disproportionate to the size of their equity investment. One control lever results from the staged timing of venture capital investment. The initial investment is typically too small to allow the portfolio company to carry out its business plan. The venture capitalist will decide later whether to provide the additional funding that the portfolio company needs. The contract between a venture capital fund and a portfolio company. provides other control levers. The venture capitalist typically receives convertible debt or convertible preferred stock. This stock carries the same voting rights as if it had already been converted into common stock, plus greater board representation (often an absolute majority on the board) than if board representation were proportional to voting power. Board control lets the venture capitalist replace the entrepreneur as chief executive officer if necessary. Even where the venture capitalist lacks board control, the investor rights agreement gives the venture capital provider veto power over significant operating decisions by the portfolio

[13] Source: Here be Dragon (HBD) Venture Capital. www.hbd.co.za: ***Funding Options.***

company. The reputation market necessary to prevent the venture capitalist from misusing this power, is discussed below.

Reputational capital: Much like an investment bank underwriting an initial public offering, the venture capital fund acts as a reputational intermediary. Venture capital financing enhances the portfolio company's credibility with third parties. Talented managers are more likely to work for a venture capital-backed company, because the venture capitalist's participation provides a credible signal about the company's likelihood of success. Suppliers will be more willing to risk committing capacity and extending trade credit to a company, if a venture capitalist both vouches for and monitors, its management and technical progress. Customers will likewise take the company's promise of future product delivery more seriously. Later on, the venture capitalist's reputation helps to attract a high quality underwriter for an IPO of the portfolio company's stock. The venture capital fund's proffer of its reputation to third parties who have dealings with a portfolio company, is credible because the fund is a repeat player and has put its 'money where its mouth is' by investing in the portfolio company.

Economies of scope in venture financing: The management assistance, monitoring and service as a reputational intermediary that a venture capitalist provides, share a significant economy of scope with its provision of capital. This economy of scope arises from a number of sources. The portfolio company must evaluate the quality of the venture capital fund's proffered management assistance and monitoring. Similarly, potential employees, suppliers and customers must evaluate the fund's explicit and implicit representations concerning the portfolio company's future. Combining financial and non-financial contributions enhances the credibility of the information that the venture capitalist provides to third parties, and bonds the venture capitalist's promise to provide non-financial assistance to the portfolio company. Combining financial and non-financial contributions also lets investors in a venture capital fund evaluate the fund's non-financial contributions, by measuring its return on investment.

The vital role played by venture capitalists (VCs) in the creation of public corporations is well established. In addition to providing capital at critical stages of development, VCs add value to the public listing process, through their screening, monitoring and decision-support functions.

2.8. The role of the IPO market

The health of the venture capital industry is dependent on the existence of a strong and vibrant IPO market, as venture capitalists generate the majority of their profits from firms that go public. The

ability of the venture capital industry and its ability to grow is, therefore, dependent on a strong IPO market (Jain and Kini, 2000).

The under-performance of enterprises listed for the first time on the securities exchange (see Ritter, 1991; Loughran and Ritter, 1995) comes primarily from small, non-venture-backed IPOs. While small, low book-to-market IPOs perform no differently from similar small, low book-to-market non-issuing firms, the pattern of relative performance in other portfolios needs to be examined in greater detail. Some of the IPO size and book-to-market portfolios appear to exhibit either under- or over performance (Brav and Gompers, 1997).

The presence of venture capitalists in the issuing firms, serves to lower the total costs of going public and maximises the net proceeds to the offering firm. Venture capital backing reduces the mean and median degree of IPO under-pricing, and significantly reduces the underwriting spread charged by the investment banker handling the issue. Further support for the venture capitalist certification hypothesis, is provided by the finding that venture capital-backed issuers are able to attract more prestigious auditors and underwriters than non-venture capital-backed issuers. In addition, venture capital-backed issuers also elicit greater interest from institutional investors during the IPO, and are able to go public at a younger age than other firms. If venture capitalists are able to convey credible information about the firm, the compensation to investors, underwriters and auditors will be reduced, since their cost of acquiring information about the company (personally certifying the issue) will be lowered (Megginson and Weiss, 1991).

The following section further illustrates (using the Italian securities exchange) the performance of venture-backed entities in a securities exchange, as opposed to non-venture-backed entities.

2.9. Performance of the venture capital-backed listed business, versus the non-venture capital-backed listed business

The Ernst & Young Venture-Backed Index for shares listed on the Italian Stock Exchange, created in November 1999, monitors venture-backed companies with shares listed on the Electronic share market, the Mercato Telematico Azionario (MTA) managed by Borsa Italiana. The basket of companies in the index includes companies that have been listed for more than three months and not more than three years. Companies in the first three months after listing are not included, to avoid under-pricing an IPO, whilst those listed for more than three years are no longer considered to be influenced by their venture-capital investors. Figure 1 (below) summarises the performance of the

EYVBI (i.e. Ernst &Young Venture Backed Index) from March 01, 2009 through February 28, 2010, versus the FTSE - MIB:[14]

Figure 1: The Ernst & Young VBI



Source: Ernst & Young Financial-Business Advisors calculation on information provider's data

Figure 1(Ernst & Young VBI) shows that the EYVBI generally followed the market trend, though performing better than the latter, especially in the last quarter of 1999. The results of EYVBI indicates that over the period, the index increased by 63.8%, compared to the performance of 46.7% registered by the Financial Times and Stock Exchange -Milano Italia Borsa (FTSE MIB).

The key information derived from the literature is now discussed.

2.10. Summary of key points derived from the literature

Much literature pertaining to venture capital finance and IPOs, contains guidelines on how the challenges faced by venture capitalists, policy makers and private financiers can be addressed. It is also clear that for any economy to thrive, create employment and combat poverty, whilst contributing positively to the economic growth of each economy, the creation of new ventures is important.

[14] Source: Ernst & Young Financial Business Advisors calculation on information provider's data.

2.10.1. The economic environment of venture-backed entities

The current economic environment in African economies needs to improve if the venture capital sector is to thrive. The lack of relevant and appropriate legislation hampers the rapid establishment of new enterprises. The inadequate form of financing for these enterprises remains one of the greatest challenges that need to be addressed. However, there is an emerging trend of government trying to assist the SMME sector. The announcement by the Zambian government about creating a new venture fund aimed at addressing this specific problem, is encouraging.

The proposed exit method for this sector and how beneficial it is to the sustainability of these enterprises, is now discussed.

2.10.2. The investment exit method through an IPO

It is clear that the exit of mature ventures through an IPO, is the most viable and profitable method for venture capitalists to exit their investments. For the venture capital industry to flourish and operate at an optimal level, African economies need to create an environment that encourages this exit method, starting with properly functioning securities exchanges. African countries like Botswana and Zimbabwe need to create a securities exchange for the trading of corporate debt and other financial instruments that might aid in availing financing to start-up enterprises.

Some might argue that this is all premature for African economies. This is considering that there are still challenges of access to finance, and inadequate legislation in place - those needs have to be addressed first. However, the empirical evidence from the literature suggests that taking mature enterprises to securities exchanges, is more beneficial in the long run for the entrepreneur and the investors or venture capitalists.

The existing literature derives mainly from developed markets and this study seeks to add to the studies already conducted on the African continent (e.g. Ojah, 2009). This would be by providing guidance for African economies on how to address the challenges being faced by SMMEs, and by creating a stimulating environment for this sector in order for it to ultimately contribute to the GDP of each African economy.

CHAPTER 3

METHODOLOGY

3.1 Introduction

This chapter deals with the research methodology chosen to carry out the research, and also the design and limitations of the study. The advantages and disadvantages of using the qualitative research methodology are discussed. The research methodology addresses the research questions in chapter 1. The research questionnaire is meant to address the problems identified in Chapter 1. The research methodology will also compare the outcomes of the study with the literature reviewed in chapter 2. The study will use a qualitative research methodology approach. Qualitative research is defined as research devoted to developing an understanding of human systems or large cultural systems. The author discusses the type of data to be collected and its analysis. The research instrument is discussed under the 'research design' subsection.

3.2. Research Methodology

3.2.1. Data

The qualitative data were obtained from the respondents to the survey. The respondent's answers were analysed and interpreted, to arrive at a meaningful conclusion. Qualitative data are considered to be the "rough materials researchers collect from the world they are studying; they are the particulars that form the basis of analysis" (Bogdan and Biklen, 1992, p. 106).

3.2.2. Choice of Methodology

Zikmund (2003, p. 110) states that "exploratory research is a useful preliminary step that helps ensure that a more rigorous, more conclusive future study will not begin with an inadequate understanding of the nature of the management problem". Usually, exploratory research provides greater understanding of a concept or crystallises a problem, rather than providing precise measurement or quantification. Exploratory research has therefore been chosen for this study.

The research conducted is a first step towards gaining a broad understanding on the challenges and opportunities facing venture capital in African economies. Zikmund (2003, p. 111) states that "the purpose of exploratory research is intertwined with the need for a clear and precise statement of the

recognised problem", and further that "there are three interrelated purposes for exploratory research: (1) diagnosing a situation, (2) screening alternatives, and (3) discovering new ideas."

A research questionnaire was designed and sent to participants in the study to collect data (Appendix A).

Qualitative research methods typically include interviews and observations, but may also include case studies, surveys, and historical and document analyses. Qualitative research is conducted in a natural setting, without intentionally manipulating the environment. The qualitative research method was used for the survey - the administration of a standardised questionnaire to a sample of respondents.

The importance of using this research method is that the respondents will complete the questionnaire sent to them and return it by mail once complete. This will eliminate bias, as the outcomes of the survey will be analysed and interpreted, outlined and discussed without any manipulation. The survey is appropriate because many of the respondents finance these small enterprises (i.e. SEDA, Business Partners). They also understand the challenges that SMMEs face on a daily basis. The respondents have performed extensive research on African economies and some work for the government agencies (i.e. SEDA, Business Partners). The respondents have performed and continue to perform extensive research on African economies and their securities exchanges.

The outcomes of the survey are discussed in chapter 4.

In the population sampling section a number of institutions where the research questionnaire was sent to, are listed.

The research also involved reading publications released by the institutions mentioned, as well as the Africa-Growth Agenda. These institutions carry out weekly, quarterly and yearly surveys on companies backed by private equity investments, and the financing methods being deployed.

3.3. Analysing qualitative data

Qualitative researchers choose their analysis methods, not only by the research questions and types of data collected, but also based on the philosophical approach underlying the study.

There are different kinds of ways of interpreting qualitative data, and they are listed below:

3.3.1. Interpretive techniques

The most common analysis of qualitative data is observer impression. Here expert or bystander observers examine the data, interpret it via forming an impression, and then report their impression in a structured and sometimes quantitative form.

3.3.2. Coding

Coding is an interpretive technique that both organises the data and provides a means to introduce the interpretations of it into certain quantitative methods.

3.3.3. Recursive abstraction

Some qualitative datasets are analysed without coding. A common method here is recursive abstraction, where datasets are summarised; those summaries are then further summarised, and so on. The end result is a more compact summary that would have been difficult to accurately discern without the preceding steps of distillation.

3.3.4. Mechanical techniques

Some techniques rely on leveraging computers to scan and sort large sets of qualitative data. At their most basic level, mechanical techniques rely on counting words, phrases, or coincidences of tokens, within the data. Often referred to as content analysis, the output from these techniques is amenable to many advanced statistical analyses.

The author has applied the interpretative method for analysing the outcomes of the survey. This method is suitable, as the respondents provided their professional opinion based on their experience in the industry they work in.

3.4. Research Design

The research instrument is a form of a questionnaire that was sent to respondents in the survey. The survey research method employed is where the unit of analysis is the individual respondent. A structural questionnaire was designed and sent to different institutions and experts in this field (Savenye and Robinson, 2005). It reduces bias that may be introduced in the study, in order to obtain the intended outcome by the researcher.

The research questionnaire can be completed at the respondent's convenience and permits and provides a more detailed analysis than interviews. The disadvantage of this form of research is that some participants are not willing to complete the questionnaire. The risk of subjectivity is also increased, as there is difficulty obtaining verifiable data to compare to the respondents answers.

The questionnaire is attached as Appendix A. The respondents were asked to provide their professional opinion based on their years of experience in the industry on the thesis topic.

The types of questions are investigative. *Investigative questions* are defined as specific questions the researcher must answer to provide sufficient detail and coverage of the research question (Cooper and Schnidler, 2011). This is the most appropriate form of questions for the study.

3.5. Population Sampling

Qualitative research involves non-probability sampling - where little attempt is made to generate a representative sample. For this study we have applied 'purposive sampling' - a process where the researcher chooses participants arbitrary for their unique characteristics or their experience, attitudes, or perceptions. As conceptual or theoretical categories of participants develop during the research process, researchers seek new participants to challenge emerging patterns (Cooper and Schnidler, 2011). To ascertain the importance of venture capital in African economies, it was important to choose a sample of experts in the field.

The population consists of industry associations, venture capitalists, entrepreneurial institutions, and fund managers who invest in African economies, the Development Banks, commercial financial institutions and market researchers who have extensive knowledge of market conditions and macro-economic conditions. These institutions have knowledge of the challenges that entrepreneurs encounter, and form the core of data collection and analyses.

The list of experts and policy makers is listed below, and the profile of those who responded to the questionnaire is provided in chapter 4:

The research questionnaire was sent to the following institutions:

1. African Development Bank
2. Africa Alliance
3. African Venture Capital Association

4. Audax Ideas
5. Business Partner (South Africa)
6. Capital Africa
7. Coppernet Zambia
8. Coronation Fund Managers
9. Deloitte Corporate Finance
10. Development Bank of Southern Africa
11. Ernst &Young Africa Business Centre
12. Fund managers who invest in Africa
13. Future Growth Asset Management (Responsible Investment)
14. Government Employee Pension Fund
15. Helios Private Equity (Africa Practice)
16. Horizon Equity Partners
17. Identity Partners
18. Industrial Development Corporation
19. i.e. Consulting (UK)
20. Imara S.P. Reid Research Division
21. Invenfin Venture Capital
22. Institute of Behavioural Finance
23. Jacque Malan Consultants and Actuaries
24. Kagiso Trust
25. Khula Enterprises
26. KPMG Private Equity Practice
27. KPMG Malawi
28. Medu Capital

29. Metier
30. National Empowerment Fund
31. OMIGSA African Private Equity Fund
32. Pan African Development Fund
33. Quickberry Venture Capital Firm
34. Reyakgona Hygiene Services (SMME)
35. Sanlam Investments (Africa Business)
36. Sasfin Bank
37. Sentinel Mining Retirement Fund
38. South African Department of Economic Development
39. South African Department of Trade and Industry
40. Southern African Regional Poverty Network
41. South African Venture Capital Association
42. South African Economic Development Agency
43. Venture P. Com

Some of the selected institutions have a wide footprint in the Africa Continent (e.g. KPMG, Ernst & Young, Africa Alliance, African Development Bank, African Venture Capital Association, Imara S.P. Reid, Kagiso Trust, and OMIGSA African Private Equity Fund). Their views thus derive from an in-depth knowledge of African economies.

3.6. Limitations of the study

While the study proposes to evaluate the prospects of venture-backed enterprises and to make recommendations about what needs to be done to address the impediments this section of the financing industry faces, there are also challenges that the researcher faces in carrying out this study.

The author has chosen a qualitative method of research, instead of the quantitative method, as there is currently limited quantifiable, standardised information on measuring the impact of venture capital-financed enterprises in African markets. There is also no accurate and properly collated data

relating to the performance of venture capital-financed enterprises and their exit strategies in these markets.

There are also no financial data in the form of a time series for venture backed enterprises on the different African securities exchanges. This could make it difficult to compare their performances with those of developed markets, like the USA, Japan, UK and Germany, to clearly demonstrate the role of venture capital finance in the creation of public companies.

A means of addressing the difficulty of obtaining data in other African economies (e.g. East, West and North Africa), was through the study and analysis of the weekly updated review by Africa Alliance, which performs extensive research on African economies.

CHAPTER 4

RESULTS OF THE STUDY

4.1. Introduction

This section discusses the outcomes of the study and is divided into four sections. The first is the outcomes of the survey and discussion of the outcomes, followed by the demographic profile of respondents. The final section is the results of the study, which summarises the outcomes and compares them to the literature reviewed in chapter 2. By comparing the survey's outcomes with the literature review, some of the major impediments to and prospects for the SMME sector, are highlighted.

The results of the survey table below, provides us with the responses from the different participants

Number of questions	Research questions	Yes	No	South African Venture Capital Association	Africa Alliance, (i.e. Researchers and Asset Managers)	Business Partners	KPMG (African Private Equity Practice)
	Number of respondents			**1**	**2**	**3**	**4**
	Country of operation and activities			**Africa (South Africa)**	**Rest of Africa**	**Rest of Africa**	**Rest of Africa**
1	Do current business regulations in African economies allow for the faster establishment of a business?		No	But this is not the major stumbling block	Many countries have been reforming their business regulations to make this easier. We believe that LS, ZA, BW and ZW have done some steps in this direction, but it is highly dependent on the skills at the responsible government departments. But overall we think that this can be achieved with adequate resources and political will; during the past few years Rwanda has climbed rankings in doing business has been the best reformer globally; this is certainly achievable.	There is so much red tape. In fact this inhibit conclusion of transactions.	No they do not
2	Are the funding models currently being applied by banks, (i.e. credit history or earnings track record) appropriate in addressing the challenges faced by start-up enterprises?		No	The Financial Institutions, in particular the banking sector is not doing enough. There is lack funding models that will assist SMMEs.	Start-ups don't have any of these. There needs to be a structure to assess the business idea and not the "historical" factors. Need to be able to scout and support the business concept.	Banks are not risk takers; hence they funding models are usually tailored towards securitised-based transactions. Start-up ventures are usually risky.	Banks are commercial enterprises and cannot take on excessive risks. 1 in 10 venture capital operations survive. This record is not bankable.
3	Will the current state of African economies security exchanges (i.e. illiquid and hampered by corruption, weak legislation and gross inadequacy of infrastructure) contribute to the low levels of venture capital finance-backed IPOs?	TRUE		Liquidity constraints in the African securities markets have also contributed negatively to these low levels. The lack of funding for supporting these enterprises is also contributing to these low levels. In appropriate regulations to ensure that investor's assets are protected.	The current state of many African securities exchanges are far from what you described (hampered by corruption, weak legal system and inadequate infrastructure). There are large liquid exchanges (eg Kenya, Nigeria, SA) and largely illiquid exchanges which have specific reasons for illiquidity (typically limited investment options available in those countries so investors apply buy and hold strategies).	No Comment	No comment

Number	Research questions	Yes	No	South African Venture Capital Association	Africa Alliance, (i.e. Researchers and Asset Managers)	Business Partners	KPMG (African Private Equity Practice)
	Number of respondents			**1**	**2**	**3**	**4**
	Country of residence and operatoin			**South Africa**	**Africa**	**Africa**	**Africa**
4	Do the policy makers in African economies have a critical role to play in creating a stimulating environment for venture capital finance-backed initiatives?	Yes		There is a need for aggressive marketing and selling the success stories of the previous entrepreneurs who have succeeded.	Government / policy makers needs to: Encourage entrepreneurship, especially technical and management training. Private sector should: provide adequate funding for risky ventures, currently there are no incentives and extensive effort to fund startups. Government should: make it easy to set-up new businesses. Tax incentives would also channel more capital into the sector.	It could be through an enabling environment whereby financial institutions can finance transactions without rigorous legal framework for instance red tape in terms of property registrations in the deed office delays everything	The policy makers can contribute through some form of tax breaks for Venture Capitals
5	Would a Public Private Partnership (PPP) between government and private sector financiers, to create a specific new venture creation fund for start up enterprises, be beneficial?	Yes		This model has worked. In South Africa the government went into partnership with Business Partners and others.	This is one way of doing it. Effectively government should provide incentives (and where appropriate subsidies) where a privately run investment fund could take the risk of investing in venture capital, potentially sharing some of the risk with government. We think that the private sector has better skills to manage this process than government; however government involvement would be essential in this process.	As long as the operations of the fund are left at capable private managers, success is probable.	It can only operate only if the following conditions are in place and enforced: Efficiency and independency
6	Would the creation of a financial institution (i.e. new venture creation bank), that is specifically focused on providing financing that's tailor-made for start-up enterprises be beneficial?		No	In South Africa currently there are many financing institutions, (e.g. Khula, Seda, IDC, NEF) just to mention a few. Creating other instititutions will not necessarily improve the financing constraints. These institutions need to be utilised more effectively.	This could work, but is has to be run on commercial basis and by private sector. There are many cases of development institutions that have been hampered by government bureaucracy, lack of skills and necessary technical ability to identify and support start up businesses. There are numerous case studies where often "concessionary funders" are worse in supporting the growth phase of new companies than for profit investors; donors often pull out or limit funding even when the company is about to make a critical breakthrough in the market.	A specialized tailored bank would help because the focus will be understanding intricacies of SME sector. In other words, it would be an entrepreneurial bank as opposed to securitised bank.	For this institution to work the following conditions should be in place and enforced: (1) Run it out of an established bank. (2) The government will be required to underwrite all or a portion of the losses as this is far in excess of normal banking risk. (3) The bank should account for its Venture Capital investment to a Joint Committee made up of both bank and government representative.

Number	Research questions	Yes	No	South African Venture Capital Association	Africa Alliance, (i.e. Researchers and Asset Managers)	Business Partners	KPMG (African Private Equity Practice)
	Number of respondents			**1**	**2**	**3**	**4**
	Country of operation and activities			**Africa (South Africa)**	**Rest of Africa**	**Rest of Africa**	**Rest of Africa**
7	Does the behaviour and psychology of investing have any impact/contribute to the low levels of venture-backed IPOs?				No comment	No Comment	The market capitalisation of less than R200m and no track record influences the investors to sell the business privately amongst themselves.
8	Does the behaviour and psychology of investing have anything to do with the private placement exit method of ventures?			No comment	The behavior of the ivnestors are influenced more by the economic environement in each african region	No Comment	This question is supported by the one above. The market capitalisation of less than R200m and no track record influences the investors to sell the business privately amongst themselves.
9	Is the Initial Public Offering (IPO) through a securities exchange a viable investment exit strategy for investors in Africa's markets?	Yes		No comment	IPOs tend to give a broader section of investment public and encourage more transparency in the listed business. Private placements are often done in private companies, which hope to list one day, and hence disclosure tends to be weaker, and prospect of trading unlisted shares is also more problematic.	No Comment	The company must have at least a market capitalisation of R200m in order to attract investors and be able to absorb the significant costs of listing and maintaining the listing.
10	What do the policy makers in African economies need to do to create an economic environment that encourages entrepreneurship?		FALSE	Inappropriate regulations. There is a need for aggressive marketing and selling the success stories of the previous entrepreneurs who have succeeded. Entrepreneurial education from school level should be built in curriculum.	Entrepreneurship needs to begin at an early level (school and home). Despite many business schools "teaching" entrepreneurship. We don't believe that people who are not "born" entrepreneurs can easily start and commercialise new ideas. Hence the need for support, as well as access to experienced management skills. Also, entrepreneurship should be shown as a viable career option. In many cultures entrepreneurship is seen as a "fall back" option – if you cannot get a decent job in the formal sector then you can start your own business. Focus should also be placed on differentiating "survival" entrepreneurs (those that have businesses just to survive) from those entrepreneurs who are able to create growth companies and provide substantial employment with their ideas.	Relax legal framework governing SMMEs.	Increase tax breaks for Venture Capitals, reduce red tape for business and ultimately stamp out corruption

Name of respondents	Research questions	Ernst & Young (African Business Practice)	Sasfin Bank	Venture P. Com	Metier
	Number of respondents	**5**	**6**	**7**	**8**
	Country of operation and activities	**Rest of Africa**	**South Africa**	**South Africa**	**South Africa**
1	Do current business regulations in African economies allow for the faster establishment of a business?	It varies from country to country. There are advanced markets and permitive ones.	No comment	Yes, although not fully utilised	Not sure – I haven't looked to establish a business outside of SA
2	Are the funding models currently being applied by banks, (i.e. credit history or earnings track record) appropriate in addressing the challenges faced by start-up enterprises?	Most of the banks are risk averse; and that can be understood considering the pressure they are under to preserve the capital deposited by their clients. However, most business bankers do not have an understanding of how the business work and the models they use to assess credit worthiness is more consumer-loan focused than productive loan-focused.	Banks in general are aversed to funding start-ups and they are not prepaired to take the risk	Most startup enterprises aren't in a position to produce such, as there is no prior record or record	Earnings and credit history are indicative of risk – but there are many other factors most of which can't be assessed
3	Will the current state of African economies security exchanges (i.e. illiquid and hampered by corruption, weak legislation and gross inadequacy of infrastructure) contribute to the low levels of venture capital finance-backed IPOs?	African stock exchanges are not necessarily hampered by corruption. They are not connected to the rest of the financial markets. Information about African Economies is not readily available to the world of investors, so the valuation and risk assessment cannot be done without these two. We cannot expect investors to support us. Investment decisions are based on comparable information about the potential return on investment.	No comment	investors may view as an opportunity to participate in revenue generating activitiesthat they would otherwise not have access to because of (mal-pratised) exchange procedures	As an investor looking at Africa, the lack of established secondary markets that we could sell into are certainly a negative factor that we are conscious

Number of questions	Research questions	Ernst & Young (African Business Practice)	Sasfin Bank	Venture P. Com	Metier
	Number of respondents	**5**	**6**	**7**	**8**
	Country of residence and operatoin	**Africa**	**South Africa**	**South Africa**	**South Africa**
4	Do the policy makers in African economies have a critical role to play in creating a stimulating environment for venture capital finance-backed initiatives?	It is not necessarily the government who need to play a significant role. Venture Capitalists by their nature are opportunity spotters who see potential where not many people can. Governments on the other hand might just promote their country as the best investment destination. They can create legislation to encourage investment in general and venture capital is one of the consequence of a good entrepreneurial culture.	No comment	With good polieces in place, foreign and local investorscould participate with larger amounts(e.g Bharti Airtel sagawith MTN where too many restrictionswere being imposed on the ale/meger by gov, leading to no deal. Also seen with Wallmart.)	Maybe they do, but I's minimal. Venture capital (early stage private equity) is very high riskinvestment that is arguably not really successful anywhere in the world. Even later stage investment in Africa is difficult to do in an high risk, so venture capital is just that much harder
5	Would a Public Private Partnership (PPP) between government and private sector financiers, to create a specific new venture creation fund for start up enterprises, be beneficial?	Public Private Partnerships, especially in a form of a development finance institutions would definately be beneficial	Banks in general are aversed to funding start-ups and they are not prepaired to take the risk. This partnership will also be run on commercial terms	Unlike cases of strictly private sector, the mixture will address the need of start ups without achieving a set IRR	It all helps to reduce the risk. But what is a PPP like that, other than cheap capital for a VC to invest?
6	Would the creation of a financial institution (i.e. new venture creation bank), that is specifically focused on providing financing that's tailor-made for start-up enterprises be beneficial?	There are already many venture capital and private equity firms which are specifically focused in African economies.	Banks in general are aversed to funding start-ups and they are not prepaired to take the risk. This instiution will also be run on commercial terms that the normal banks are currently applying	To a certain degree yes , but start-ups face more than financial challenges i.e. opretional, manegerial and track record(reference for new business)	Lending to start-ups is virtually impossible. No track record, no assets. Only way is equity.

Number of questions	Research questions	Ernst & Young (African Business Practice)	Sasfin Bank	Venture P. Com	Metier
	Number of respondents	**5**	**6**	**7**	**8**
	Country of operation and activities	**Africa**	**South Africa**	**Africa (South Africa)**	**Africa (South Africa)**
7	Does the behaviour and psychology of investing have any impact/contribute to the low levels of venture-backed IPOs?	No comment	Stock exchange is an illiquid market	the idea that many people have is that venture backed IPOs are high risk	Not sure. Do not have extensive knowledge of the subject
8	Does the behaviour and psychology of investing have anything to do with the private placement exit method of ventures?	The risk reward ratio is skewed in favour of defensive investment. Some private business people do not see investing in a business through a stock exchange as an viable option. It takes an appreciation of the value of taking calculated risks, rather than assuming preservative stance.	Stock exchange is an illiquid market. Investors would want to realise their proceeds/cash immediately	It is easier with regars o sale and other regulations partaining to tax and trade, and sale of capital gains fro one person to the other than other means of exist	Not sure. Do not have exact knowledge of the impact of investors behavior in relation to exiting mature ventures
9	Is the Initial Public Offering (IPO) through a securities exchange a viable investment exit strategy for investors in Africa's markets?	Most of the investors are more interest in getting best returns on their investments. The exit method does not play a critical role in their decisions.	Not sure. Do not have much knowledge around this investment exit strategy	To a certain extent it creates citezen empowerment, but, IPO has its difficulies, especially when it doesn't raise the desired equity	Its possible. But very few Venture Capital investments grow large enough to exit on a stock exchange. Given illiquidity of African exchanges means that the companies need to be even bigger to warrant even considering listing
10	What do the policy makers in African economies need to do to create an economic environment that encourages entrepreneurship?	Exit of any venture for an investor should be for optimum returns. So, if an IPO will provide investors with the best price, then it should be done. The decision is purely an investment one, which should be influenced by what is best for the investor.	Not sure.	No comment	Not sure. Do not have exact knowledge of the African market conditions.

Number of questions	Research questions	Small Enterprise Development Agency	SMME: Entrepreneur	Jacque Malan Consultants and Actuaries	Imara. S.P Reid: Research Division
	Number of respondents	**9**	**10**	**11**	**12**
	Country of operation and activities	**South Africa**	**Africa (Botswana, South Africa and Swaziland)**	**South Africa**	**Rest of Africa**
1	Do current business regulations in African economies allow for the faster establishment of a business?	The new Companies Act was set up to ease business registrations. It is probably too soon to comment on its effectiveness.	Too much political interference. (eg.some countries require foreign investorsto shed 51% stake to locals)	The current legislative requirements are onerous and complicated (eg Value Added Tax and Labour laws)	It takes a number of days to merely get a registration further to that most African countries have a number of permitting requirements which stifle investment rather than promote it.
2	Are the funding models currently being applied by banks, (i.e. credit history or earnings track record) appropriate in addressing the challenges faced by start-up enterprises?	Not entirely. Banks fund based on risk, and not really on the business idea. Historical data like your credit history tends to carry more weight than your business idea, or entrepreneurial drive. The repayment terms could also be more flexible, maybe allow the start up to get as close to breakeven point before the loan repayments kick in.	Banks demand too much from greenfield projects. The credibility requirements and reting criteria is too strict and restrictve/prohibitive	The banking institution is not structured to finance venture capital.	I appreciate the credit analysis by Banks as its primary function is to reduce asymmetric information and moral hazard on the part of the borrower. That said start-up enterprises could do with support from Developmental Banks and Small Business Support Agencies. Banks are risk managers and they have little motivation to increase their risk for limited beneficial exposure.
3	Will the current state of African economies security exchanges (i.e. illiquid and hampered by corruption, weak legislation and gross inadequacy of infrastructure) contribute to the low levels of venture capital finance-backed IPOs?	My take is that the volumes are too low, and one thus cannot connect between the two.	Businee confidence remains low. Volatility of the political environment translates into a weak market from continued illtimed and rather misinformed threat of nationalisation is long term potential market distabiliser.	No comment	Not at all a number of exchanges notably the JSE and BSE have provisions for the listing of venture capital firms. The real problem is sufficient investor education in venture capital. The TSX (Toronto) and the LSE's AIM have a thriving junior mining exchange which invest in some risk perceived areas of Africa. So actually African venture capital has a better chance on the TSX or Aim rather than the JSE due to low investor education on the sector

Number	Research questions	Small Enterprise Development Agency	SMME: Entrepreneur	Jacque Malan Consultants and Actuaries	Imara. S.P Reid: Research Division
	Number of respondents	**9**	**10**	**11**	**12**
	Country of residence and operatoin	**South Africa**	**Africa**	**South Africa**	**South Africa**
4	Do the policy makers in African economies have a critical role to play in creating a stimulating environment for venture capital finance-backed initiatives?	Yes; they need to open up markets for small entrepreneurs. Entrepreneurs need to know that they are starting a business in a market where they can still profit from, as opposed to flooding an already saturated market.	Venture capital finance-backed initiatives depend on the ongoing poitical setup.	No comment	An enabling environment is a policy issue there is more that can be done via government sponsored agencies.
5	Would a Public Private Partnership	Most definitely. Run along private sector business principles but with developmental considerations which call for a bit of risk taking. The state would somehow need to cover the risks.	Funding is a serous challenge. A genuine PPP might help a lot, (e.g Umsobomvu/NYDA does not help young entrepreneurs). It is too far fetched for an ordinary South African	It is suitable depending on size and nature of business	Government participation is always perceived by markets to be politically motivated and more so in Africa. See YDA, IDC and other agencies that have been reduced to political agencies by the market and media.
6	Would the creation of a financial institution (i.e. new venture creation bank), that is specifically focused on providing financing that's tailor-made for start-up enterprises be beneficial?	There are quite a number of government funded institutions that should be playing in this space. I don't think creating a new one will add any value. What is needed is better coordination of the already existing ones and improved monitoring of whether they operate as mandated.	It will help bridge the very	No comment	Yes but who will ultimately carry the underlying risk of the venture. Promotion of venture capital exchange looks the better option. If the risk is carried by someone else there is no motivation for the venture to succeed.

Number	Research questions	Small Enterprise Development Agency	SMME: Entrepreneur	Jacque Malan Consultants and Actuaries	Imara. S.P Reid: Research Division
	Number of respondents	**9**	**10**	**11**	**12**
	Country of operation and activities	**Africa (South Africa)**	**Rest of Africa**	**Africa (South Africa)**	**Rest of Africa**
7	Does the behaviour and psychology of investing have any impact/contribute to the low levels of venture-backed IPOs?	Not sure	Yes	No comment	Efficient Market Theory tells us that at any time there are heterogeneous expectations across the market so a security will always be priced on risk and if there is sufficient return for the risk it can motivate investment
8	Does the behaviour and psychology of investing have anything to do with the private placement exit method of ventures?	Not sure	Not sure. Do not have knowledge	No comment	No comment
9	Is the Initial Public Offering (IPO) through a securities exchange a viable investment exit strategy for investors in Africa's markets?	Not really au fait with IPOs in Africa, but I guess there is probably better transparency and more information in an IPO than a	Not sure. Do not have knowledge of the subject	The exit of an investment varies on time and depends on market cycle	It has proved very popular in Botswana where recently the development agency BDC invested in Cresta and used the IPO as an exit strategy the move was well received and in my opinion offers a credible option.
10	What do the policy makers in African economies need to do to create an economic environment that encourages entrepreneurship?	There needs to be a collaborative effort between the two. Private sector financiers should partner with government to co invest in some of the start ups, especially social entrepreneurs that talk to the government's mandate.	National Leaders must give profesionals and entrepreneurs more sope to operate	The policy makers needs to create an environment that is curruption free and provide mentorship to new entrepreneurs	Create an enabling environment e.g. tax incentives for business promotion, addition of SMMEs into supply chain along with a number of other initiatives

Number of questions	Research questions	Yes	No	Coronation Fund Managers	Kagiso Trust	Future Growth: Responsible Investment	Audaxideas
	Number of respondents			**13**	**14**	**15**	**16**
	Country of operation and activities			**Africa (South Africa)**	**Rest of Africa**	**Africa (South Africa)**	**Rest of Africa**
1	Do current business regulations in African economies allow for the faster establishment of a business?	Yes		Too much regulatory admin and time needed to register a company.	More African countries need to feature in the top 20 places that provide an ease of doing business in the world.	yes	No comment
2	Are the funding models currently being applied by banks, (i.e. credit history or earnings track record) appropriate in addressing the challenges faced by start-up enterprises?		No	Very low risk appetite	Start-ups by nature have no credit history since they have not previously operated. To circumvent the problem, financial institutions request more security from the owner who is not able to provide it.	Although start-up enterprises don't have much history, they can always check on the key-management's track record	Yes they are.
3	Will the current state of African economies security exchanges (i.e. illiquid and hampered by corruption, weak legislation and gross inadequacy of infrastructure) contribute to the low levels of venture capital finance-backed IPOs?	Yes		Yes they have and will to continue to have a negative impact.	IPO in a country of origin is not necessary. Perceived corruption on the African countries should not be translated to corruption on the security exchange as that is a function of willing buyer/willing seller based on publicly available information. There can be primary listing in foreign countries.	Illiquidity, corruption, weak legislation and gross inadequacy of infrastructure will never positively influence these levels	yes

Number	Research questions	Yes	No	Coronation Fund Managers	Kagiso Trust	Future Growth: Responsible Investment	Audaxideas
	Number of respondents			**13**	**14**	**15**	**16**
	Country of residence and operatoin			**South Africa**	**South Africa**	**South Africa**	**South Africa**
4	Do the policy makers in African economies have a critical role to play in creating a stimulating environment for venture capital finance-backed initiatives?	TRUE		Policy makers do have a critical role to play in their respective economies	There is an important role to be played, both from attracting capital and creating an enabling environment for capital repatriation.	They could definitely contribute to a more stimulating environment by for instance creating tax advantages. According to our compliance officer it wouldn't help much, because of risk-adversity in SA	Policy makers do have a critical role to play in creating a stimulating economic environment for business owners
5	Would a Public Private Partnership (PPP) between government and private sector financiers, to create a specific new venture creation fund for start up enterprises, be beneficial?	Yes		Could be – depending on how well it is implemented	It would probably decrease the cost of borrowing for businesses and may be more developmental in nature.	Yes	Poor track record of govt initiatives in this area
6	Would the creation of a financial institution (i.e. new venture creation bank), that is specifically focused on providing financing that's tailor-made for start-up enterprises be beneficial?	Yes		Yes	90% of start-up companies fail, so the returns for a bank that is solely focused on start-up would be less than ideal.	Yes	This seems to describe current venture capital funds

Number	Research questions	Yes	No	Coronation Fund Managers	Kagiso Trust	Future Growth: Responsible Investment	Audaxideas
	Number of respondents			**13**	**14**	**15**	**16**
	Country of operation and activities			**Africa (South Africa)**	**Rest of Africa**	**Africa (South Africa)**	**Rest of Africa**
7	Does the behaviour and psychology of investing have any impact/contribute to the low levels of venture-backed IPOs?		No	Portfolio managers don't like losing money, therefore they are risk averse if not compensated by the potential for higher return	Investment psychology has to do with creation of wealth, if wealth can be created and appropriate risk for an investor any model can be pursued.	It's a matter of risk and return. If returns are too low compared to the risk, then levels of investment stay low.	No comment
8	Does the behaviour and psychology of investing have anything to do with the private placement exit method of ventures?		No	Proven track is record required	Private placing is not an exit method, as a new fund or venture can raise money on the market through the private placing method. However, it can also be used as a exit method where investors offer their shares to potential buyers at an attractive price.	Yes	No comment
9	Is the Initial Public Offering (IPO) through a securities exchange a viable investment exit strategy for investors in Africa's markets?	Yes		It can be – investors need track record as above and are cautious	When executed properly it provides investors appropriate returns as value of shares can drop from date of listing or the market may not be deep to allow exit of large stake which may have to be done through a book-build method.	Definitely, but haven't seen it much. More secondary market sales.	Yes it is
10	What do the policy makers in African economies need to do to create an economic environment that encourages entrepreneurship?			Deregulate as much as possible and create a flexible environment entreprenuers	There is a need to provide an environment in which company laws are easily understood and cost of compliance is reasonable. In addition, cost of borrowing should be affordable and capital should be available.	Tax advantages would probably help a bit. Creating better infrastructure, a safer environment, more stable politics, better education levels, etc would lower the risk and thus potentially encourage entrepreneurship.	No comment

Number of questions	Research questions	YES	NO	Sentinel Mining Retirement Fund	Invenfin Venture Capital	KPMG Malawai
	Number of respondents			**17**	**18**	**19**
	Country of operation and activities			**South Africa**	**South Africa**	**Africa (Malawi)**
1	Do current business regulations in African economies allow for the faster establishment of a business?	YES		Red tape prohibits ease of establishment.	Refer to World Bank ease of doing business surveys, it outlines the challenges and opportunities.	It takes so long before a business can be registered and the procedures are numerous
2	Are the funding models currently being applied by banks, (i.e. credit history or earnings track record) appropriate in addressing the challenges faced by start-up		NO	Unfortunately banks are similar to short-term insurance – they only assist those that do not need money.	As banks require assets to secure loans which start-ups do not have	Banks need to move to another platform in assessing their new business potentials. They need to focus on future potentials
3	Will the current state of African economies security exchanges (i.e. illiquid and hampered by corruption, weak legislation and gross inadequacy of infrastructure) contribute to the low levels of venture capital finance-backed IPOs?	YES		The current capital maket conditions hampers exit strategies.	Venture Capital backed businesses most often are exited through trade sales and not IPOs. Exchanges do tend to be well regulated in markets where there are VC investors & companies	Venture capital are a concern esp. where you consider the source of funding. As such with deep African corruption, the venture capilist remains exposed.

Number	Research questions	Yes	No	Sentinel Mining Retirement Fund	Invenfin Venture Capital	KPMG Malawai
	Number of respondents			**17**	**18**	**19**
	Country of residence and operatoin			**South Africa**	**South Africa**	**Africa (Malawi)**
4	Do the policy makers in African economies have a critical role to play in creating a stimulating environment for venture capital finance-backed initiatives?	TRUE		Provision of a stable economic / regulatory environment is key to success.	Need to introduce start-up & VC friendly legislation	Policy makers should embrace the fact that not all capital can be loaned from the traditional banking system
5	Would a Public Private Partnership (PPP) between government and private sector financiers, to create a specific new venture creation fund for start up enterprises, be beneficial?	Yes		They have contradicting agendas.	Gov can help to reduce the risk but not requiring a very high return in PPP - refer to the Israeli model	This will enable the potential investors to have alternative finance for business
6	Would the creation of a financial institution (i.e. new venture creation bank), that is specifically focused on providing financing that's tailor-made for start-up enterprises be beneficial?	Yes		The balance between risk and return will not make this viable.	No – Gov assistance programs & PPP are better. 80% of VC investment is lost which is not good for a bank & we have too few true VC deals	Presently most financial institutions traditional products are a misfit in modern economy

Number	Research questions	YES	NO	Sentinel Mining Retirement Fund	Invenfin Venture Capital	KPMG Malawai
	Number of respondents			**17**	**18**	**19**
	Country of operation and activities			**South Africa**	**South Africa**	**Africa (Malawi)**
7	Does the behaviour and psychology of investing have any impact/contribute to the low levels of venture-backed IPOs?	YES		Exit strategy is purely based on the best alternative at the time of exit.	Trade sales are the most likely exits	To a greater extent current behaviours have an influence. Corruption and risk averse/low risk appetite by investors
8	Does the behaviour and psychology of investing have anything to do with the private placement exit method of ventures?		NO			This is often individual decision which and in most cases driven by personal desires of the acquirer
9	Is the Initial Public Offering (IPO) through a securities exchange a viable investment exit strategy for investors in Africa's markets?		NO	This will depend on the specific market and the timing of the exit.	They could be if they are well managed and timed properly	Large equity holdings may not be easily disposed of on these markets without challenges. The stock exchange has its own challenges
10	What do the policy makers in African economies need to do to create an economic environment that encourages entrepreneurship?			Create stability and allow entrepreneurs to benefit freely from their creativity.	Change legislation & decrease risk	Policy makers need to make some deliberate policies which will unlock the potential in individuals wanting to invest in various industries. Presently certain industries are under invested.

Number of questions	Researchquestions	Yes	No	OMIGSAAfrica Private Equity Funds	CoppernetZambia
	Numberof respondents			**20**	**21**
	Countryof operationand activities			**Africa (Botswana,Egypt,Ghana, Mauritius,Morocco,Nairobi, Namibia,Nigeria,Tunisia)**	**Zambia**
1	Do current business regulationsin African economies allow for the faster establishment of a business?	Yes		Most African economies, SA included do not have coherent or well understoodsystems, even by theirownlawyers	Countries have provided ways in which to do so in an effort to improve investor confidence and attract investment into their countries. Through their Investment Agencies established under their irrespective governments it is possible to see how this has been done. Zambia, for example, has the Zambia Development Agency. Although there is still plenty that can be done to further improve these systems it is sufficient to say that measures are in place to improve the speed of establishement.
2	Are the funding models currently being applied by banks, (i.e. credit history or earnings track record) appropriate in addressing the challenges faced by start-up enterprises		No	Banks are there primarily to preserve the savings of people, not to invest in businesses	No, the current financing models are not appropriate
3	Will the current state of African economies security exchanges (i.e. illiquid and hampered by corruption, weak legislation and gross inadequacy of infrastructure) contribute to the low levels of venture capital finance-backed IPOs?	Yes		The main hold back is the lack of investors in African exchanges due to few institutions	It is still a serious concern raised by investors and has resulted in many cases to financing difficulties

Number	Research questions	Yes	No		Coppernet Zambia
	Number of respondents			**20**	**21**
	Country of residence and operatoin			**South Africa**	**Zambia**
4	Do the policy makers in African economies have a critical role to play in creating a stimulating environment for venture capital finance-backed initiatives?	TRUE		Not sure	It is essential that policy provide for the protection of financiers in the market by putting in place ways in which funds can be protected from unnecessary risk. It is also important that the right systems be in place, such as quick access to court systems and other dispute resolution arrangements. Financiers would also be intested in exit strategies for funds and banking policies as well, amongst other things.
5	Would a Public Private Partnership (PPP) between government and private sector financiers, to create a specific new venture creation fund for start up enterprises, be beneficial?	Yes		However, Govt generally does not like the private sector making money and the want to hold as many cards as possible	It is increasingly considered important that investments be anchored for the benefit of locals. Government participation inspires local confidence and is likely to reassure the investor that the enterprise will be taken seriously.
6	Would the creation of a financial institution (i.e. new venture creation bank), that is specifically focused on providing financing that's tailor-made for start-up enterprises be beneficial?	Yes		What is lacking most is not capital, but actual entrepreneurs, but yes, such an institution would help	It is for this reason that Micro- Financing institutions are as successful as they are in Africa at the moment

Number	Researchquestions	Yes	No	OMIGSAAfrica PrivateEquity Funds	CoppernetZambia
	Numberof respondents			**20**	**21**
	Countryof operationand activities			**Africa (Botswana,Egypt,Ghana, Mauritius,Morocco,Nairobi, Namibia,Nigeria,Tunisia)**	**Zambia**
7	Does the behaviour and psychology of investinghave any impact/contributeto the lowlevelsof venture-backedIPOs?	Yes		No, many venturesare simply too smallto list	Yes, it doeshavean impacton the methodsof investing
8	Does the behaviour and psychology of investinghaveanythingto do withthe private placementexitmethodof ventures?		No	No, many venturesare simply too smallto list	Yes, it doeshavean impacton the methodsof investin
9	Is the InitialPublicOffering(IPO)through a securitiesexchangea viable investmentexit strategyfor investorsin Africa'smarkets?		No	No, many venturesare simply too smallto list	Yes
10	What do the policy makers in African economiesneed to do to createan economic environment that encourages entrepreneurship?			More tenders geared to local suppliers who manufacturewillopen up the gaps, they will in turn need funding.	Policy makerswould requireeasy, quick and efficient establishmentprocedures, free of unnecessarybureaucracy. They would also require readily available information, via website, etc, so that investors can access information. Policies to reduce corruption would also boost confidence.a bankingand courtsystemthatcaneasilyresolvemattersand the correctinfrastructurefor ease of business. policywouldneedto work to the achievement of thesethings.

4.2. Discussion of results

4.2.1. Analysis of results

The outcomes of the study are reviewed in the summary below, as follows:

Firstly, to be able to properly analyse the outcomes of the study, the interpretive technique methodology was used. From the questionnaire sent out to 43 participants, 21 responses from the participants were received (a 49% response rate). The quality of the participants who responded to the survey, assisted with reaching a meaningful conclusion.

The benefits and importance of the study are not based on the number of respondents, but on the quality of respondents, measured as follows:

(i) Years of experience in the industry
(ii) Level of expertise
(iii) Wide footprint and presence in African economies
(iv) In-depth knowledge of political challenges and risks in African economies.

The responses to the questionnaire indicates that for African economies to grow and make inroads in reducing unemployment and poverty, we need an SMME sector to work efficiently and effectively. Policy-makers are once again requested to play a significant role by implementing the policies they create and formulate. From the responses received and analysed, one can safely conclude that the most prominent challenge in this sector is the access to appropriate and tailor-made funding. A high percentage of respondents indicated that we need an innovative funding model for the SMME sector.

The part of the study where there is no conclusive agreement, is the development of a Venture Bank run by government. Some 50% of the respondents agree that having focused venture institutions can be part of the solution to the funding challenges, while the other 50% indicated that what government needs to do is to run the existing agencies more efficiently and effectively. With regards to the exit of these ventures, the participants agree that IPO is the most effective method.

The source of further problems relating to SMMEs was also raised by respondents. They indicated that the real problem is sufficient investor education in relation to the IPO for venture capital. One of the participants from Imara. S.P. Reid, used as an example the investor education seminars being held by the Toronto Stock Exchange (TSX) and the London Stock Exchange Alternative Investment

Market (LSE AIM), and indicated that they have a thriving junior mining exchange which invests in some risk perceived areas of Africa. One can infer that African venture capital has a better chance on the TSX or AIM than on the JSE, due to low investor education on the sector.

The answers from the participants are supported by the literature reviewed around the role of the IPO market. The literature indicates that the health of the venture capital industry is dependent on the existence of a strong and vibrant IPO market, as venture capitalists generate the majority of their profits from firms that go public. The ability of the venture capital industry and its ability to grow is, therefore, dependent on a strong IPO market (Jain and Kini, 2000). The participants, however, indicated that due to the structural challenges in the African capital markets, this method is not suitable. This has subsequently led to a high number of private placement sales. The other factor that has contributed to a low level of venture-backed IPOs, is the inability of these enterprises to raise the minimum capital required for listing.

A detailed analysis of the outcomes of the survey is provided below. The results received from the survey are analysed and compared with the literature review, and a conclusion is drawn.

4.2.2. Discussion pertaining to the research questions

4.2.2.1. Discussion pertaining to Research Question 1

This research question is meant to investigate and provide feedback on the critical role that policy makers should play in creating a stimulating environment for venture capital. The research question was addressed through research questionnaire questions 4 and 10. The responses of the participants are discussed below.

For any sector of the economy to succeed and thrive, government needs to play a critical role. Participants indicated that entrepreneurship should be encouraged as a viable career option, with the opening up of markets for small entrepreneurs. This part of the study is strongly supported by the literature about the faster starting up of a business. This can be through ensuring that the economic environment is conducive for conducting business. The responses from the participants clearly indicate that there is more that policy makers can do, particularly around the following:

(i) Reducing red-tape

Other respondents indicated that regulations by policy-makers do not represent a major stumbling block. It can be concluded based on the analyses performed, that the role of policy-makers is critical. Implementation of policies is also of utmost importance.

4.2.2.2. Discussion pertaining to Question 2

This research question is meant to investigate the challenges relating to financing SMMEs and alternative funding sources, as indicated below. This research question was addressed research questionnaire questions 2 and 5. The responses of the participants are discussed below.

The literature and the outcome of the survey indicate that the current funding models applied by banks need to be refined and to be tailor-made for SMMEs. The literature outlined the lessons that African economies can adopt and use to improve their environment; one such lesson is from India. The responses from the survey are supported by the literature, where some authors like O'Rourke (2006) indicate the importance of micro-financing institutions and their structure. O'Rourke (2006) argues that creating structured partnerships between commercial lending institutions and Micro Financing Institutions (MFI) can provide the best long-term sustainability results and can allow MFIs to flourish as independent and vital parts of developing world systems, without threatening the security and stability of the financial systems supporting these innovations.

The research questionnaire number 5 sought to address an alternative funding model through the Public Private Partnership (PPP) between government and private sector. The responses from the participants indicate that this has worked before in South Africa. They went further to suggest that government should provide incentives to encourage privately run firms, so that they could take on more risks in investing in venture capital, and potentially sharing some risks with government. The respondents also indicated that these PPPs should be run professionally, in order to ensure success.

4.2.2.3. Discussion pertaining to Research Question 3 and its sub-questions: Exit of mature ventures

This research question is meant to investigate the benefits of different exit methods of private placement and IPO for mature ventures. This research question is addressed through questionnaire number 3. The responses of the participants are discussed below.

The literature and the outcome of the survey indicate that the IPO exit method is the most appropriate model, with the following benefit(s):

(i) Transparency

(ii) The creation of capital for use by the new business to be listed or to expand

The respondents also indicated the challenges that exist in African economies, when it comes to this exit method. As there is minimal literature on African economies with regards to IPOs, the author relied on the responses received from the respondents who completed the questionnaire. They indicated that the following reasons are all contributing factors for ventures exited not being taken through to the securities exchange:

(i) Some ventures are small and don't reach levels where they can be exited through securities exchanges.

(ii) Corruption and poor legislation may not be solely to blame for illiquid exchanges. One of the reasons listed was non-capital flows into those regions' securities exchanges.

4.2.2.4. Discussion pertaining to Research Question 3 and its sub-questions: The behaviour and psychology of investing and its impact on venture-backed IPOs

This research question was addressed through research questionnaires numbers 7 and 8. The responses of the participants are discussed below.

Most participants in the survey did not provide any answers relating to these research questionnaires. There are many reasons that could have lead to that, based on the analysis of other questions relating to the IPOs. It can be concluded that lack of quality verifiable data made it difficult for most respondents to provide any answers. Other respondents indicated that the size of the company could have an impact on this. The risk/reward ratio is skewed in favour of defensive investment. Some private business people do not see investing in a business through a stock exchange as a viable option. It takes an appreciation of the value of taking calculated risks, rather than assuming preservative stance. From the responses received, it can be concluded that much research needs to be undertaken in behavioural finance, in relation to venture-backed IPOs.

4.3. Demographic profile of respondents

The respondents to the survey are senior executives and researchers who have extensive knowledge of African markets and economies. They have advised small enterprises and have conducted

extensive research in these markets. Most respondents are based in South Africa, with offices and activities across the whole of the African continent.

TABLE 2: Respondents and their profiles

Number of respondents	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21
Name of respondents	Africa Alliance	Audax Idea	Business Partner (South Africa)	Coronation Fund Managers	Ernst &Young Africa Business Centre	Fund managers who invest in Africa	Future Growth: Responsible Investment	Imara S. P. Reid: Research Division	Invenfin	Jacque Malan Consultants and Actuaries	Kagiso Trust	KPMG Private Equity Practice	Meier	South African Venture Capital Association	Sasfin Bank	Sentinel Mining Retirement Fund	Venture P.Com	SMME Company	KPMG (Malawi)	Old Mutual Equity Funds	Africa Coppernet Zambia
Profile	Senior Economist	Managing Director	Senior Manager		Associate Director	Senior Investment Managers	Senior Investment Manager	Senior Research Analyst	Senior Research Analyst		Chief Finance Officer and Chief Investment Officer	Director	Executive Manager for Investments	Chief Executive Officer	Head of Private Equity	Manager: Investments	Senior Invesment Manager	Chief Executive Officer	Audit and Advisory Partner	Botique Head	Employee benefit specialist
Country of operation and activities	Rest of Africa	Rest of Africa	Rest of Africa	Rest of Africa	Rest of Africa	Rest of Africa	Rest of Africa	Rest of Africa	South Africa	South Africa	Rest of Africa	Rest of Africa	South Africa	South Africa	South Africa	South Africa	South Africa	Africa (Botswana and Swaziland)	Malawi	Africa (Botswana, Egypt, Ghana, Mauritius, Morocco, Nairobi, Namibia, Nigeria, Tunisia)	Zambia

For a conclusive answer regarding venture capital and IPO, all the answers from respondents were analysed and interpreted, and compared to the outcomes in the literature.

4.4. Conclusion

From the outcomes of the survey, an inference of the importance of venture capital can be drawn from the answers provided by the participants. The responses confirm the points raised in Chapters 1 to 3 of the study. The answers also align closely to the literature and confirm those points raised as valid. The most significant points that respondents raised, was the need for:

(i) Tailor-made and innovative funding for SMMEs and most importantly implementation of policies
(ii) Flexible regulations by policy-makers
(iii) Private partnerships between government institutions and the private sector, in making access to finance available to those who need it.

Regarding the appropriate exit method for a venture-backed entity, the respondents indicated that the IPO is the most viable exit method for these ventures versus the private placement method, for the following reasons:

(i) Increases transparency
(ii) It decouples the existence of the current founders/shareholders
(iii) It provides capital for further expansion of the business.

This is despite the current activities of most ventures being exited through a Private Placement platform.

It is concluded that for African economies to thrive and address poverty and unemployment, there should be a solid and stimulating environment for SMMEs. There is a need for finance that is tailor-made for this sector. Governments need to draft laws and regulations that encourage the faster starting up of a business. The conclusion is supported by the extensive literature reviewed, and the analysis of results from the survey.

CHAPTER 5

CONCLUSIONS AND SUGGESTIONS FOR FURTHER RESEARCH

5.1. Introduction

The study outlines the significance of having a venture capital sector, as well as its importance in contributing to the creation of a sustainable SMME environment for African economies. The appropriate research questionnaires were formulated and the answers to those questions were presented in the previous chapter. The outcomes of the survey were compared with the extensive literature relating to venture capital and IPOs.

The following section lists the important points from the study and links them to the literature review and the outcome of the survey. Finally, suggestions for further research based on the lessons learned from the literature review and the outcomes of the survey, are made.

The responses from the survey also highlight the most common impediment to the creation and sustainability of new ventures, this being "proper access to financing and making finance work for Africa".[15]

5.2. Conclusions of the study

Taking into consideration the literature reviewed and the important points introduced, it is clear that for the economic development of African economies, a vibrant venture capital sector is critical.

The literature reviewed in chapter 3 outlines important facts pertaining to venture capital finance and IPOs. It also contains guidelines on how the challenges, (i.e. access to appropriate form of financing and the regulations that are not suitable for starting up a new enterprise) faced by venture capitalists, policy makers and private financiers can be addressed. It is also clear that for any economy to thrive; create employment and combat poverty, whilst contributing positively to the economic growth of each economy, the creation of new ventures is important.

The current economic environment in African economies needs to improve if the venture capital sector is to thrive. The lack of relevant and appropriate legislation hampers the rapid establishment of new enterprises. The inadequate form of financing for these enterprises remains one of the

[15] Patrick, and Thorsten, Beck (2007): World Bank: ***Making Finance Work for Africa.***

greatest challenges that need to be addressed. However, there is an emerging trend of government trying to assist the SMME sector. The announcement by the Zambian government about creating a new venture fund aimed at addressing this specific problem is encouraging.

The study also discussed at great length the exit of these venture when they mature. It is clear that the exit of mature ventures through an IPO, is the most viable and profitable method for venture capitalists to exit their investments. For the venture capital industry to flourish and operate at an optimal level, African economies need to create an environment that encourages this exit method, starting with properly functioning securities exchanges. Investor education as pointed out by a respondent from Imara. S.P. Reid as one of the most important factor, an example was made of securities exchanges like TSX and LSM AIM that they are far ahead in terms in terms of investor education.. African countries like Botswana and Zimbabwe need to create a securities exchange for the trading of corporate debt and other financial instruments that might aid in availing financing to start-up enterprises.

Some might argue that this is all premature for African economies. This is considering that there are still challenges of access to finance, and inadequate legislation in place - those needs have to be addressed first. However, the empirical evidence from the literature suggests that taking mature enterprises to securities exchanges, is more beneficial in the long run for the entrepreneur and the investors or venture capitalists.

The existing literature is derived mainly from developed markets and this study seeks to add to the studies already conducted on the African continent (e.g. Ojah, 2009). This would be by providing guidance for African economies on how to address the challenges being faced by SMMEs, and by creating a stimulating environment for this sector in order for it to ultimately contribute to the GDP of each African economy.

In order to address the challenges of inadequate form of financing for new enterprises being created, the African governments need to adopt and implement the following financing methods which have worked successfully in other countries:

The literature reviewed provided us with some lessons that African economies can adopt and use to improve their environment; one such lesson is from India. Other authors like O'Rourke (2006) indicate the importance of micro-financing institutions and their structure. O'Rourke (2006) argues that creating structured partnerships between commercial lending institutions and Micro Financing

Institutions (MFI) can provide the best long-term sustainability results and can allow MFIs to flourish as independent and vital parts of developing world systems, without threatening the security and stability of the financial systems supporting these innovations.

The other alternative funding model is through the Public Private Partnership (PPP) between government and private sector. There are currently many government agencies like Khula and SEDA. The challenges with these institutions are that they also use the traditional form of credit review when offering financing to start up entities. These institutions can partner with private and commercial banks where they equally share the risks. The government can offers a guarantee for any funding being given to a start-up entity as a form of insurance.

5.3. Suggestions for further research

From the impediments identified and outlined in the first chapter and the research questions formulated, the literature reviewed and lessons learned from the review, the survey's outcome clearly indicates the importance of the SMME sector. The points highlighted in the literature review around the challenges identified and how to address them are fully supported by the responses from the participants.

The exit method remains a challenge as most respondents agreed that the IPO is the most appropriate and sustainable exit platform. However, most of the exit of these ventures takes place through a private placement method between two investors. Various number of reasons were provided for this practice such as, the listing costs in the securities exchange are prohibitive (i.e. it is extremely expensive to list an entity), and that some of the securities exchanges are illiquid.

The other question that was not well answered by the respondents is the impact, psychology of investing plays in most ventures being exited through a private placement exit platform. The author is of the view that, this area needs to be researched further. The best form of data to provide us with empirical evidence would be qualitative data. Obtaining this form of data has proved to be extremely difficult. The risk/reward ratio is skewed in favour of defensive investment. Some private business people do not see investing in a business through a stock exchange as a viable option. It takes an appreciation of the value of taking calculated risks, rather than assuming preservative stance. From the responses received, it can be concluded that much research needs to be undertaken in behavioural finance, in relation to venture-backed IPOs.

However, it is clear that there is still scope for extensive and in-depth research on the topic of venture capital in African economies. Thus further studies or research on the subject are

recommended. This research should focus on the financing for these ventures and how to make financing easily accessible to them.

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APPENDIX A

The research questionnaire is divided into two sections:

(i) closed form questions

(ii) Open-ended questions

Note: Where the question does not lend itself to a yes/no responses, please skip indicating true/false as a response.

Number	Research questions	Yes	No	Provide more information for your answer
1.	Do current business regulations in African economies allow for the faster establishment of a business?			
2.	Are the funding models currently being applied by banks (i.e. credit history or earnings track record) appropriate in addressing the challenges faced by start-up enterprises?			
3.	Will the current state of African economies' security exchanges (i.e. illiquid and hampered by corruption, weak legislation and gross inadequacy of infrastructure) contribute to the low levels of venture capital finance-backed IPOs?			
4.	Do the policy makers in African economies have a critical role to play in creating a stimulating environment for venture capital finance-backed initiatives?			
5.	Would a Public Private Partnership (PPP) between government and private sector financiers, to create a specific new venture creation fund for start up enterprises, be beneficial?			
6.	Would the creation of a financial institution (i.e. new venture creation bank), that is specifically focused on providing financing that is tailor-made for start-up enterprises, be beneficial?			
7.	Does the behaviour and psychology of investing have any impact/contribute to the low levels of venture-backed IPOs?			
8.	Does the behaviour and psychology of investing have anything to do with the private placement exit method of ventures?			
9.	Is the Initial Public Offering (IPO) through a securities exchange a viable investment exit strategy for investors in Africa's markets?			
10.	What do the policy-makers in African economies need to do to create an economic environment that encourages entrepreneurship?			

Note:

For every answer, please provide reason(s) and where available data, to support your answer(s).
Private Placement: Private placement is defined as a private sale between two entrepreneurs

Behaviour and Psychology of Investing: Behavioural finance is the study of the influence of psychology on the behaviour of financial practitioners and the subsequent effect on markets. Behavioural finance helps explain why and how markets might be inefficient.

APPENDIX B

GLOSSARY OF TERMS

Behaviour and Psychology of Investing	Behavioural finance is the study of the influence of psychology on the behaviour of financial practitioners and the subsequent effect on markets. Behavioural finance helps explain why and how markets might be inefficient.
Credit Default Risk	An investor's risk of loss arising from a borrower who does not make payments as promised. Such an event is called a default. Investor losses include lost principal and interest, decreased cash flow, and increased collection costs
Convertible Securities	Type of bond that the holder can convert into shares of common stock in the issuing company, or cash of equal value, at an agreed-upon price
DBSA	Development Bank of South Africa
DBZ	Development Bank of Zambia
EYVBI	Ernst & Young Venture Capital Backed Index
FTSE-MIB	Borsa Italiana (FTSE MIB) Latvia: Riga Stock Exchange (part of OMX) Lithuania: Vilnius Stock Exchange (part of OMX)
GDP	Gross Domestic Product
Macro-economic environment	While micro-economics deals with the operations of individual firms and markets, macro-economics examines how numerous markets interact with the government and each other in the regional, national, and sometimes international realms.

MFI	Micro Financing Institutions
Initial Public Offerings	An initial public offering (IPO), referred to simply as an "offering" or "flotation", is when a company (called the issuer) issues common stock or shares to the public for the first time. They are often issued by smaller, younger companies seeking capital to expand, but can also be done by large privately-owned companies looking to become publicly traded.
Liquidity constraints	A liquidity constraint is an arbitrary limit on the amount an individual can borrow, or an arbitrary alteration in the interest rate they pay. By raising the costs of borrowing, they prevent individuals from fully optimising their behaviour over time.
Venture Capital	Financial capital provided to early-stage, high growth potential, start-up companies. Venture capital Seed capital. Start-up and early stage. Funding for research, evaluation and development of a concept or business, before the business starts trading. Funding for new companies being set up or for the development of those which have been in business for a short time (one to three years).
Private Equity	Private equity, in finance, is an asset class consisting of equity securities in operating companies that are not publicly traded on a stock exchange.
Private Placement	Private placement is defined as a private sale between two entrepreneurs.
SMME	Small Micro and Medium Enterprises.
Securities Market	An economic institute in which sale and purchase transactions of securities between subjects of economy on the base of demand and supply,

	take place. A securities market is also a system of interconnection between all participants (professional and non-professional) that provides effective conditions: (i) to buy and sell securities (ii) to attract new capital by means of issuance of new security (securitisation of debt) (iii) to transfer real assets into financial assets (iv) to invest money for short- or long-term periods, with the aim of deriving profit.
ZDA	Zambian Development Agency