Funding Strategies for Rapid Growth Businesses in South Africa at Different Stages of Development

A research report submitted to the Wits Business School in partial fulfilment of the requirements for the degree

of

Master of Business Administration

by

Keith Govender

Student number: 416562

Tel: 082 714 9122

February 2012 ***Supervised by: Dr. Kerrin Myres***

ABSTRACT

This dissertation seeks to understand the funding strategies adopted by South African businesses to enable rapid rates of growth. The importance of business growth to the development of the South African economy, as well as job creation, is frequently cited in the literature. The ability of a business to grow rapidly and develop to a sustainable level of maturity is therefore highly attractive for all stakeholders involved. However, there does not appear to be much focus in identifying which factors, both internal and external, will enable businesses to successfully manage this growth. This research serves to uncover the key issues where this gap exists.

Nine rapid growth South African businesses across different stages of development were interviewed to gain insight into the challenges faced by rapid growth businesses from a funding perspective as well as to determine the tactics and strategies employed that have enabled them to survive in a rapid growth environment. A qualitative research approach, underpinned by an interpretive research paradigm, was adopted as it was believed that the researcher could best understand the meaning that the businesses ascribed to the issue of funding rapid growth by conducting face-to-face interviews.

The study has produced interesting findings on the strategic orientation of rapid growth businesses and their approach to funding. It has emerged that funding of many businesses appear to be more of a reactive process than the formulation and development of a well researched strategy. Bootstrapping, which is commonly associated with start-ups and early stage businesses, was found to be employed by some of the larger companies in this study. The rapid growth businesses also employ a variety of tactics to leverage their sources of funding or to avoid external sources of funding.

The research is of particular importance within the South African context as the country has been characterised by an alarmingly high failure rate of small businesses. The implications of the findings will be useful for external stakeholders such as government, policy-makers and investors as well as for the management of current and potential rapid growth businesses who can take the necessary steps to ensure that they have geared themselves as effectively as possible for a rapid increase in growth.

DECLARATION

I declare that this research report is my own work. It is submitted in partial fulfilment of the requirements for the degree of Master of Business Administration at Wits Business School. It has not been submitted before for any degree or examination in any other university. I further declare that I have obtained the necessary authorization and consent to carry out this research.

Keith Govender

DEDICATION

To my parents: Teddy and Visalatchee Govender

You have instilled in my siblings and me the importance of gaining a sound education and have constantly motivated us to strive for the best results in any journey we embark on. I have learnt, from an early age, that the only obstacle to success is one's own mind.

You have provided and guided us towards the opportunities that were not available to you both growing up and have selflessly given of your time and energy to ensure we could get the best education that you were able to provide.

I am grateful for your love, encouragement and support.

ACKNOWLEDGEMENTS

Through my academic endeavours I have sought to expand my knowledge base and grow my intelligence. However, I have learnt that one's intelligence and mind must always be balanced and guided by a sound intellect. I am deeply grateful for my dear friend, Vivashan Muthan, who constantly provides me with the tools to develop my intellect and who is always there to remind me to "stay in the light".

Going back to school provided me with the opportunity not only to build a network but to find real friendship and to develop a brotherhood. I have built relationships that will last a lifetime. The late evening lectures for two years would not have been bearable without the rapport that I developed with my classmates.

It was very pleasing and encouraging to see how willing the management and owners of the businesses targeted for this study were to assist a young man with his research. Despite their busy schedules they went out of their way to accommodate me and offer their insights. I left each and every interview feeling deeply inspired. I extend my deepest gratitude to each of them.

My supervisor provided me with a sense of calm from day one when I ran into her office, without an appointment, panic-stricken. Thank you for your kind demeanour, ongoing support and guidance.

I would like to thank my employer, Shell, for funding a large portion of my study fees and your willingness to support the development of your employees.

Lastly, I would like to thank my partner, Zeidah, for accommodating a mistress in the form of this research report with whom I have spent many hours with. Your understanding and support has enabled me to dedicate a lot of time, in the final hours, to ensure I delivered a solid piece of work.

TABLE OF CONTENTS

LIST OF TABLES

LIST OF FIGURES

1 INTRODUCTION

1.1 Purpose of the study

The purpose of the study is to identify the various funding strategies adopted by rapid growth businesses in South Africa. The report will provide insight for business owners anticipating rapid growth at the various stages within the business growth cycle. The report will also help policymakers, funders and support agencies understand some of the specific requirements of businesses at various stages of development.

1.2 Context of the study

South Africa is an emerging economy which was characterised by its political and economic isolation during the Apartheid era. The first democratic government of South Africa, inaugurated in 1994, inherited an economy in crisis but through rapid interventions at the level of macroeconomic policy, government set the country on a path to sustainable growth (Dobson 2002) .However, inherent problems still remain. The unacceptably high unemployment rate sits at the forefront of these problems. It has been argued that high unemployment may be attributed to slow economic growth as well as relatively low labour-intensity of economic growth (van der Berg 1989).

The small business sector in South Africa has the potential to make a positive contribution to job creation while contributing to economic growth (Luiz 2002; Dennis Jr. 2011; Carland, Hoy, Boulton and Carland 1984; Naude 2010). For the small business sector to make a meaningful contribution to the economy, it would need to be integrated into the mainstream economy which would require strong support from both government and the private sector (Luiz 2002).

Government is aware of the role that the small business sector plays in the development of the South African economy and a number of policies, legislations and acts have been put in place to support this sector. In the 2007 Budget Speech, Minister of Finance, Trevor Manuel stated: “Entrepreneurship remains a vital ingredient in the growth of our economy” (Manuel 2007).

While entrepreneurship is a vital ingredient, perhaps, not all entrepreneurial activity make substantial contributions to economic growth. This could explain why the importance of high and rapid growth entrepreneurial activity for job creation is commonly cited. Rapid growth firms (often defined as those with a sales growth rate of at least 20% per year for five consecutive years), in particular, have attracted growing interest from the public sector and have been argued to make a disproportionate contribution to the creation of jobs (Fischer and Reuber 2003). It is critical that these small businesses grow to become large organisations so that they can create sustainable job opportunities. Finance remains a critical challenge for business growth and this challenge is exacerbated within a rapid growth environment (Asah and Fatoki 2011). Combined with a lack of business acumen within the small business sector the result is numerous business failures along with inefficiently run enterprises with questionable sustainability (Asah and Fatoki 2011).

The challenge for South African businesses, therefore, lies not only on focusing on innovation as a means to facilitate more labour intensive growth but also in developing business competencies and strategies to build successful and sustainable enterprises. Organisation’s that have not geared themselves for rapid growth quickly find themselves struggling to keep afloat which ultimately leads to their demise.

Success within the small to medium business sector will yield significant benefits for the South African economy as a whole. The opportunity exists to guide players within this sector to realise their full potential and make significant leaps towards the microeconomic reform of the country.

1.3 Problem statement

1.3.1 *Main problem*

Identify the funding strategies adopted by rapid growth businesses in South Africa at the different stages of development and the reasons underpinning the strategic choices.

1.3.2 *Sub-problems*

The first sub-problem is to identify the funding requirements of rapid growth businesses in South Africa at the various stages of development.

The second sub-problem is to identify the sources of funding used by these businesses to meet their funding requirements.

The third sub-problem is to identify the impact of rapid growth on the business and the associated financial implications.

The fourth sub-problem is to identify the challenges faced by these rapid-growth businesses in attempting to secure funding.

The fifth sub-problem is to identify the consequences businesses being unable to secure the desired sources of funding and the subsequent impact on operations.

The sixth sub-problem is to identify the funding strategies adopted by rapid growth businesses and the tactics employed to leverage sources of funding.

1.4 Significance of the study

The study fills a gap in that there is currently not much research available to provide business guidance for Small to Medium Sized Enterprises (SMEs) within South Africa. There is little or no research that specifically addresses funding strategies for SMEs within a rapid growth environment. This study seeks to identify the various stages of growth of SMEs and the associated funding requirements as well as synthesise some of the effective funding strategies used to enable high growth rates.

The study provides guidance to entrepreneurs and managers of local South African businesses who wish to identify the challenges faced by rapid growth organisations as they transition through the various stages of growth and gain insight to the various funding strategies that could be employed. Insight into how small businesses change during growth and expand beyond SME size has the potential to provide useful guidance for organisational planning (Chan, Bhargava and Street 2006). The financing patterns of local businesses also become an important issue in terms of policy and resource support implications (Datta 2010).

1.5 Delimitations of the study

- The study will take a cross-sectional view of the entire market and will not be biased towards any specific sector.
- Only rapid growth enterprises as defined in this document will be analysed.
- Micro-enterprises, which represent the lowest level of businesses (typically self-employed within the informal sector) will not be included as part of the study.
- Large corporations and multinationals will not be included in this study.
- Only businesses in the Gauteng region will be assessed.

1.6 Definition of terms

- Agency risk – *the risk that results from divergent interests of venture capitalists and the entrepreneurs running the firm.*
- Business risk – *the risk related to the success of a product or service in the market .*
- Collateral – *assets that are pledged as security for payment of debt.*
- Decentralisation – *the dispersing of decision-making power closer to people at lower levels of the organisation.*
- Enterprise Architecture – *a coherent and consistent set of principles and standards that guides enterprise design.*
- Financial distress – *when financial obligations of a company are honoured with difficulty.*
- Informational asymmetry – *refers to a situation where one party has more information than the other.*
- Letter of credit - *is a mechanism that enables the buyer to take product on terms.*
- Nascent – *An adult who has, during the past 12 months, taken tangible action to start a new business; would personally own all or part of the business; would actively participate in the day-to-day management of the business; and has not yet paid salaries in the last three months.*

- Rapid growth - *companies showing a year-on-year growth rate of 20% for five consecutive years.*
- Risk Capital – *refers to funds used for high-risk, high-reward investments.*
- SME – *Small to Medium-sized Enterprises which include a very broad range of firms from the established business employing over a hundred people down to the self employed, survivalist business.*

1.7 Assumptions

The following assumptions have been made regarding the study:

- The respondents are open to sharing information regarding the operation and strategies of their business.
- The respondents are able to accurately articulate their strategies and synthesize the challenges relating to growth.
- The total number of respondents is sufficient to gain adequate data.
- One person's view of the world can be linked and compared to that of another.

2 LITERATURE REVIEW

2.1 Introduction

This literature review addresses some of the key themes that are relevant to this research. The first section provides some background on small businesses and the role of entrepreneurship within this environment. The following sections look at the businesses challenges and changing funding requirements as the business transgresses the various stages of growth; the sources of funding available to businesses; the characteristics of rapid growth and the associated funding requirements; the challenges faced by small businesses in attempting to secure funding; and funding strategies that business may adopt and the tactics employed to leverage sources of funding.

2.2 Background discussion

2.2.1 *Small business and growth*

Carland et al (1984) define a small business as one which is independently owned and operated and which is not dominant within its field of operation. The small business environment may be further classified by four categories: micro, which includes the survivalist enterprises; very small; small; and medium (Luiz 2002). Almost any literature on the subject of small businesses highlights its importance and potential to contribute to job creation and growth. The small business sector is thus a vital ingredient for economic development in developing countries, such as South Africa. Despite the noted contribution of new Small to Medium-sized Enterprises (SMEs), the creation rate of new SMEs in South Africa is amongst the lowest in the world implying that the probability of a new SME surviving beyond 42 months to become an established firm is less likely in

South Africa than in any country sampled by the Global Entrepreneurship Monitor (Olawale and Smit 2010).

Also, not all small businesses play a significant role in terms of economic development. It is argued that the entrepreneurial portion of the small business environment plays a disproportionate role in economic development (Carland et al 1984; Naude 2010). What exactly then defines an entrepreneurial venture and how does it differ from a typical small business?

Autio (2007) defines entrepreneurship as “any attempt by individuals to start a new firm, including any attempt for self-employment.” The literature reviewed, however, contrasts the entrepreneur from just any start-up or business attempt. The entrepreneur appears to be one who specifically intends to grow his or hers business utilising strategic management as a method to facilitate and enhance growth and profit-making (Carland et al 1984; Naude 2010; Chan et al 2006; Gundry and Welsch 2001). So the strategic nature, it seems, is one of the key characteristics of the entrepreneurial venture. Carland et al (1984) supports the notion that the entrepreneurial venture may be identified by the strategic behaviour of such firms and suggests that five categories of behaviour are characteristic of these ventures: introduction of new goods, introduction of new methods of production, opening of new markets, opening of new sources of supply and industrial reorganisation.

Entrepreneurs also have the ability to spot profitable opportunities and re-allocate resources (Naude 2010). The entrepreneur is characterised by a preference for creativity, manifested by new combinations of organizational activity, indicating innovative behaviour (Carland et al 1984).

Rapid growth entrepreneurs may be differentiated along several dimensions: they are likely to select strategies that emphasise market growth and technological change; stronger commitment to the success of the business; greater willingness to incur opportunity costs for the success of their firms; utilisation of team-based forms of organisation design; concern for reputation and quality; strong leadership and use of a wider range of financing sources for the expansion of the venture (Gundry and Welsch, 2001).

The rapid growth nature of these ventures thus ensures that the stakeholder list extends beyond those that are interested in economic development and job creation. Stakeholders may be identified as investors who show interest for high returns; other managers who want to beat competitors; governments who recognize entrepreneurship and innovation to be important engines of economic growth around the world (Foster and Davilla 2010).

The growth-orientation of entrepreneurial ventures is an important point within the context of this study as this research is based on rapid growth businesses. While small firms may grow, many of them will remain small businesses. Distinguishing entrepreneurial ventures within this sector will help identify "true" growth enterprises.

2.2.2 *Need for funding*

The most critical resource for the development and ongoing success of a business is funding. Funding is required by businesses to start and expand operations, develop new products, invest in new staff or production facilities (Asah and Fatoki 2011). Start-up capital is essential to establish the business during the early phases and quite often requires serious investment, particularly in a manufacturing type environment. To sustain the operations of the business and to maintain cash flows working capital is needed which may require the business to secure funding. Finance, be it internal or external is the lifeblood of the organisation and is a key factor that promotes failure or success of the organisation.

Growth requires funding and to fully capitalise on market opportunities, organisations must ensure they create reliable avenues of funding. Funding may be required to service the growth of the organisation from a capital perspective or to manage the instability of working capital that growth can create. This is especially important in a rapid growth environment. High levels of funding are required for rapid growth (Gundry and Welsch 2001).

2.3 Funding requirements at different stages of business growth

This section will look in more detail at the critical stages of business growth along with the operational challenges faced by the business, funding requirements and management strategies adopted by companies to sustain growth.

2.3.1 *Homogeneity of growth*

The dominant view within the area of business growth is that successful firms are more different than similar to each other implying that there is no golden template that may be used to guarantee a path to sustainable rapid growth (Chan et al 2006). However, there is a conflicting view of sustainable rapid growth that argues that successful small businesses are actually quite homogeneous in style and strategy and that there is a small set of distinguishing characteristics to which sustainable rapid growth may be attributed to (Chan et al 2006). The study conducted by Chan et al (2006) provides support for the homogeneity theory of small firms which sustain rapid growth by demonstrating that reported small business management challenges did not significantly vary across common organisational characteristics. Some of the findings are listed below:

- Leadership challenges decreased as the companies increased in size; attributed to owner/managers moving further from the daily operations of the business
- Changes in leadership style during business growth is a requisite for a business to succeed
- External environment challenges changed as the companies increased in size

This is by no means a conclusive list but it does highlight an important finding in the existence of some homogeneity which could be very useful for businesses that seek to understand and develop characteristics that have enabled other small businesses to sustain rapid growth. This is an opportunity for further research.

2.3.2 *Stages of growth and growth models*

As businesses grow, it is postulated that they pass through various stages and must overcome certain hurdles and obstacles to endure and continue to grow. Business growth models are a form of process model that depicts the growth of the business as a progression through identifiable stages (Chan et al 2006). These growth models typically comprise three to six phases and have distinct stages that follow a sequential pattern. These growth models generally assume that an evolutionary process stimulates movement through the various stages (Chan et al 2006).

Due to the different characteristics of each stage of growth, a crisis accompanies the transition through the various stages (Scott and Bruce 1987). If the entrepreneur is successful in dealing with the crisis, his next challenge would be to manage the "new" organisation. As a result, change management becomes a key component enabling the business to sustain growth. This crisis theory also, by implication, suggests that the business has the potential to fail as it tries to transition each stage. In their paper “Five stages of growth in small business” Scott and Bruce (1987) depict the Greiner model which highlights the five growth stages and the corresponding crises.

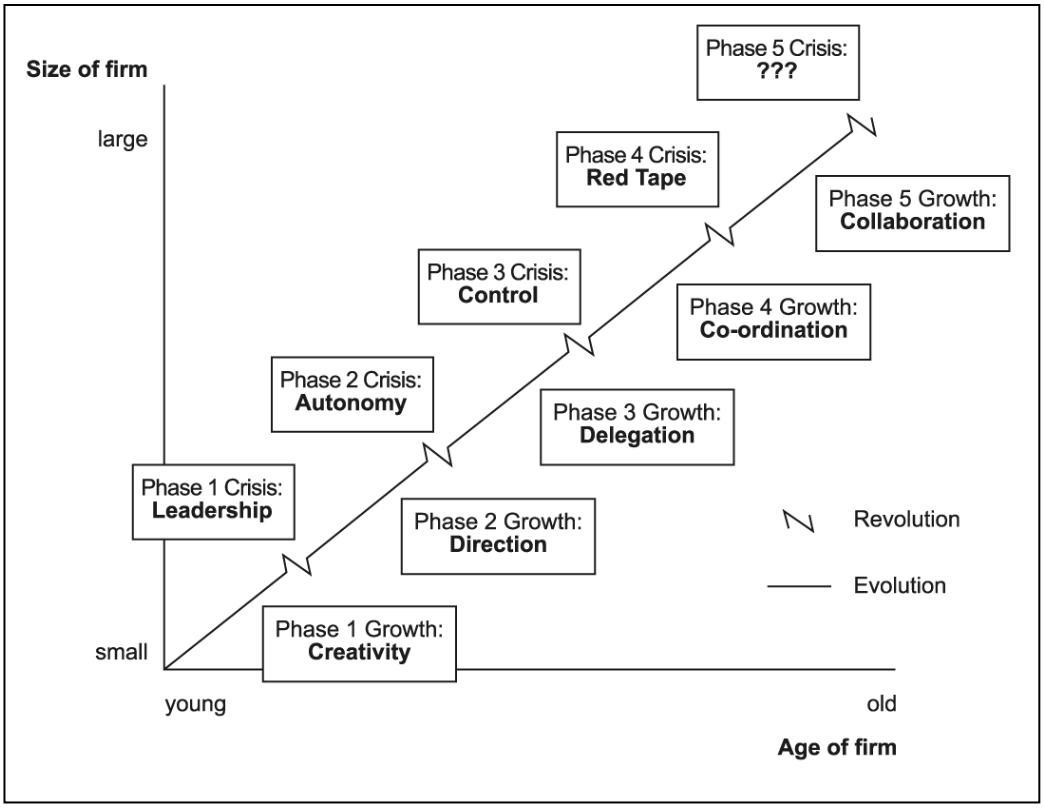


Figure 1: Greiner Stages of growth model (Scott and Bruce 1987)

The following paragraphs summarises the basic features and crises across the various stages of growth as described by Scott and Bruce (1987).

Stage 1: Inception

During this initial phase the business tends to operate one-dimensionally. The business is usually characterised by a single operating unit typically operating in a single market with limited distribution channels. Processes are usually informal and planning is low or non-existent. Funding requirements are of a capital nature required to set up the organisation. As the business transitions to the next phase there is a shift from establishing itself to a mindset of profitability and loss minimisation. Working capital starts becoming a more important funding requirement and management of cash conversion cycles are key from the outset. The push for profits and the increase in business activity will require some formal systems and processes. The increased business activity will also place significant demands on the manager's time and a change in management style will be necessary. If the owners successfully meet the demands of time, energy and finance that the business requires, they become stage 2 enterprises.

Stage 2: Survival

As the business expands working capital becomes central to the financial challenge. Owner's equity may no longer be a viable means of finance and a broader range of financial support would need to be investigated and employed. The business at this stage would still typically maintain a limited product line with growth being driven by market expansion. Overtrading is a challenge and can be the source of a crisis at this stage and the business must therefore ensure that it controls growth moving forward. The drive to increase sales inevitably requires a growth in the customer base which has implications for the distribution channel. The business would need to adopt a more complex distribution network and this would necessitate structural changes within the organisation. Management of change once again becomes central to the growth realm. The business will encounter increased levels of competition at this stage and this will affect the marketing dimension of the business. This added dimension increases business complexity and will also have financial implications from a product price perspective. The business will have to evolve and expand the breadth of its management structure.

All the potential crises mentioned above have an impact on the increase in information management within the organisation. Information systems will need to be employed for control purposes and the organisational structure will have to widen further as the need for full time financial management becomes clear. The management style will have to continue to adapt and evolve and has the potential to threaten the existing power base.

Stage 3: Growth

The business should be profitable at this stage but cash will continue to be thrown back into the business to fund growth. The majority of time will be spent coordinating activities of the functional managers and a formal organisational structure would have to be in place. Systems, processes and financial controls should be in place as the organisation takes on a more professional style. Once again overtrading could pose a risk and liquidity could pose a major problem. If opportunities exist for new products or markets, the business could see itself moving into the next stage.

The most likely crises at this stage may come from the entry of large competitors and the demands of expansion into new markets or products. Large firms entering the market have the benefit of economies of scale which they use to their advantage. The pressure on price thus increases. The small business thus has the option to forfeit market share and use differentiation as a strategy. This exchange of volume for margin results in the business remaining in stage 3. If the business opts to play the volume game, expansion into new products and markets are required. Managerial and financial resources will continue to be stretched and control of growth will remain a key challenge. Internal funding may not be enough to finance the growth and increased levels of external funding in the form of longer term debt will have to be considered. The management style will once again change to cope with the evolving organisation. A degree of decentralisation may be required and the manager will need to relinquish some power if the business is to continue to grow.

Stage 4: Expansion

The basic features of this stage include budgetary control, regular management reports, formalised accounting systems and decentralised authority. Systemisation of most administrative functions will be fundamental through this stage. Securing long-term debt becomes essential at this stage despite retained earnings still being used as a major source of finance. As the breadth of the business is significantly larger and with managers lacking the same emotional attachment to the business as those during the start-up phase, politics within the organisation start to emerge and could be a source of a crisis. The most likely crisis, however, would occur as a result of the founder manager becoming increasingly more distant from the action. This occurs naturally as the organisation grows and decentralisation becomes further entrenched. The other crisis to avoid is that of competition. As the industry matures and consolidates, competition becomes intense and the need for a strong source of competitive advantage becomes vital. External focus must become a key behavioural imperative of the organisation.

Stage 5: Maturity

It is important to note that even at the maturity stage the business is still growing. Most are companies on the verge of moving away from being a small business. Expense control, productivity and growth opportunities are the key issues facing management. Major investments within the areas of marketing and plant upgrading and maintenance would be required. Firms can opt to remain at this stage, shrink operations or go on to become a large corporation.

Alternative view to Stages of Growth Models

Levie and Lichtenstein (2010) propose an alternative model to the numerous stages of growth models that have appeared in much management literature and text books. The authors have found that there has been no agreement about stages model features and that principle propositions shared by these models appear to have no empirical validity when tested with large samples. The alternative approach that they propose – the dynamic states approach – replaces two major assumptions of the stages theory while retaining the most intuitive and accurate propositions.

The central assumption of the stages of growth paradigm is that businesses grow as if they are developing organisms. The propositions arising out of this assumption is that just as in a growing organism; the organisation will pass through distinctively different stages; the sequence and order of these recognisable stages is predetermined and thus predictable; all organisations develop according to prefigured rules that progress from a latent state to a more mature and differentiated state (Levie and Lichtenstein 2010). This central assumption is the primary reason for ongoing criticism of stages of growth models as all enterprises don't pass through all the stages in a specific sequence (Jacobs, Kotze, van der Merwe and Gerber 2011). It is not easy to extract a coherent picture of the distinct stages of SME growth but the inherent complexity of the phenomenon is at least acknowledged (Jacobs et al 2011)

The dynamic states approach that Levie and Lichtenstein (2010) propose replaces the propositions, that businesses develop through a specific number of stages and that these stages represent an imminent program of development, with foundations from complexity science. According to Levie and Lichtenstein (2010), dynamic states are open, complex adaptive systems that operate in disequilibrium conditions. The dynamic states approach assumes that it is most probable that the organisation will grow in a series of configurations and differs from the old stages theory in that there can be any number of dynamic states in an organisation's existence which can occur in any number of sequences. This occurs as a result of the dynamic states approach aim to reflect an optimal relationship between the firm's business model and its environment with both sides of the equation having the potential to change infinitely.

While Levie and Lichtenstein (2010) have argued that the traditional stages models should be discarded by entrepreneurial scholars they agree that an element of stages theory that is empirically true is that businesses tend to operate in some definable state for some period of time. Jacobs et al (2011) have explored the use of Enterprise Architecture (EA) to enhance existing stages of growth models so as to provide guidance to SME managers as their businesses transforms from being a small to medium size business. A model such as the Greiner model would therefore still be appropriate for categorizing businesses for the purpose of this study.

2.3.1 *Research Question 1*

What are the funding requirements of rapid growth South African businesses at the various stages of development?

2.4 Sources of funding

This section addresses the various forms of finance available to businesses as they develop and grow.

Enterprises from countries with marketing economies can acquire funding resources though the use of internal financing, or self-financing, whereby financial resources are provided from the firms outcomes; or funding resources may be obtained from outside of the enterprise (Diana 2010). Having a lower cost than the average cost of capital for a business, Diana (2010) highlights internal financing as the most effective solution to cover ongoing capital needs. A vast majority of South African SMEs depend on internal finance to survive and grow. This, however, is often inadequate especially in a high growth environment (Asah and Fatoki 2011, Diana 2010). The first place businesses usually turn to are the banks. This would explain why banks are considered to be the most important enabler of financial transactions in most economies (Ackermann and Meyer 2007). Banks may provide businesses with funding in the form of short-term or long-term debt.

Risk capital or Private Equity (PE) refers to external equity financing of entrepreneurial businesses and consists of both the formal venture capital and informal venture capital (Collewaert et al 2010). The money given to the entrepreneur, or established company, in exchange for shares in the business requires no interest payments with the PE financier expecting their return to come purely from the appreciation of capital invested in the business (James 2010).

Very new businesses may actually get their initial funding from family and friends (James 2010). The stage of PE funding after the funding by family and friends is known as “angel” investing (James 2010). Angel investors refer to high-net-worth individuals who invest their time and money to assist start-up companies to overcome the inertia associated with the early stages of growth (Markova and Petkovska-Mircevska 2010). In the United States of America (USA), angel investors supply more capital to early-stage companies than venture capital firms do (Markova and Petkovska-Mircevska 2010). Angels may not have the capability to conduct in-depth due diligence, understand all aspects of the venture they are evaluating, or have the negotiating leverage to set ideal valuations and terms and conditions, however, they play a vital role in filling the gap, below the threshold at which venture capital firms would invest, in terms of funding entrepreneurial ventures (Markova and Petkovska-Mircevska 2010).

Table 1: Investment needs at different stages of the start-up venture lifecycle (Markova and Petkovska-Mircevska 2010)

Stage	Seed	Start-up	Funding Gap	Early Venture Stage	Later Venture Stage
Source	Founder Friends Family	Idividual Angels	Angel Organisations	Venture Funds	
Amount Invested	$25,000 to $100,000	$100,000 to $500,000	$500,000 to $2,000,000 +	$2,000,000 to $5,000,000 +	

The South African government through its Department of Trade and Industry (DTI) has implemented support programs for SMEs which has been supported by the National Small Business Council (NSBC), the Centre for Small Business Promotion (CSBP), Ntsika Enterprise Promotion Agency and Khula Enterprises (Rogerson 2001). These institutions, collectively, provide wholesale financial and non-financial support to SMEs through retail service providers. The interim review findings of the first five years of the SME support program in South Africa highlighted that the program suffers from institutional underperformance and policy weakness. This has resulted in the knowledge of these programs not being communicated effectively to potential beneficiaries and adequate and improved access to finance by SMEs has not been ensured (Rogerson 2001, Ray 2010).

Funding may come from a variety of sources which can more broadly be categorised as formal or informal in nature. Formal sources of finance include those that one would typically secure from a bank through formal processes. Informal finance can be described as financing that occurs outside the regulations of the formal banking and financial sectors (Aryeetey and Udry 1995). The table below highlights the more common of these formal and informal sources of finance.

Table 2: Informal vs. Formal sources of Finance (own compilation)

Informal	Formal
Personal Savings	Long term loans from banks or other financial institutes
Personal loans: family members, friends, employers or colleagues	Credit card loans
Money lenders	Personal loan from a financial institute
Additional team equity	Asset-backed loan such as second mortgage
Venture capital	Overdraught facilities
Private equity investors (angel financing)	
Local/municipal revolving loan programs	

The demand for collateral, delay in loan processing and the generally blasé approach of banks in granting of loans often prompts borrowers to rely on the informal sector for credit and as a result the formal and informal loan markets co-exist for small business finance (Datta 2010). Credit from moneylenders within the informal sector, typically, is the most expensive form of finance but will be used by the business that needs quick access to funding and cannot afford to deal with bureaucracy of attaining a more formal loan.

The informal lending sector would often not rely on formal contracts but rather on relational contracts and will lend on the basis of a past reputation in conjunction with the overall financial solvency of the borrowers (Datta 2010). Financial development has been found to be associated with faster growth and there is a dominant view that informal financial institutions play a complementary role to the formal financial system by servicing the lower end of the market (Ayyagari, Demirguc-Kunt and Maksimovic 2010).

2.4.1 *Research Question 2*

What are the sources of funding adopted by rapid growth South African businesses?

2.5 Funding requirements associated with rapid growth

2.5.1 *Rapid growth and its characteristics*

Quite often, high and rapid growth are used interchangeably. Siegel, Siegel and Macmillan (1993), and Fischer and Reuber (2003), respectively, view high and rapid growth in terms of year-on-year revenue growth. According to Siegel et al (1993), rapid growth was defined as the doubling of sales over the three most recent years that the firm had been in operation. This equates to a sustained annual growth rate of 25% for three consecutive years. According to Fischer and Reuber (2003) rapid growth firms were defined as those sustaining a sales growth of at least 20% for five consecutive years.

Revenue was not only the basis used to define rate of growth of organisations. Naude (2010) defined rapid growth firms as firms that achieve average employment growth in excess of 10% per year. For the purpose of this study we will adopt the definition of Fischer and Reuber (2003) which requires 20% year-on-year growth for five consecutive years to be considered as rapid growth. In the USA these rapid growth firms tend to be of businesses with sales between $5 million and $150 million and fewer than 500 employees (Nicholls-Nixon 2005).

As highlighted in the previous section, firm growth has been almost implicitly construed to be a condition or assumption of entrepreneurship (Gundry and Welsch 2001). Taking this a step further it has been found that there is a direct relationship between the entrepreneur’s level of education and work experience and the rate of growth of the business (Nichter and Goldmark 2009). Nichter and Goldmark (2009) also highlight 3 firm characteristics that are associated with business growth:

(a) Firm age

On average, young small businesses tend to grow substantially more rapidly than their older counterparts do. One explanation is that a firm first expands quickly and then tapers off its growth as it approaches optimal size (Nichter and Goldmark 2009, McPherson and Rous 2010). While growth may slow down, productivity is expected to increase as the business ages and becomes more familiar with its optimal size of operation. However Nichter and Goldmark (2009) also present the alternate finding that some firms actually suffer productivity losses as they become older due to failure to sufficiently invest in existing or emerging technologies.

(b) Formality (or informality)

The informal nature of the business in itself is an impediment to growth. The informality is also associated with other characteristics that make growth difficult. Small, informal businesses can, initially, circumvent government regulations and taxation but growth increases the risk of visibility and these firms are thus not incentivised to expand beyond a certain size. This rules out rapid growth and close relations with formal firms (Nichter and Goldmark 2009).

The challenge of securing access to financial and legal systems also ensure the tendency for informal enterprises to grow more slowly than their formal counterparts (Nichter and Goldmark 2009).

(c) Access to finance

There is a strong relationship between investment and rapid growth (Turner 2006). Although many SMEs have limited access to capital, it is not clear whether credit provides a binding constraint on firm growth. It has been argued that credit access is not a significant determinant of firm performance and that there is a difference between factors significantly affecting credit access versus growth and profitability in certain industries (Nichter and Goldmark 2009).

Some external factors driving high growth according to Nichter and Goldmark (2009):

- *Vertical linkages* (formed by firms with their buyers and suppliers) can facilitate rapid growth by expanding a firm's set of viable business opportunities and improving a firm's capabilities.

- *Horizontal linkages* (where similar firms group themselves) may facilitate rapid growth by enabling a firm to overcome the disadvantages of being small and enabling an improved negotiating position with buyers or suppliers and generating a greater access to market information and services.

- *Supporting markets* provide services such as finance, consulting, legal, tax advice and so on. Access to these markets are often directly related to improved capacity and help firms respond to new opportunities.

- *Contextual factors*, such as the overall state of the economy, directly influences opportunities in the market. As a result SMEs tend to grow more quickly during periods of overall economic growth.

2.5.2 *Importance of high growth*

The importance of rapid growth business, in terms of economic development and job creation as well as for external stakeholders was highlighted in the first section of this literature review. Rapid growth has great benefit from a business model perspective too. Growth may be associated with staying ahead of the curve and expanding market share (Foster and Davilla 2010). The enhanced visibility created by rapid growth strengthens a brand and facilitates the generation of economies of scale whereby each additional customer increases the value of the business to other customers.

2.5.3 *Rapid growth challenges and Strategies*

Challenges

Some challenges, with the potential of leading to a crisis, were mentioned in the stages of growth section. The common managerial issues relating to rapid growth are typically related to people, processes and resources (Fischer and Reuber 2003). The continuous and rapid influx of employees, as the organisation expands, means that stress levels are high and skill levels are often inadequate. There is internal turmoil associated with quickly integrating new employees into the organisation combined with the need for extraordinary resources to meet the demands of rapid growth (Nicholls-Nixon 2005).

Entrepreneurs in rapidly growing ventures face greater managerial complexity and often have difficulty in determining what kinds of organisational changes and transitions are required (Nicholls-Nixon 2005). This creates an additional demand on people who have to work within inadequate management infrastructures. Management bandwidth becomes overstretched as they try to operate within the limited infrastructure with significant additional time and effort spent on selecting, training, mentoring and transferring the culture to an expanding employee base (Foster and Davilla 2010).

The issues relating to people are interrelated with process issues. It is not an issue, for most managers, to put in organisational structures according to functions. However, the challenge lies in implementing processes and systems that are designed for execution (Foster and Davilla 2010). The systems and processes in place prior to the surge in growth are rarely adequate to support the expansion of the organisation. Organisations further compound the issue by trying to adopt formalised processes wrought with bureaucracy which stifles the ability to be innovative (Fischer and Reuber 2003).

Cash flow presents a challenge as it is a scarce resource. Working capital requirements erode the profits generated by growth, and as a result of the constant change rapidly growing firms cannot realize the efficiencies that are enjoyed in more stable environments (Fischer and Reuber 2003).There are also external challenges of growth that one must be aware of. Growth attracts attention and encourages new competitors to enter the market. There is the threat that customers and suppliers may leverage their collective power to negotiate or demand better turns or even bypass the company completely (Foster and Davilla 2010).

Studies have been conducted that have found no evidence to prove that firms with access to credit grew faster than those without such access (McPherson and Rous 2010). South African studies, however, have revealed that seventy-five percent of new SMEs created in the country fail within the first two years of operation and one of the primary causes of failure is the non-availability of formal finance (Asah and Fatoki 2011)

Strategies

Success may be found for businesses that are able to develop and sustain a strong market position by acquiring and exploiting distinctive capabilities and strategic assets

(Turner 2006). Employing the right tactical and operational actions to enable a strategy depends as much on managerial and operational strengths as it does on ideas and vision (Turner 2006).

Barbero, Casillas and Fieldman (2011) highlight four different functional capabilities that may be directly related to high growth: human resource capabilities, organizational capabilities, marketing capabilities, and financial capabilities. Depending on the selected strategy, businesses should focus on controlling specific types of resources and capabilities in order to perform better.

A key focus area is the process and systems challenge. Management systems are an accelerator for building sustainable, rapid growth start-up companies (Davilla et al 2010). Too many systems can, however, lead to bureaucracy but having no systems leads to chaos (Davilla et al 2010).

In their study, Davilla et al (2010) found that companies with more sophisticated management systems grew much faster than their counterparts. Managers used the systems; to make goals explicit and stable in uncertain environments such as rapid growth start-ups; to help with co-ordination and planning the sequence of steps; to facilitate decision-making and resource allocation; to promote accountability and facilitate control. One external reason for management systems adoption is to develop the credibility of the company so as to be portrayed as a reliable and well-managed unit. The other external reason is because a partner, customer, or government regulation imposes the system onto the company.

If the company does not have a hard-to-replace capability that provides it with a source of competitive advantage, then the company must quickly and precisely put up barriers to entry to prevent competitive forces dragging down the growth (Foster and Davilla 2010).

Olawale and Smit (2010) identified collateral, business information, managerial competencies, and networking as internal factors influencing the availability of debt to SMEs in South Africa. Collateral helps reduce the informational asymmetries and moral hazard problems that arise between banks and entrepreneurs. The ability of an organization to provide financial information reduces the informational asymmetry resulting in an increase in the likelihood of obtaining capital. High levels of managerial competency of the owners of SMEs results in a greater probability of success of the firm which, in turn, promotes a greater willingness for banks to extend credit to such businesses (Rogerson 2001). Networking may be described as an activity where business owners or managers develop and manage personal relationships with particular individuals in their surroundings. Research has found that the formation of networks has helped SMEs to tap into resources in the external environment successfully (Olawale and Smit 2010).

Rapid growth brings about managerial complexity. Nicholls-Nixon (2005) highlighted a variety of approaches that can be used to cope with the increasing managerial complexity brought about by rapid- growth which include:

- Diffusing complexity by restructuring the organisation to ensure that specific individuals or groups do not get overwhelmed;
- Reducing complexity by outsourcing certain activities or simplifying the venture’s operations;
- Redefining complexity by developing a deeper understanding as to why operational problems exist and how they could be resolved. This could be

achieved by bringing together people with a variety of different functional perspectives and capabilities; and

- Developing new skills and capabilities to cope with increasing complexity through acquisition of new resources which may include personnel or systems aimed at improving organisational effectiveness.

It may be argued that rapid growth may be dealt with more effectively by developing the necessary knowledge and resources ahead of time before the pressures of growth forced a reactive response. However, a different view suggest that rapid growth could be more effectively dealt with by creating an infrastructure that enables periods of self-organised change to occur (Nicholls-Nixon 2005). This new perspective of managing rapid growth is based on the premise that existing formal structures and systems that are in place in rapid growth enterprises can rarely keep up with the rate of growth of the organisation. For any rapid growth company, the ability to quickly implement and manage change is fundamental (Turner 2006).

According to the research within the field of complexity science, it is suggested that self-organising behaviour emerges in firms that possess a deep structure (Nicholls-Nixon 2005). Nicholls-Nixon (2005) defines this deep structure as a simple set of shared rules that outlines the firm's reason for being and its basic principles of organisation. These shared rules, which includes business logic, the manner in which information is captured and shared, relationships between people internally and externally, serves to provide employees with a framework that encourages and enables leadership at all levels thereby creating a more dynamic and responsive organisation.

The current literature does not address, specifically, the funding requirements associated with rapid growth businesses. The limited literature available on rapid growth highlights the challenges and impact on the business from a management and operational perspective. As a result there is a large gap in the literature from a funding perspective.

2.5.4 *Research Question 3*

What are the financial requirements associated with the rapid growth of South African businesses?

2.6 Challenges in securing funding

Funding is crucial for the success of the business (Turner 2006). Yet many small businesses struggle to source funding or funding at good rates from the formal sector. One of the impediments contributing to the high SME failure rate in South Africa is the non-availability of formal sector finance (Olawale and Smit 2010). It has been found that the formal credit sector usually despises lending to small businesses and Datta (2010) cites a few reasons for this. Firstly, lending to small businesses poses a problem of scale. The unit cost of lending money to a small business is much higher than that of lending to a large business. Secondly, the approval of small lending usually happens at the lower echelon of management, at the lending firm, and these managers tend to be risk-averse. The third reason is that of risk. There is uncertainty associated with the small business and there is a greater risk of them failing versus that of a well established organisation.

Collewaert, Manigart and Aernoudt (2010) highlighted the high level of information asymmetry in small and young companies as a reason for market failure. This results from the lack of a track record and profit generation which creates high uncertainty for investors resulting in supply constraints from public capital markets and bank financing. The lack of collateral and credit history are also often cited as an inhibitor of access to formal business financing for small businesses (Badelescu 2010, Nichter and Goldmark 2009). Ackermann and Meyer (2007) argue that the credit decisions of South African commercial banks should be based on the quality of the applicant's business plan or potential of the venture instead of the applicant's creditworthiness and available collateral.

Higher interest rates either draw riskier applicants or influences borrowers to choose riskier investments (Peterson and Rajan 1994). This is termed the adverse selection effect and moral hazard effect respectively. To account for the issues of risk mentioned above, the formal sector insists on collateral for security while approving loans for small businesses. Despite possessing a solid business proposition the small borrower may find securing collateral, for larger loan amounts, to be a serious challenge (Datta 2010).

So if an increase in the interest rate increases the average riskiness of clients, lenders may optimally choose to ration the quantity of loans they grant as opposed to raising the rate to clear the market based on supply and demand effects. The result; limited opportunities for small business to secure formal sources of finance (Peterson and Rajan 1994).

The irregularity of information between the external lender and the small business within the formal sector also increases the cost of handling the financial transaction as a result of the need to organise, carry out and monitor the exchange in a manner which seeks to reduce the inherent irregularity (Winborg and Landstrom 2000). The relatively high transaction costs results in increased financial costs for small business versus larger organisations (Winborg and Landstrom 2000).

Entrepreneurs are not always fully aware of the range of possible financing sources available to them (Collewaert et al 2010). Venture capital is the least well-known of the capital supplying businesses (Johnson 1979). Angel investors and venture capitalists would usually mitigate the information problems highlighted above. However, due to scale economies, even venture capitalists have shifted their focus towards larger and older investments (Collewaert et al 2010). The lack of venture capital funds for small businesses in South Africa has left many dependent on bank loans and overdrafts for early stage external financing (Olawale and Smit 2010).

There are studies that have conceived that the gap between the demand for finance may reflect business problems and a lack of business experience as opposed to the failure of suppliers to provide adequate credit to meet the demand for finance (Ray 2010). Ray (2010) highlights the managerial shortcomings and underutilization of capacity as some of the key problems. Olawale and Smit (2010) also highlighted managerial competency as an important factor causing non-availability of debt finance to South African SMEs. Management considerations was found to be the single most important determinant of funding denials by venture capital firms (Johnson 1979). While business risk may be important when dealing with venture start-ups, venture team characteristics (i.e. agency risks) was found to be most important in terms of the criteria used by venture capitalists to make funding decisions (Dos Santos, Patel and D'Souza 2011). Decision-makers are often forced to make quick decisions with limited information. As such, time constraints prevent venture capitalists from studying each of the hundreds of proposals they receive in detail (Kirsch, Goldfarb and Gera 2009).

Ferreira, Strydom and Nieuwenhuizen (2010) claim that there is substantial assistance available to South African SMEs and yet the failure rate is still very high. This has prompted the question as to whether these businesses are receiving the right type of assistance at the right time to enable them to develop a sustainable organization. South African research points to the need for policy interventions designed specifically to enable successful growth for small businesses (Rogerson 2001)

There is a gap in the literature with regard to the consequences of not being able to secure funding. While the literature does mention that SME failure can be attributed to the lack of formal sector finance, it is not clear that the lack of funding always leads to failure. Findings from this study should provide insight into the consequences of rapid growth businesses being unable to secure funding.

2.6.1 *Research Question 4*

What are the challenges associated with securing funding for rapid growth South African businesses?

2.6.2 *Research Question 5*

What are the consequences of rapid growth South African businesses being unable to secure funding?

2.7 Funding strategies and capital structure decisions

This section looks at the tradeoffs and decisions that businesses must make in selecting sources of funding. These decisions taken by businesses will define the funding strategy for the organisation.

2.7.1 *Funding Strategies*

Raising funds for rapid growth requires a strategic approach (Turner 2006). Businesses can adopt various types and combinations of funding depending on its stage of growth. During the start-up stage funding tends to be haphazard and puts a strain on the finances of the founder, partners or friends and relatives (Scott and Bruce 1987). In a study conducted by Reynolds (2011) on a group of 160 nascent enterprises, the major source of financial support came from the savings of the start-up team. This was followed by family members and relatives. Credit card loans were the third most common source. Formal financial support was reported at 37% of the sample.

Financial Bootstrapping

With reference to some of the challenges faced by the small business in securing funding, financial bootstrapping thus becomes an important funding strategy for a business, particularly during the early stages of growth (Tomory 2011). Financial bootstrapping refers to the use of methods for satisfying the resource requirements of the business without relying on long-term external finance (Winborg and Landstrom 2000). There are six groups of financial bootstrapping methods that can be described.

The first group, labelled “owner financing methods,” refers to direct or indirect provision of resources from the (owner) manager or relatives. The second group is regarding methods of dealing with accounts receivable such as expediting of invoicing and is labelled “minimisation of accounts receivable.” The third group of methods concerns sharing or borrowing of resources and is named “joint utilisation.” Methods included in the fourth group deal with deliberate delayed payments from the business and are appropriately labelled “delaying payments.” The fifth group refers to methods used to minimise the capital invested in stock. This group is labelled “minimisation of capital invested in stock.” The final group includes methods concerned with obtaining subsidies from public organisations for meeting resource requirements and is referred to as “subsidy finance” (Winborg and Landstrom 2000).

In the study conducted by Winborg and Landstrom (2000) it was found that the six bootstrapping methods most used are: (1) buy used equipment instead of new; (2) seek out best conditions possible with suppliers; (3) withhold manager's salary; (4) deliberately delay payments to suppliers; (5) use routines for speeding up invoicing; and (6) borrow equipment from other businesses. These bootstrapping methods, when used effectively, play an important role in the development of a small business.

Internal versus external funding

Pecking order theory is based on the notion that SME owners prefer to use internal sources of finance before external sources (Watson 2006). According to the theory, external financing would only be used where insufficient internal funds were available to capitalise on value adding opportunities. This suggests that younger firms, with limited internal resources, would tend to be the most likely applicants for external funding. Peterson and Rajan (1994), in support of this view, also state that the youngest firms in their study relied most heavily on debt with the firms eventually reducing their dependence on banks resulting in lower fractions of borrowing.

It has also been found that loan capital is productive and enables the firm to increase revenue but has the downside in that it brings the business under the control of the bank (Watson 2006). Watson also highlighted the findings that women SME owners desire greater control over the business and confirmed these findings by demonstrating a greater level of external funding by male business owners over female business owners.

Furthermore retained earnings can be used effectively as an internal source of finance. As the business expands the owner could plough back earnings to help finance the increased demand for working capital (Scott and Bruce 1987). Self-financing can bring significant benefits to some, while for firms using it in great proportions there may be negative effects (Diana 2010). Firms with high cash flows are more likely to make acquisitions that lead to abnormal declines in operating performance (Habib 2011).

Overinvestment is more likely to be evident in firms with fewer growth opportunities (Moon and Tandon 2007).

The effect of managerial ownership on leverage is significant for large firms. Managerial ownership aligns the interests of shareholders and managers through increased leverage while institutional investors discourage managerial overspend through the board of directors and encourage firms to preserve their borrowing capacity (Moon and Tandon 2007). The latter supports the Pecking Order Theory mentioned earlier. An important finding was that the effect of ownership structure on leverage is stronger for low-growth firms than for high-growth firms (Moon and Tandon 2007). While internal funding can be less risky, it can lead to complaints from shareholders who now have to choose between dividends and economic growth (Diana 2010).

Lending Relationships and concentration of borrowing

Relationships play a pivotal role within the credit environment and can be used strategically to secure a healthy source of external funding. The age of the firm should determine the lender's cost and availability of funds based on information from prior creditors or other fixed claim holders regarding the firm's ability to service debt-like claims (Peterson and Rajan 1994). However, the length of the relationship exerts an independent influence in instances where information generated within prior financial relationships is not observable, or transferable, to outsiders (Peterson and Rajan 1994).

It must be noted that loans are not the only service that a business may require from a formal institution. These institutions offer a range of products and packages. This added dimension of the relationship has two implications. Firstly, it increases the accuracy of the information that the lender receives about the borrower. Secondly, it enables the lender to spread any fixed costs associated with production of information about the borrower over multiple products (Peterson and Rajan 1994). These effects should have positive implications for the borrower as it helps reduce the cost of finance that would usually be imposed by the lender. The assumption of course is that the lender does pass on the savings to the borrower.

In the study conducted by (Peterson and Rajan 1994) it could not be shown that the lending relationship reduced lending rates significantly. However, it was proven that the availability of funding from the lending institutions increased as the firm spent more time in the relationship. As ties with the lender strengthens, an expanded financial service portfolio is made available to the borrower. So there appears to be a direct benefit in concentrating borrowing and strengthening relationships.

Working capital management

Working capital management may be seen as a tactic to leverage internal funding as a strategy for funding growth. Most SMEs have little regard for working capital management (Sunday 2011, Ek and Guerin 2011). The lack of focus on working capital, in simple terms, implies that these businesses are leaving cash on the table. From a funding perspective this is of particular relevance as releasing cash from working capital is usually the least expensive source of cash for a company (Ek and Guerin 2011). Establishing the correct level of working capital is critical and yet a frequently cited reason for avoiding the optimization of working capital is the difficulty in establishing the right levels of it (Ek and Guerin 2011). There is no “one size fits all” approach to determine the optimal level of working capital. Establishing the optimal level of working capital is company specific and must incorporate the company’s strategy and appetite for inherent trade-offs involved in managing working capital (Ek and Guerin 2011).

2.7.2 *Capital Structure*

Most literature, implicitly, point out the significance of financial resources in enabling the growth of the organisation. But how much debt and how much equity are healthy for financing start-up and growth strategies? This essentially is the capital structure decision that the management of firms face. Most research within the domain of capital structure focuses on public corporations with little regard for SMEs. Some of the factors that have been identified to show influence to financing decisions of SMEs include culture; business goals; preferred ownership structures; views regarding control; short- vs. long-term debt; sources of funding for growth; and issues relating to independence and control (Romano, Tanewski and Smyrnios 2000). The characteristics of the entrepreneur may also play a key role in these capital structure decisions (Gundry and Welsch 2001). Investment decisions may be seen as solely important in a perfect capital market. However, when the assumptions associated with this perfect capital market are relaxed, factors such as taxes, agency costs, costs of financial distress and information asymmetry that could make capital structure important.

Two common approaches highlighted in capital structure theory include the Pecking Order approach and the Trade-off theory. According to the Pecking Order approach, managers follow a pecking order in which internal funds are preferred, followed by debt, hybrid securities and lastly a new issue of ordinary shares (Romano et al 2000).

In contrast the Trade-off theory suggests that there is an optimal capital structure that maximises value of the company and that management aims to maintain this target debt-to-equity ratio which is based on the effects of taxes, agency costs and costs of financial distress (Romano et al 2000). Firms with greater tax shields of debt, lower costs of financial distress and favourable mispricing of debt relative to equity are expected to be more highly leveraged (Faulkender and Petersen 2006).

Research within the field of SME capital structure tends to be of the view that some of the existing capital structure theories do not include some of the factors more pertinent to smaller businesses such as the owner’s objectives and business planning which are more relevant at an SME level. There are more relevant frameworks that have been proposed in which the capital structure decision-making is influenced by the owners attitude towards debt, risk propensity as well as the owners need to be in control (Romano et al 2000).

The following summary regarding financing strategies of rapid growth and low-growth entrepreneurs is based on the findings of the study conducted by Gundry and Welsch (2001). Family, friends and relatives were more likely to be used by rapid growth businesses during start-up although there were no significant differences in the utilisation of that source during expansion. Personal savings and leasing companies were also just as likely to be used, at start-up, by rapid growth businesses. During expansion, loan programs (or subsidised finance) was significantly more likely (twice as likely) to be a source for rapid growth businesses. The Pecking-order approach is of particular relevance to small firms as the costs associated with external finance are significantly higher than they are for their larger counterparts (Romano et al 2000).

In a study conducted by Peterson and Rajan (1994) involving a sample of 3,404 firms, it was found that 28% of the corporations and 45% of non-corporations (sole proprietorships and partnerships) had no institutional borrowing. The institutional debt-to-asset ratio, for the organisations with debt, was 43% percent for non-corporations versus 37% for corporations. So while a greater percentage of corporations took on debt, they were less leveraged than non-corporations. Romano et al (2000) noted that firms within a particular industry tend to have a more similar capital structure than those in different sectors. Asset intensive industries, for example, have a likelihood of having a higher debt-to-equity ratio due to the collateral that could be provided as a result of their asset structure.

The challenge when looking at debt ratios to determine whether the company's capital structure is that of the simultaneous equation bias. Firms may have low debt ratios because they have little need for external capital (a demand constraint) or is liquidity constrained (a supply constraint) (Peterson and Rajan 1994). According to Faulkender and Peterson (2006), private lenders have often been described as being good at investigating informationally opaque firms and these firms are also the firms that theory predicts may be credit constrained. These firms are thus more likely to borrow from active lenders. The source of capital may therefore be intimately related to a firm's ability to access debt markets (Faulkender and Petersen 2006).

2.7.3 *Capital Budgeting and Cost of Capital*

Capital budgeting or the allocation of funds in assets for the long term is an important process for both large and small organisations (Uddin and Chowdury 2009). Small and large firms evaluate capital projects differently (Danielson and Scott 2006). Large firms tend to rely on the Discounted Cash Flow (DCF) while small firms have most often cited "gut feel" and the payback period as their primary project valuation tool (Danielson and Scott 2006).

This capital budgeting process is essentially and investment decision-making process in which the viability of future projects or investments are assessed through the use of techniques such as the Net Present Value (NPV). NPV is one of the most frequently used capital budgeting techniques and involves discounting all relevant cash flows at a market discount rate (Uddin and Chowdury 2009). A Firm's WACC or Weighted Average Cost of Capital is widely used as a discount rate and consists of a Cost of Debt component and a cost of Equity component. The cost of equity is usually straight forward to determine as this is usually the price of borrowing from the financial institution. The Capital Asset Pricing Model is the most popular method used for the estimation of the cost of equity component (Truong, Partingon and Peat 2008). The value of investments is maximised when the NPV of its future cash flows, discounted by the WACC, is maximised. The quantification of the cost and value of equity are thus necessary for optimal investment and capital structure decisions (Moro, Lucas and Kodwani 2010).

Determining the cost of equity for large listed corporation is usually straightforward as this is provided by the share price on the stock market. It is however, important to recognise that the associated risk varies between projects. It must be acknowledged that in these types of analyses an attempt is usually made to allow for the existence of that uncertainty. This attempt typically takes the form of superimposing a "risk discount" to be subtracted from the expected yield or a "risk premium" (as seen in CAPM) to be added to the market rate of interest (Modigliani and Miller 1958).

In the case for unlisted SMEs there are no stock market prices or data available. In an ideal world the value of equity and its expected return could be derived from financial statements, however, Moro et al. (2010) point out that financial statements as a source of relevant information for the estimation of cost of capital have three major limitations; Firstly, the figures reported in financials may not necessarily represent the economic value of the underlying assets and liabilities; secondly, there are many intangible assets and other off balance sheet items which may not be captured in the statements; and thirdly, financial statements are affected by subjective estimation processes such as depreciation. The authors go on to mention that entrepreneurs are often required to provide personal guarantees in order to secure bank finance leading to the assumption that equity invested in an owner-managed firm is the sum of the nominal value of cash invested by the entrepreneur as well as the amount of personal guarantees provided.

Building on the two assumptions mentioned above, Moro et al. (2010) propose a model for determining the expected return for the entrepreneur which includes two premiums;

a premium for the probability of bankruptcy; and a premium for the impact of the loss at liquidation.

There is little research underpinning particular funding strategies and whether rapid growth businesses reflect a distinctive pattern in their capital structure and funding strategies. Furthermore there is limited literature that highlights tactics that rapid growth businesses could employ to leverage their funding strategies.

2.7.4 *Research Question 6*

What are the funding strategies and tactics adopted by rapid growth businesses in South Africa?

2.8 Conclusion of Literature Review

The literature review provided some insight into the different stages of growth or development of a small business along with the challenges and funding requirements that a business may encounter at the different stages. However, there appears to be a lack of empirical evidence underpinning the theory which has opened most of the literature up for criticism.

Some of the more common sources of funding and funding strategies were highlighted. Rapid growth and its characteristics were also highlighted. Any literature on rapid growth has almost invariably been linked to start-up and early stage businesses. There is a gap in the literature with regard to the nature and behaviour of rapid growth businesses at later stages of growth.

There is a gap in the literature with regard to funding requirements associated with rapid growth and the implications for not securing funding. There is little or no research underpinning particular funding strategies and whether rapid growth businesses reflect a distinctive pattern in their capital structure and funding strategies. In general, there is a lack of research in South Africa relating to business growth and funding. These gaps have motivated the current study.

3 RESEARCH METHODOLOGY

3.1 Introduction

This section addresses the research methodology component of this research. The research design and paradigm that underpin the research will be discussed. This includes plans and procedures for research that range from the broad assumptions to detailed methods of data collection and analysis and the decisions associated with it (Creswell 2009).

3.2 Research methodology / paradigm

The purpose of this research is to define the funding strategies utilised by rapid growth businesses at the various stages of their development. As there is little prior research, this study research is exploratory in nature and does not seek to prove or disprove any hypotheses or examine any relationship among variables but is conducted to highlight key findings in this area. Qualitative research is used to explore and understand the meaning that individuals or groups ascribe to a social or human problem (Creswell 2009). In this case, the problem of financing rapid growth is explored. As a result a qualitative research is a suitable methodology that guides this research.

Qualitative research covers a multitude of research paradigms which there exists many methodological approaches, processes and techniques (Carroll and Swatman 2000). Essentially, a paradigm is a set of principles, or philosophies, that govern the way we think. The research paradigm that underpins this study is interpretive in nature. The interpretive paradigm assumes that the researcher can best understand the reality of a situation by being part of it as the belief is that knowledge comes from human experience (Hathaway 1995). With the research being exploratory in nature and requiring the researcher to tap into the minds of entrepreneurs and business managers whose perspective may, at times, be subjective in nature at times and not always based on fact, it is appropriate that an interpretive philosophy guide this research.

3.3 Research Design

Based on the research paradigm, face-to-face interview would be the most suitable methodological approach. The face-to-face interview enables the researcher to present a set of open-ended questions aimed at inquiring into the approaches taken by the managers of the business in securing finance in the past and present. It will also seek to understand what the implications were as a result of the various methods adopted by the business. Room for probing would be required and a semi-structured interview would need to be conducted.

The advantage of the face-to-face interview is that it supports the research paradigm and enables the researcher to understand the reality as created by the respondent. It enables the researcher to delve deeper into the mind of the respondent with the potential of uncovering something that may not have been covered in the literature. The interview also enables the researcher to uncover the respondent’s own framework of meanings (Britten 1995). The semi-structured nature of the interview will enable the researcher to guide the conversation and probe deeper where necessary to uncover more detail. This will ensure a richer quality of data.

The disadvantage of this method is that it is a time-consuming process and requires respondents to take a significant amount of time out of their day. In order to accommodate the interviewees (who where owners and directors with busy schedules) as far as possible, the researcher made meeting times as flexible as possible and often arrived an hour before the scheduled interview and was prepared to wait for as long as possible if the interviewee was running late. Locations were selected based on convenience for the interviewee and even included meeting at a coffee shop for one particular respondent.

Interviewees may feel the need to distort the truth relating to the start-up of their enterprise to create a “rags to riches” perception. The semi-structured nature of the interview allows the interview to moderate embellishment through the use of probing questions. The interview process can be negatively influenced if the interviewer does not create a good rapport with the interviewee. The researcher made a conscious effort to demonstrate emotional maturity and objectivity so as to manage the “climate” of the interview.

The underlying problem of the interpretivist approach, in general, is that humans are poor processors of data. This is characterised by a poor short-term memory capacity; the tendency to draw conclusions from limited data; the tendency to pay more attention to influential informants; poor grasp of the concepts of causality and other basic statistical concepts; and the potential to disregard disconfirming evidence (Carroll and Swatman 2000). All interviews were recorded and transcribed to ensure that data collection was complete and unbiased.

3.4 Population and sample

3.4.1 *Population*

As the methodology used is qualitative and makes use of interviews, there was not really a population that is being studied. The scope of the respondents that were included in this study are small, medium to large organisations (excluding very large corporate and multinationals) that meet the rapid growth requirement of 20% year-on-year revenue growth for five consecutive years or more who operate within the Gauteng region. For the early stage companies or start-ups (with less than 5 years of operation) to be included, year-on-year growth of greater than 20% for 2 to 4 consecutive years was allowed for these exceptional cases.

3.4.2 *Sample and sampling method*

Interviewees were selected based on their particular stage of development. The Greiner 5-stage model was used as a guide to identify what stage of development the business was at. Businesses across different industries and different stages of development were interviewed. As such the sample was heterogeneous. The businesses were not limited to a particular sector or industry and as such the "sample" was a maximum variation sample due to its broad range of subjects (Marshall 1996).

As a result of the research design, combined with the fact that rapid growth businesses within a depressed economy are somewhat limited, nine companies were identified. Probability sampling is not effective when the subjects constitute a small part of the general population (Heckathorn 2002). While this method of sampling usually refers to quantitative research, the nature of the sample is relevant in this study. As such a non-probability method, in the form of snowball sampling, was used as a method of selecting respondents. Snowball sampling is, essentially, the process by which the researcher is referred on to other respondents by the current respondents (Flint and Atkinson 2001). This was based on the premise that rapid growth businesses have strong business networks and will be aware of other businesses within the network that are experiencing the same levels of growth. The sample has an element of convenience sampling as the researcher sought to choose the most accessible subjects but also is a judgement or purposeful sample as the researcher actively selected productive samples to meet the selection criteria mentioned above based on information and not statistical considerations (Marshall 1996).

3.4.3 *Overview of the companies and sectors*

The companies interviewed were across different industries although the two largest were within the mining industry. The size of the companies ranged from an 'R850k' to 'R600m' in terms of annual revenue. The ages of the company ranged from 2 years through to 33 year old businesses. The companies provided a nice spread across the different stages of development which was the intent for the research.

Companies were mapped according the Greiner Stages of growth descriptions as best as possible. It quickly became apparent that businesses do not fit neatly into the stages as defined by the Greiner Model.

Table 3 provides an overview of the characteristics of the businesses interviewed. A more detailed description of each business can be found in Appendix 3.

Table 3: List of respondents (own compilation)

Company	Industry	Age	Annual Revenue	Stage of Growth
A	Materials Handling	2	R1.7m	1
B	Art	10	R850k	2
C	Petrochemicals	4	R55m	2
D	Signage	10	R44m	2
E	Transport	27	R200m	2/3
F	Trailers	27	R70m	3
G	Plastics	14	R94m	3/4
H	Mining	24	R600m	3/4
I	Mining	33	R500m	4

3.5 The research instrument

The actual instrument used for the research was an interview schedule. The interview was designed to take a semi-structured approach. The questions were designed to be open-ended. The first part of the schedule contains general questions about the business. These easy to answer questions were aimed at putting the interviewee at ease with the interview by enabling him/her to easily respond to questions ensuring a level of comfort.

The second part of the schedule delved deeper into funding requirements. The questions sought to understand the current funding requirements of the business and also tested the memory of the interviewee in terms of inquiring on past funding requirements of the firm.

The third part of the schedule addressed the funding requirement associated with rapid growth. There was a gap in the literature with regard to this specific information and this part of the interview was a source of valuable information.

The final part of the interview dealt with the sources of funding and strategies employed by the business. Only rapid growth businesses were studied, as such the strategies utilised by the companies gives direct insight into strategies of rapid growth business which addresses the main purpose of this research.

A copy of the interview schedule is included in Appendix B.

3.6 Procedure for data collection

Data was gathered using an audio recorder. Writing notes during the interview tends to be distracting and writing notes after the interview may result in key information being overlooked. Provided that interviewees are comfortable with talking in the presence of a recorder, recording the interview provides the most robust means for data collection in this instance. During the process of the data collection, the interviewer clarified any misunderstandings with the interviewee instead of relying on his own assumptions. The recordings were transcribed and the researcher checked the transcriptions against the recordings for accuracy and completeness.

3.7 Data analysis and interpretation

The data collected from the interviews was analysed using a method called content analysis. This is a common method used to analyse written, verbal or visual communications (Elo and Kyngas 2007). The aim of the analysis is to synthesise the key findings relating to funding strategies and methods of approach adopted by the entrepreneurs interviewed. Since content analysis seeks to provide knowledge, new insights, representation of facts by making valid inferences from data to their context, it is the most suitable method to be used for this data set (Elo and Kyngas 2007).

There is not enough former knowledge on this research topic, therefore the analysis will be inductive in nature. Inductive content analysis is an approach that moves from the specific to the general so that the instances observed, may then be combined into a general statement (Elo and Kyngas 2007).

The following figure illustrates a method to be followed when analysing interview transcripts in qualitative research.

Figure 2: Qualitative data stages of analysis (adapted from Burnard 1991)

The last phase of the content analysis is a process called abstraction. Abstraction regards formulating a general description of the research topic through the generation of categories and sub-categories (Elo and Kyngas 2007). Content analysed would then be integrated with the abstraction process.

3.8 Limitations of the study

It is possible that interviewees may not accurately recall strategies adopted or outcomes regarding funding if it had occurred many years ago. Interviewees may not be willing to give too much detail on their strategies or true reasons underpinning their strategies.

3.9 Validity and reliability

It must first be noted that validity does not carry the same meaning in qualitative research as it does in quantitative research (Creswell 2009). Qualitative *validity* means that the researcher employs certain procedures to ensure accuracy of the findings while qualitative *reliability* regards consistency of the researcher's approach across different researchers and different projects (Creswell 2009). It is important to ensure validity and reliability within the research process to avoid misinterpretations and generalisations leading to the drawing of inaccurate conclusions.

The following two sections will highlight some of the strategies that the researcher will use to ensure validity and reliability of the data and findings

3.9.1 *Validity Strategies*

The snowball sampling approach enabled trustworthy, authentic and credible sources to be selected during the sampling stage. It was clearly articulated to the respondents that confidentiality would be maintained throughout the research process. This ensured that respondents had peace of mind and were willing to openly share detail instead of masking answers.

Member checking was used to validate accuracy of qualitative findings. A colleague, who was not involved with any other aspect of the study, was briefed on the process of category generation and thereafter read through the transcripts to identify an independent category system. This category system was then compared to the researcher's category system and the final category system was then agreed upon.

Creswell (2009) suggests the use of rich descriptions to convey findings as these detailed descriptions create a more realistic and richer perspective which can contribute to the validity of the findings. The findings presented in this report are relatively granular thereby ensuring that richness of data was not lost

3.9.2 *Reliability strategies*

To ensure reliability, the same procedure was used for all the interviews. Interview transcriptions were reviewed to ensure that they did not contain obvious mistakes that could have occurred during transcription. The categories identified were consistent across all the transcripts.

4 PRESENTATION OF RESULTS

4.1 Introduction

The following chapter contains the key findings from the interviews that were conducted with each of the rapid growth businesses. The findings have been grouped into seven themes (containing sub-themes) and have been categorised according to the research questions underpinning this study. The figure below illustrates the key themes, in the column to the right, and their relationship to the research questions in the column to the left. The last theme "ability to survive without funding" does not relate directly to a research question but represents key findings and, as such, is such categorised as an emerging theme.

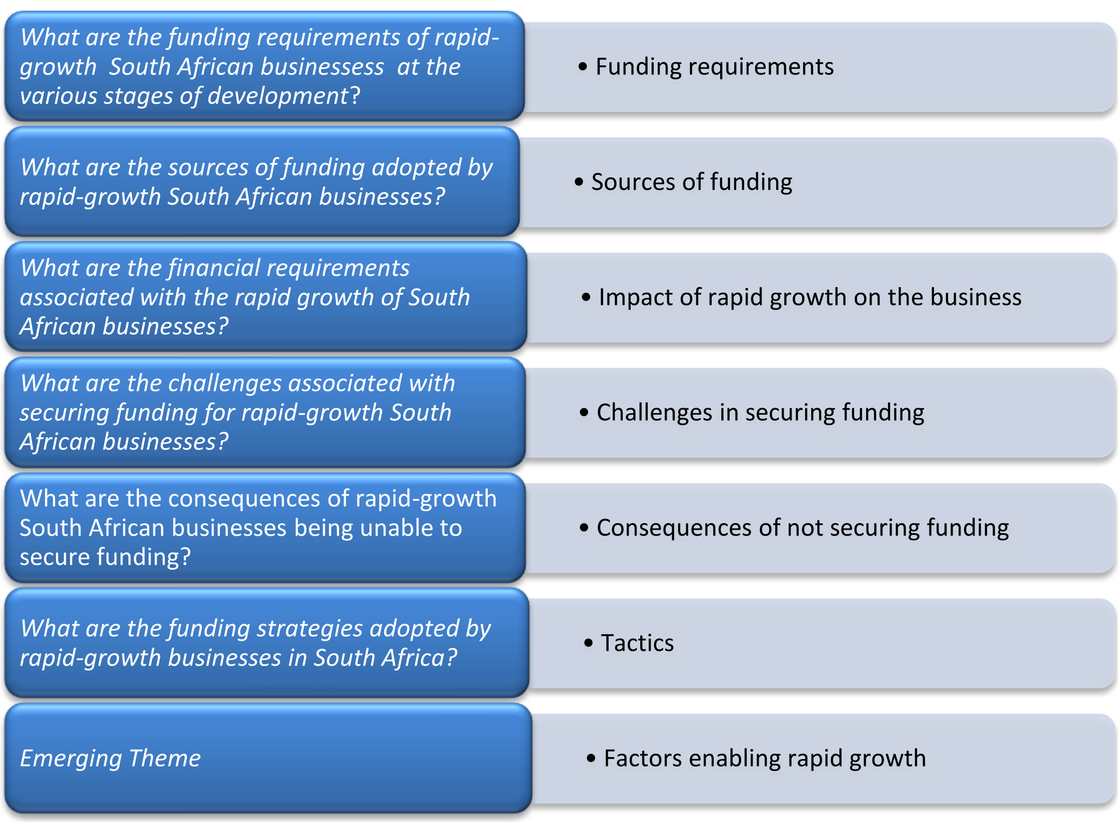


Figure 3: Themes related to the research questions (own compilation)

The following schematic provides an interesting visual representation of the companies based on the parameters of revenue, number of employees and stage of growth as guided by the Greiner model. The number of employees is measured along the x-axis and the stage of growth is measured along the y-axis. The size of the circles, which represents each of the companies interviewed, is relative to the company's annual revenue. The figure below clearly illustrates the maximum variation of the sample used for this study.

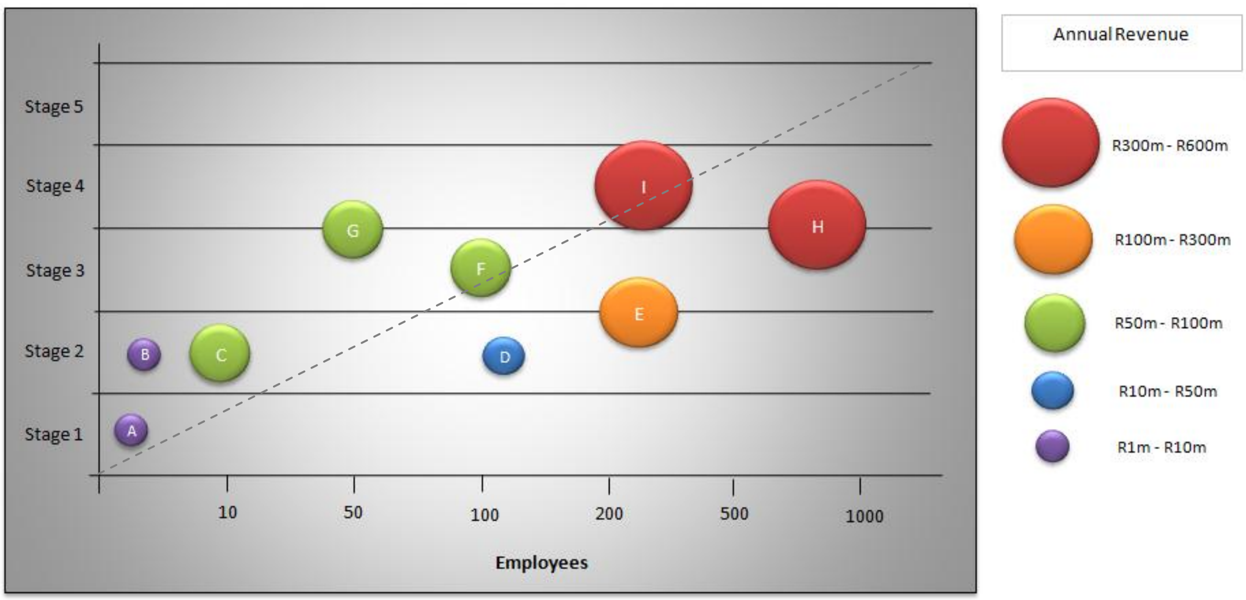


Figure 4: Sample mapping (own compilation)

4.2 Findings relating to funding requirements

What are the funding requirements of rapid growth South African businesses at the various stages of development?

– Research Question One

4.2.1 *Funding requirements*

This section highlights the funding required at the various stages of growth. The funding requirements may be defined by three broad sub-themes i.e. *working capital*, *capital expenditure (CAPEX)* and *operational expenditure (OPEX).*

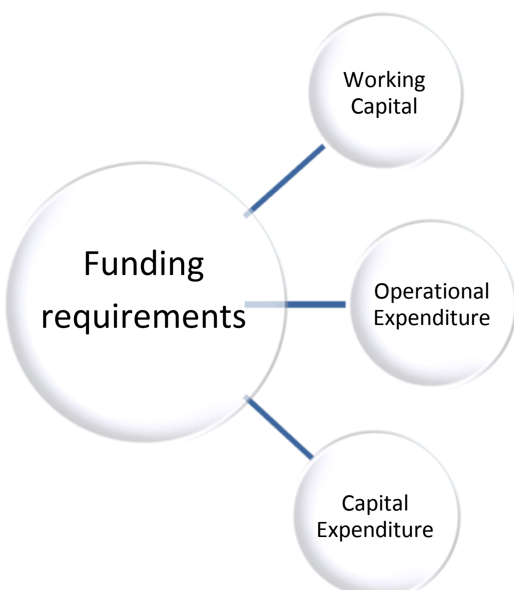


Figure 5: Funding requirement sub-categories (own compilation)

Working Capital

Working capital refers to the money that is tied up in accounts receivable, accounts payable and inventory and impacts the cash flow of the business necessitating the need for short term funding in order to manage the flow of cash.

Working capital appeared to be a common challenge among rapid growth companies and became central to the financial challenge as the businesses transgressed their earlier stages of growth and moved into a rapid growth phase. Orders tend to come in at a rate faster than the business can often handle. Companies that have not geared themselves to convert orders into sales find themselves running over budget as works in progress and inventory escalates driving up working capital

> *"We are running at 155% above budget on the order in-take, but we are not converting the orders into sales, invoicing in other words. So we are being caught in terms of cash flow and as a result we are borrowing more money from the group than we would like to." – Company I*

The increased activity means that management attention becomes focussed on the operational aspect of the business. Some see the need to implement robust management controls but this does not happen overnight. The diversion of management focus from debtors allows for a creep in debtor days as it is in every debtor's best interest to pay as late as possible or even not at all!

> *"You just take your eye off the ball because you are focusing on something else and I promise you, people don't pay, they use excuses and before you know it you are sitting with a book and your 60 and 90 days are starting to pile up." – Company G*

The pressure on working capital is also applied from the supply side as businesses are forced to deal with new suppliers to meet growing demand along with facing new credit terms. The need to secure contracts quickly, in a rapid growth environment implies that the business is not in a strong negotiating position and often has to accept the terms imposed upon them. This problem is further compounded when importing product as the long lead time associated with shipping in supplies has a negative impact on the cash conversion cycle of the business.

> *"The best terms you can get out of India are about 45 days from the time they ship it. Now remember it can take 6 to 8 weeks depending how it's shipped. So if you look at 6 weeks on the water, it arrives here, it comes from Durban to Johannesburg then we still have to convert it and distribute it. So the truth is we were paying for our product before we were receiving our money" – Company G*

> *"In certain instances ...because also you must know that this is where the juggling part comes in, because 60 days from invoice, but these heavy equipments gets sea freighted, so as soon as it's dispatched the invoice goes out. So now the clock starts ticking, so I've got to be very sharp with this." - Company A*

Capital Expenditure

Capital expenditure refers to expenditure on assets that is capitalised and will sit on the company's balance sheet. These are typically expenditures on property, plant and equipment and are usually big ticket items that will require funding.

.

The growth in the sales of businesses tends to prompt an increase in the capacity of most businesses to enable and to sustain the growth. For some businesses this implied increasing factory and office space along with the machinery to support it. For others it meant increasing equipment such as trucks and trailers. Simply put the investment is in long term assets that will generate future economic benefit for the business.

“So a lot of the funding requirement at this stage is for expansion and growth into capital expenditure. So new facilities, factory buildings, new equipment and that sort of thing, so that's the main funding requirement of the business at the moment” - Company H

“Funding basically is to buy trucks and trailers, that's what we want the money for” - Company E

Operational expenditure

The increased activities within the business also implies that more resources are required which increases operational expenses. This compounds the cash flow challenge for the business and short term debt is required if tactical moves are unable to be executed to delay payment of OPEX. Labour was found to be a significant operational expense amongst many businesses as businesses were required to grow their staffing compliment in line with growing demand.

“We are not really in the business at the moment of acquiring other businesses, so our funding is primarily from an operational perspective, so it's funding the operational costs.” – Company I

“There have been two key elements to it. There has been a massive requirement for capital infrastructure, machinery, capital equipment like that and also to fund our staffing growth. So operational costs in terms of employees and growing our staff labour.” - Company D

An interesting finding was the inclusion of Value Added Tax (VAT) as an operational expense. Typically this would not be labelled as an operational expense but it does appear to impact cash flow amongst companies with large sales, relative to the size of the business, and where debtor days are longer than most other companies are accustomed to. Certain companies have required facilities to enable them to manage this expense item.

> *"My other funding challenge is always the VAT issue, you have huge sales. When I say huge, you sell art work for R100 000 to a museum, that's great, museums take 6 months to pay. VAT on R100 000 is R14 000 which I've got to pay then. So at this stage it's funding but also cash flow, finances, bridging finances is always a challenge" – Company B*

Working capital requirements stands out from the OPEX and CAPEX requirements. This could be attributed to rapid growth. In general the findings are not surprising.

4.3 Findings relating to sources of funding

What are the sources of funding adopted by rapid growth South African businesses?

– Research Question Two

This section highlights the various sources of funding adopted by rapid growth businesses. Funding can come from a variety of sources as depicted by the following figure.

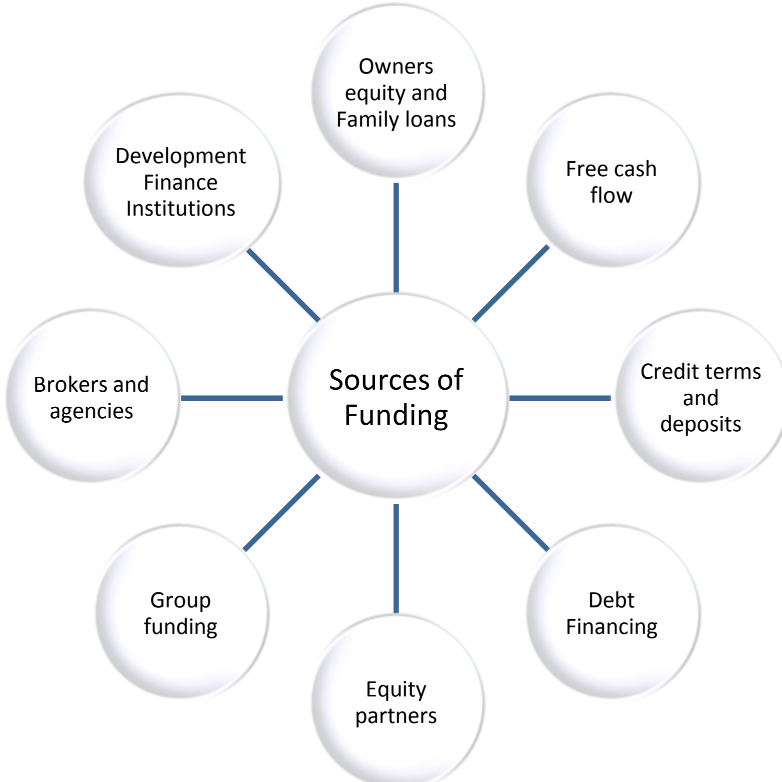


Figure 6: Sources of funding sub-categories (own compilation)

Owner's equity and family loans

Owners' equity is found to be the common source of funding during the start up stage of the business. Entrepreneurs may source funds from previous investments or from savings accumulated over the years. Businesses are unable to secure loans from financial institutions and need to have money in the bank to get the business going.

> *"When I sold my shares in **** ******* ********, I took R600 000 there because I felt I needed some money in the business to start. So I took R600 000 and relinquished my shares to my brother, so there was a transaction. That's R600 000 went into starting the business" – Company C*

A number of the businesses had a strong support system from family which enabled the business to fund growth in the early stages. Owner-managers, in certain cases, continued to leverage family resources to secure funds when the business faced challenges even during later stages of development.

> *"My first big purchase was this property. The initial funding was through family, so it was loans based on family, no equity, just loans payable back to family, which was a fortunate position to be in. That's was probably for the first 2 to 3 years." – Company D*

> *"My mother is obviously older than me – my partner and she has got certain assets, like she had a lot of money in a bond. Not a lot of money but she's got certain assets like bond or one that is at least available. So there has been a lot of moving money in between individuals and businesses and loan accounts" – Company B*

Where access to family funds or personal funds were low business owners have had to bootstrap the business in order to get it running.

> *"My mother started from the corner of our lounge. I won't say she's risk averse; you won't start a business if you are risk averse. She also didn't have a choice..." - Company B*

Free cash flow

Free cash flow, as a source of funding, refers to the use of cash generated out of the profits of the business to meet future funding requirements. It was found that business owners and managers will fund growth with free cash flow as far as possible i.e. Internal funding was the most common source of funding amongst all the companies interviewed.

"My cash flow was strong enough that I could roll my cash flow into growth, so my (external) funding requirements were very small." – Company D

"We don't have an overdraft facility, we don't finance any of our vehicles, if we've got to buy something we save up and buy it and it all comes out of cash flow, our profit so to speak" – Company F

Credit terms and deposits

Where the business could not generate enough free cash flow to fund the operations they used their suppliers and clients as a source of funding. A business's creditors can be effectively used as a funding mechanism through the negotiation of favourable credit terms which allows the business to procure supplies without there being a physical outflow of cash from the business. Businesses are thus able to retain cash for a longer period of time, enabling them to fund their operational expenses while the supplier carries the cash flow burden.

"I honestly believe that a large portion of businesses are using their creditors as a funding mechanism. So the slow payments that they do to their suppliers frees up capital for them at the moment. So they hold onto it to make sure you are first in the line to make sure you are noticed in terms of payment. But I get a sense that companies are using that as another avenue of funding. So securing slow payments, instead of paying on 30 days terms going through to 60 and 90 days. I've negotiated 60 day accounts with my five big suppliers, but bearing in mind that that comes at a premium because I don't get the discounts." – Company D

Where credit terms cannot be negotiated, clients have also been made to pay deposits on their orders to fund the procurement of supplies and raw materials, or can help to reduce the funding gap created by a long cash conversion cycle. The deposits can sometimes go a long way in funding a business's work in progress. Some of the businesses have managed to secure deposits of up to 50% which is a substantial cash flow injection.

> *"Then on the bigger trailers they also take a longer lead time, we ask for a 40% deposit. So we use the deposit just to cater for that, because you've got to go and lay out quite heavily on certain primary items that you've got to buy from overseas" - Company F*

> *"So I've got my first months funding that I need to cover, but what I do on certain of the bigger items, because it's customer specific designed I would ask the customers for a 50% deposit. So I would get that 50% deposit in, I would use that money to fund the manufacturing process." - Company A*

In some instances, companies that had developed strong relationships with clients were able to get the client to pay staggered payments, following the initial deposit, as the product moved through the different stages of development.

> *"Normally we request 50% up front, and they either accept or they bring us down to 30% up front. It would cover the materials cost to a large extent, and then depending on the history that we've had with that client, the client would either pay another staggered payment before the goods are completed and then would pay on completion or on credit terms" - Company I*

Debt Financing

Overdraft appears to be a certainty within a rapid growth environment even for companies that have enjoyed limited inventory and favourable terms in the past. Whether a business managed their working capital effectively or not, short term debt was always required to manage the funding gap. The instability created within a rapid growth environment necessitates the need for an overdraft facility to act as a buffer against cash flow issues. Overdraft facilities are mostly used to help businesses close the funding gap created by a long cash conversion cycle i.e. the gap between when the business pays its supplier and when it receives money from the customer. Some companies manage to avoid overdrafts in the early years of the business when growth is manageable but the instability created by rapid growth requires a buffer to manage working capital.

> *"Overdraft facility probably came into account probably in year 5. An overdraft facility where I was able to roll that short term finance back into the business. So that sustained my annual growth of 20 % plus over years 4 through to 8, round about that stage." – Company D*

> *"My cash conversion cycle is directly linked with my overdraft facility." – Company D*

An interesting finding was that certain businesses have used their overdraft facility to make capital purchases which is uncommon as typically long term debt would be used for such expenses. This was driven by the businesses attitude towards the signing of surety.

> *"Then we used Standard Bank for the overdraft. Because what we did was we used the overdraft for everything, to go buy cranes or buy whatever, we didn't want to sign surety, we just used the overdraft to go and buy it" - Company F*

Letters of credit were found to be used by a number of foreign markets. As a result of its ability to enable the buyer to purchase products on terms, it was used effectively as a source of funding. The system has benefited both the buyer and the supplier.

> *"Letter of credit...that's the way the majority of businesses work. So from that basis now what happens is as you are placing orders, and even if you are placing orders 6 weeks before, and with polyester it's a long production line. It's not something that you can say I need x and they quickly produce it. So when you*

are placing it's already holding the money, so we had to take our facility from R500 000 to a million, from 1 million to 1 and a half million, from 1 and a half million to 2 million, to 2 and a half million. And all that was doing was funding getting our product in." – Company G

Except for high margin businesses with a very healthy cash flow or historic cash position, long term debt finance was a key form of finance that was required to enable growth. Businesses have sought this form of finance from all four of South Africa's major banks to investment in property, plant and equipment. The owners would have had a personal preference for certain banks which has led them to finance the business along the same channels. Businesses have reported, however, that certain banks are better at certain activities. Respondents have highlighted Absa as good for commercial funding, Wesbank and Standard Bank for vehicle and asset finance and Nedbank for home loans.

"Current sources of funding without a question of a doubt, whether it be rightly or wrongly it's through financial institutions. That makes up for a lot of our capital expenditure, so that's our capital, our products, our machinery." – Company D

"I found certain banks are good at certain things, for example Standard bank is fairly good at vehicle asset finance and that type of thing…. Nedbank, I've taken out loans with them, they are very good with home loans and that type of stuff" – Company F

Companies looking at moving into foreign countries are also looking at alternative sources of funding that can be provided by the local banks abroad. Some of the foreign banks offer rates that are far more attractive than the South African banks.

"We are looking heavily into Africa and Australia. We are looking at different ways to fund it. The Australians market interest rate is a lot more attractive than South Africa, they are sitting at between 4% and 5%. So for us to set up an entity

in Australia and use their banks to finance it, and supply here is much better than spending 10 %, so we are looking at those funding options." - Company F

Equity Partner

Equity partners are another source of finance for the business that can provide not only an injection of cash but also introduce new skills, access to resources and networks. Businesses have found that bringing in high profile equity partners can be a strategic move to take the business to the next level. Taking on an equity partner can be a key source of finance, especially for high potential young businesses that are unable to secure funding from financial institutions. Private equity funders are typically interested in such young businesses that they can help grow, get their return and leave. The private equity route, however, was not exploited by the majority of the companies interviewed.

> *"So there is a lot of value and there has been a huge amount of work as you know over the past few months to see the pros and cons of bringing external partners in to this business from an equity basis and see what benefits they bring. Not only from a sales point of view and open certain doors to participate, but from a funding and equity and just from a financing arrangement in which they have the skills to do much better than me, so to improve the efficiencies of this business" - Company C*

> *"I think to a very large extent Company I was a South African company operating in an African environment and mid 2000's the decision was made to make it more of a global player in selected territories where there is sustainable mining, and thus the fact that the BEE partner brought some cash injection into the company which did assist with that rapid growth that we were embarking on" – Company I*

At the end of the day, however, it is a legal requirement to show progress in terms of Black Economic Empowerment (BEE) and as such there is a national drive to have black equity within organizations. This also can become a “licence to operate” in the sense that clients score more favourably on their BEE rating if their suppliers are accredited BEE companies. Companies without a BEE rating may find it difficult to do business in the current environment. It is a major driver for equity transactions.

> “*There is a national drive to have black empowerment. So it is a legal requirement to show progress in terms of black empowerment. From a clients perspective because our clients are primarily mines, they score more favourably if their suppliers are accredited BEE companies” – Company I*

Development Finance Institutions (DFIs)

Like private equity, the majority of the businesses interviewed made no attempts to secure DFI funding or knew very little about it. The Industrial Development Corporation (IDC) and Enablis were the only two sources of DFI funding highlighted by the respondents.

> *“We took out a loan in the late 90’s for our first expansion through the IDC and we paid that back fairly quickly…The IDC had a relatively low interest rate, I can't remember what it was, but it was probably prime less 4 or something at that stage, it was a nice interest rate” – Company F*

> *“Enablis helps you facilitate funding with the bank, I don’t know if you know anything about their funding? It's like a funding, they facilitate small business funding in either loan or equity situations via FNB” – Company B*

Brokers and agencies

The use of brokers and funding agencies has been employed by certain companies. The funding, ultimately, comes from the bank but the brokers or agents provide an intermediary service to the business. They determine the business needs and would apply to the various financial institutions, on behalf of the business, to secure the best funding. Businesses don't negotiate directly with the bank in such situations.

> *"We used to deal with brokers, and the brokers would come along and say what is your requirement? You would say 10 (million rands), he would say cool and he would put together a bundle, you would fill in application forms and he would try and discount it to a number of institutions. So I would say 4 or 5 years ago you never really negotiated directly with your banks. The banks relied on the brokers or their intermediaries to come and get the business." - Company E*

> *"There are various funding agencies and one of the things about our business is networking. We've had quite a lot of success with various funding agencies before foundation funding came through after 4 years of working on a particular proposal for a client." – Company B*

The findings in this section are a rich source of information. It can be seen that there is a wide range of funding sources that businesses may choose from. All the sources may not be readily available to the individual business, however, it does indicate that a variety of options do exist and businesses should determine which sources of funding best supports their strategy and devise tactics to make optimal use of these funding options.

4.4 Findings relating to rapid growth requirements

What are the financial requirements associated with the rapid growth of South African businesses?

– Research Question Three

This section highlights the effect that rapid growth, in particular, has had on the business from an operational and financial perspective. The sub-themes that consolidate the impact of rapid growth are defined as *business instability*, *cash flow drain* and *rapid investment of CAPEX*.

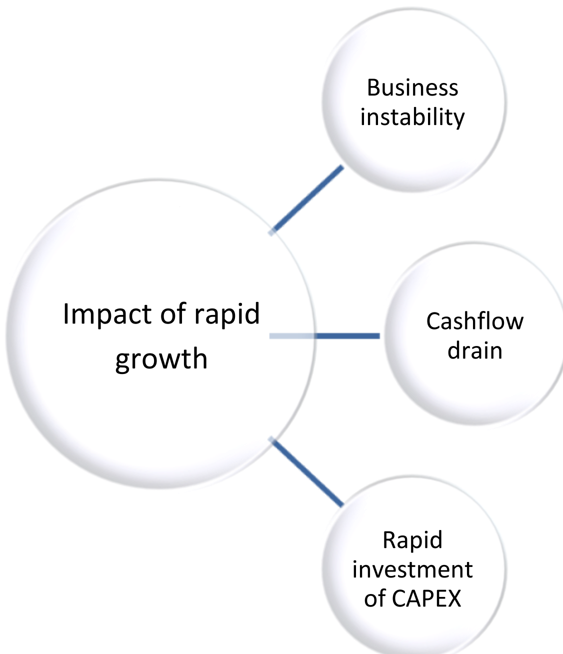


Figure 7: Impact of rapid growth sub-categories (own compilation)

Business instability

From an organizational perspective the rapid pace of growth results in managers growing the business at a pace faster than that which they can restructure thereby creating instability within the organization. A good business may find that it may not have developed the relevant competencies, skills or processes to effectively deal with a rapidly growing organization. This can lead to the business collapsing in the future due to the lack of robustness

“I think growth is a good thing but I’ve seen that it can also be a bad thing. When you build a house and you have to build it quickly, the foundation is not as strong as it should be…I think around us too, often people have this rapid growth and then things start falling in and it actually blows up in your face.” – Company C

The lack of structure within the organisation was found to manifest in three broad results i.e. a lack of focus, operational inefficiencies and management complexity.

The increased activity within the business and the lack of resources and processes to effectively deal with the activity results in management losing focus on key areas such as debtor days, as was highlighted previously. This lack of focus may lead to cash flow instability within the organisation.

“Once you get rapid growth then you start losing your eye on those guys (debtors) and you start using overdraft facilities because things become a bit unstable” - Company G

The second factor contributing to instability is the inability of the business to develop the key competencies to match the evolving needs of the business. The result is operational challenges which introduce inefficiencies. The lack of competencies may not necessarily have quality implications but can really unsettle the input of key parameters which can lead to a drop in inefficiency which, in turn, can affect marginal costs of products and reduce profitability.

“Operational issues, with rapid growth you normally incur some operational issues and that is somewhat what we are experiencing. Even though we are sub contracting a lot of the work, we’ve had rapid growth in the last 5 years and we haven’t necessarily grown our competencies from an operational perspective in

line with our financial growth, so we do have those issues to address" - Company I

"There haven't been really of a working capital perspective, it's been the capacity issues. The rapid growth was not necessarily addressed in terms of capacity as well as competency, so that has impacted on delivery accuracies. It has impacted not necessarily on the quality of the product, it has impacted on the quality of the inputs into the way we do business" - Company I

Whether one prepares the business adequately or not, rapid growth will undoubtedly impose greater management challenges than a good structured growth. Structured growth is predictable and allows management to plan more accurately and allows adequate time to structure the organisation effectively. Rapid growth, along with its uncertainty and frenetic pace, introduces management complexity which results in an evolution of the business if it is to survive.

"And remember it's harder to manage rapid growth than a good structured growth." – Company D

"It (rapid growth) puts it (management) under serious strain" – Company E

Cash flow drain

The rapid growth environment is where management has to react quickly and the deals negotiated are not necessarily optimal resulting in the business carrying unfavourable terms with suppliers which can take some time to amend. The frenetic pace of growth and the increase in activity within the business also results in management losing focus on issues such as debtor days which was mentioned earlier. Businesses have found that their debtors book has grown larger and larger and basically they are funding their customers. The delay of a cash injection into the business puts the business at risk from a cash flow perspective.

“We are carrying a book now, which is ridiculous, we are becoming a bank, and it is the biggest hurdle to growth for small businesses to medium business. Certain clients are paying us 60 to 90 days and it's across the board. It's your small enterprises, it's your large corporate, construction companies, it is completely across the board” – Company D

The business may therefore find that a lot of their money is tied up in inventory or work in progress. This problem is further compounded when forecast accuracy reduces, which is not uncommon in a rapid growth environment, resulting in the business carrying more inventory than usual to avoid stock-outs. Essentially, the funding for working capital is exacerbated in a rapid growth environment.

“It's very hard to estimate their spend with us until the order is physically being placed. And once it's been placed, we’ve got to secure the raw materials to be able to deliver on it. So I think that's been a challenge in tying in with rapid growth” – Company D

“You are now funding 30 day accounts and you are bringing in material to make sure that you are able to meet the demand. So you are now carrying in your cash so to speak, 6 to 8 million sitting in your warehouse at any given time, and you are consistently using it but you are consistently replenishing it” – Company G

Rapid investment in CAPEX

Interestingly, not all respondents found cash flow to be an issue in the rapid growth environment. By setting up good terms with debtors and creditors, managing inventory or forecasting demand effectively some of these businesses had a healthy cash flow. CAPEX, however, was the challenge that some of these businesses faced. While any capital intensive business would require CAPEX to enable growth, a similar company in a rapid growth environment would need to source the CAPEX on a more frequent basis.

The faster you grow the more capital you need to fund that growth. This is consistent amongst most businesses.

> *"Rapid growth comes with capacity especially in my line of business. In my line of business I have to have that capacity, I have to be able to compete with companies that have been in the market for 70 to 80 years that have national coverage. So for example the client base that I'm locking in at the moment to deliver on my rapid growth has national coverage and I need to deliver on that." – Company D*
>
> *"…in terms of rapid growth, the faster you grow the more capital you require to fund that growth, and that's consistent. So if you grow anything more than 20%, your need for capital is huge because you are consistently funding it…" – Company G*

The instability and inefficiencies that rapid growth introduces came out strongly as a finding. Much of the literature speaks to the operational and managerial challenges that are associated with rapid growth and this has been confirmed in this study. The drain on cash flow was a significant finding as it sheds more light on the financial implications of rapid growth.

4.5 Findings relating to funding challenges

What are the challenges associated with securing funding for rapid growth South African businesses?

– Research Question Four

This section highlights the factors that have impeded the ability of the businesses in securing funding. The sub-themes that describe these findings are *family and owner manager impact*, *business and management profile* and *laws and lender policies.*

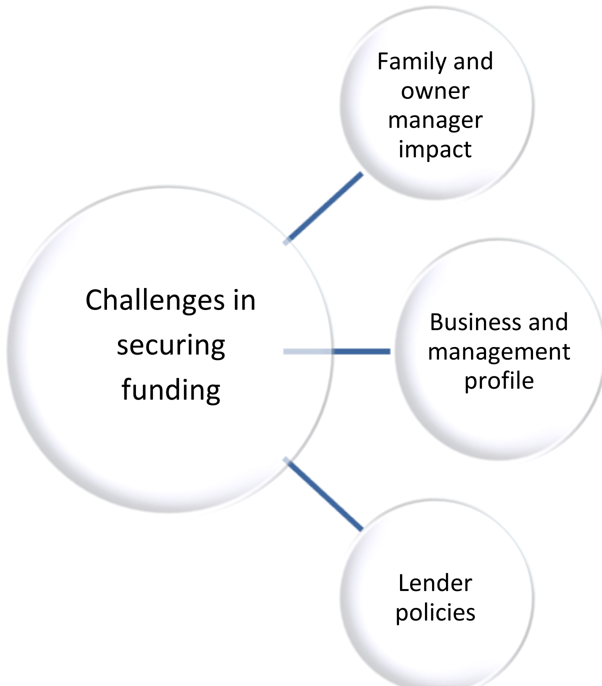


Figure 8: Challenges in securing funding sub-categories (own compilation)

Family and owner management impact

While family can be a key enabling factor when it comes to providing funds to support, it was also found that the family business dynamic can prevent the business from securing external funding which can tend to limit growth. Three of the businesses interviewed are currently owned and operated by family members with the founders still exercising a large degree of control over the organization. Businesses that choose to maintain the family orientated nature of the organisation have been found to be more conservative and tend to avoid taking on debt or divesting any portion of the business to an equity partner. This approach limits the ability of the business to secure funding or grow in line with market growth rates.

> *"On the other hand we've been too much operating as a family business, which sadly has worked against us in reaching those higher heights. They are conservative, lateral, hands on, being everything to everybody actually starts working against you." - Company C*

> *"No, it won't be responsive enough, it will limit our growth because we still won't take out debt, we still won't sign surety" - Company F*

Businesses that don't have the family dynamic but are run by the founder also tend to limit their funding options due to their emotional attachment to the business. Even though they may admit that taking on equity partners may be the best decision for the success of the business they find it difficult to take that step and tend to avoid or delay it for as long as possible. When the decision to take on an equity partner is eventually taken, in some cases, the process is drawn out due to the level of scrutiny and paranoia associated with owner.

> *"Myself, especially starting it on my own, you are emotionally invested in the business to such a degree and it's looking for the right life and I think that has been the issue that I've gone through. I've only really been looking for equity partners for the last three of years. I've been down two routes through let's say structured courtships and I just haven't found the right person, the right company" – Company D*

Business and management profile

The age and maturity of the business can be a serious impediment to growth. It was often mentioned that organizations without a strong history, or that had not yet developed enough assets to securitize loans, found it extremely difficult to secure funding from financial institutions. Despite the profit potential of the business, without a proven track record or the ability to sign surety, it is nearly impossible for a young business to secure debt finance. If the business is able to secure funding, it was found that the rates and terms are found to be unfavourable.

> *"When you start up and you need money desperately, the banks don't give you anything, and if they do, the term and the rate are a little bit punitive. So as time goes by it actually gets easier" – Company G*

> *"These are now ad hoc orders and on order, but with stock I need funding on stock, and how do you fund that if your history is not there. " – Company A*

The profile of the business as well as the entrepreneur or management was also found to be an impeding factor when searching for funding. If one operates a non-traditional business, such as the management company operating in the art industry, what may be seen as an asset to the business may not be viewed upon as a tangible asset by the bank against which security can be attained. From a management profile perspective, there appears to be a paradigm that race, age and gender can also affect one's ability to secure funding.

> *"The only problem is that in our world you can go to the bank with a house as an asset and you get it. You go to the bank with an art work and even one that has been realised that people are purchasing it, there is no way they will take that as surety." - Company B*

> *"So when you talk about your usual entrepreneurial funding, a 55 year old white women with not a lot of leverage is not very attractive" - Company B*

Businesses that have had a good track record and have managed to take on debt also find it difficult to take on further debt if they are highly leveraged. Financial leverage or gearing of a business is a key ratio that guides the decision-making of financial institutions when approving loans.

> *"You will hear over and over in terms of funding one of the words that pops out consistently is about gearing. Everything is worked on ratios and the ratio that they (the banks) worked on is too heavily geared, too heavily geared. In terms of their model of gearing that's saying you have so much debt, you are projecting so much turnover and profit...it doesn't sort of balance out." - Company G*

Lender policies

The strict policies and rigid processes of funding companies can delay or impede the ability of a rapid growth company to secure funds. Banks abide strongly by their financial models with little or no room for flexibility. They drive hard their view on the financial leverage or gearing of a business and will limit the ability of the business to take on more debt. They can also prevent the business going to another bank, in certain cases, through strict policy measures.

> *"The banks are clever, because I couldn't go to another bank while I'm operating at this bank." – Company G*

The processes of funders can also be quite onerous. It was found that institutions can drill down to bare essentials of the business such as the budget apportioned for tea and coffee. The focus that they place on the last rand and cent tends to delay the approval process.

> *"But because they look at everything from a funding perspective they look at everything, the budget works to a budget. If you say I'm going to spend R5 on tea and coffee you are not going to spend R6 or R7, and they literally drill it down to the time your machine switches on and starts running. So they look at every single cost, and understand they don't know the business but because they have*

done so many projects they understand. So that's in the phase we are now." – Company G

Furthermore, the process can be completely derailed if the business was to make changes that were not aligned to the original approval even though the business might view this to be immaterial. It could turn out to be material which is why the institution adopts such stringent processes.

> *"So from funding, the IDC signed off R37 million and we said ok we have premises in Durban, we have premises here, we were going to put it in Durban and we said it's not the right place. Durban logistically was the right place, but it wasn't for having such a huge investment, having it at such an arm's length. None of us were going to move to Durban, so we had to bring it to Johannesburg. So it meant looking at the whole thing, moving premises because the polyester line is 70 meters long, it's long it will never fit into these premises. So we went back to them and they were really upset with the fact that we wanted to move premises, even though it shouldn't have been." - Company G*

The high rates imposed by most private equity investors are not found to be attractive by many businesses. Private equity companies have been found to demand returns in multiples of what the business would pay to a bank. As a result, private equity was not commonly found amongst respondents.

> *"The problem is a lot of the guys that have private funding; the private funding rates are just ridiculous. Their requirement for return is double and sometimes three times what you get at a bank, so you avoid that scenario." – Company G*

The profile of the business as well as the strict lender policies were findings coming out of the data analysis that supports much of the theory on this topic. An interesting finding, which was not mentioned in the literature, was the impact of internal dynamics on the ability of a business to secure funding.

4.6 Findings relating to consequences of not securing funding

What are the consequences of rapid growth South African businesses being unable to secure funding?

– Research Question Five

The following section highlights the impact that the lack of funding had or could have had on the rapid growth businesses. Essentially, lack of funding limits growth, introduces inefficiencies into the business and can be risky in terms of losing current customers to competitors.

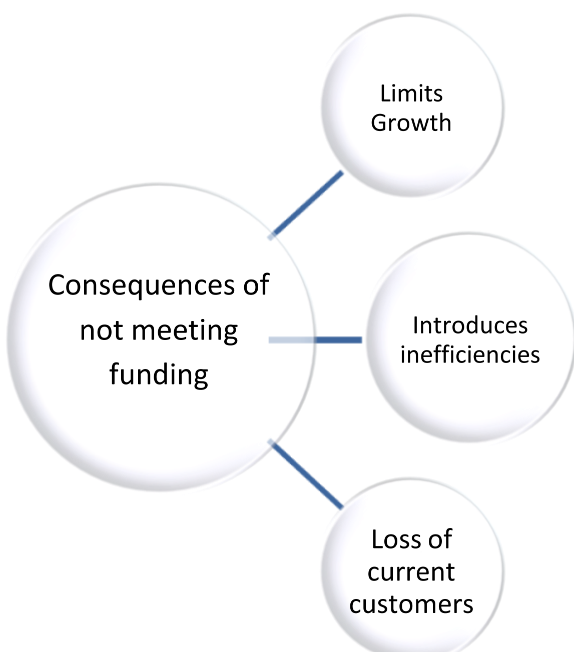


Figure 9: Consequences of not meeting funding sub-categories (own compilation)

Limits growth

The inability to secure funding will undoubtedly limit the ability of the company to continue growing. In the dynamic environment that businesses currently find themselves in it is the ability to react quickly to opportunities that will be a key driver to business success. Lost opportunities may not just be a loss of revenue but could adversely affect the business' ability to compete in an attractive market. If competitors are able to react more effectively to the market demand the result will be a loss in market share for the businesses unable to secure the funding to enable growth.

> *"It's stumped my growth, I would possibly think I could have been in growth terms possibly 6 months to a year ahead if I had the stock." - Company A*
>
> *"We've taken longer to take advantage of certain opportunities. I would have liked to be involved in the art fair a couple of years ago, because the market was a lot more robust then. We've done a lot on instinct and review, so its strategy, and maybe again we haven't moved so quickly. But again the last year we haven't been able to move as quickly as we wanted to. My original plan would have been already half way in action if we had just started with my new growth plan in January." - Company B*

Loss of contracts/customers

Besides limiting growth, the inability to secure funding to enable the growth may lead to loss of customers if the growth comes from a few large contracts. The inability to effectively service a contract or continue to meet the increasing customer demand will lead to the contract being awarded to competitors when it is up for renewal.

> *"We made a mistake once, we sat with one of our very big customers and we said we can't fund bringing this stuff in for you, you bring it in and we will convert it. The guy got a fright because gee are you having cash flow problems, and are you not going to be here anymore?" – Company G*

"(Could we lose market share?) Oh absolutely. The playing fields that we are involved in are basically with are primarily global companies in terms of competitors. So the majority of our competitors would probably have more accessible capital funding than we would, and that could to some extent obviously influence our growth." - Company I

Inefficiencies

Like rapid growth itself the inability to secure funding can also introduce inefficiencies into the business. Businesses have had to make do with existing assets to meet growing demand. The equipment may not have had the capability to deal with increased volumes which has led to operational inefficiencies.

"It's probably meant that our replacement programme is 6 months behind from where it should be." - Company E

The lack of buying power affects the ability of the business to negotiate good rates with suppliers which can reduce profitability. Funds are required if businesses want to capitalise on the economies that scale produces. Purchases in small quantities or through the use of intermediaries increase the unit cost of supplies.

"And also it has hit our efficiency, so what I mean is we are not able to, without decent funding, negotiate better rates with our clients to bring in higher volume products from overseas, so we are relying on a lot more local suppliers. I just did a recent trip to China where I managed to secure bulk supplies of raw materials that I could bring in. But with the funding I haven't been able to ship it in and hold it as stock and be able to draw from it. So now I'm using their middle man who is in the position to do that, and I'm paying a premium for that." - Company D

The lack of funding will not always lead to business failure. It was found that businesses may continue to endure but the lack of funding will impact on growth and may introduce inefficiencies into the business.

4.7 Findings relating to tactics

What are the funding strategies and tactics adopted by rapid growth businesses in South Africa?

– Research Question Six

This section highlights the tactics employed by the rapid growth businesses to leverage the sources of funding that they have selected.

Figure 10: Tactics sub-categories (own compilation)

Operational Efficiency

The most useful tactic employed by the various businesses to leverage cash flow or minimise the use of an overdraft as a source of funding was to improve operational efficiencies. The business would seek to do this through a reduction in the cash conversion cycle or through the reduction in working capital.

Lead times on production processes were significantly reduced through the investment in high-tech machinery. The introduction of technologically superior equipment meant that production times could be reduced by multiples, which has a positive impact on the time the cash is sitting in working capital, resulting in a reduction in the funding gap of the cash conversion cycle.

> *"We brought our first machine in, a slitter, it honestly revolutionised what we were doing. Where we were running at 60 metres a minute, that's how we would cut the polyester. We went from 60 meters a minute to 300 meters a minute. The Taiwanese were fantastic, they backed it up, they had people on site when we installed. Any problems we had we literally plugged in a modem, Skype and it generally worked very well. We still have a very good relationship with them" – Company G*

Companies switched from the cheaper imports to locally manufactured supplies to improve cash flow. The benefit of cost reduction that imports presented was outweighed by the excessive lead time to bring the product into the country. By hosting the fabrication locally the business' cash cycles have been significantly reduced and are under much tighter control enabling the business to keep the operation running smoothly.

> *"That line we started in 2005, and what we initially did was we brought the trailers in from China and we were just assembling them and then we found that that was a very long cash cycle and that was about a 4 month cash cycle. Now we*

are getting them produced locally, we are getting steel out of our steel manufacturers, so our cash cycles are right there. We've got guys fabricating right on us, and we pay them 30 days, so that also manages to keep our wheels turning on the cash flow side." - Company F

Reducing working capital was the second part of the equation that improves cash flow. Companies have invested in skills within the business to improve forecast accuracies and significantly reduce stockholding thereby reducing the working capital requirement while managing the risk of stock-outs that could jeopardise the operation of the business and associated businesses within the supply chain. Companies have even managed to completely eliminate inventory through the successful implementation of the Just in Time (JIT) principle.

"We've cut down substantially on stocks without jeopardising the business in any way. So we plan very carefully and very actively. We put a lot of pressure on ourselves to give accurate forecasts and we plan according to those forecasts, and we buy according to those forecasts" - Company H

"we really worked in just in time, and me being from logistics I worked very strictly in terms of just in time, so in terms of the shipping and we knew when they produced it, so we estimated consistently. So it became so close, and even in today's time, a container arrives, it's converted and it's gone. It never really sits on the floor" – Company G

On the procurement side companies, that were able to do so, shifted a lot of the cost of holding stock onto their suppliers. Instead of taking large, infrequent deliveries the business forces its suppliers to carry the stock and take small, frequent deliveries. Strict service level agreements are used to ensure that suppliers are able to maintain the necessary stock levels to ensure the business demands are met. The suppliers, essentially, become partners to the business but such a relationship can only be negotiated when a business has strong power within the supply chain.

> *"We've done quite a bit on the procurement side, what we've done there is we've shifted a lot of the cost of holding stock to our supplier...so that reduces the burden on us, we don't have to hold that much stock, because we know our suppliers are holding stock on our behalf…So just to reduce risk and to allow us to cut our stock holding because our supplier is now more a partner to us and is taking and sharing some of the risk with us" – Company H*

Within the consulting environment it was found that, as one was selling time, income could be significantly boosted if the time could be sold to multiple customers at once. Increasing the efficiency of the consultant's time, in such a manner, helps to improve the cash flow of the business.

> *"The one thing I figured out very quickly in doing that, and it's not different in the art market, it's the traditional kind of speaker's route. The guys who become experts on.... and then sell their time via seminars or via speaking etc .It's actually hugely profitable in the sense that if you are doing the repeat opportunity at different audiences, so I'm selling the same time to 40 people in the room, and my preparation is limited." – Company B*

Effective Planning

Effective budgeting can ensure that the business has adequate time to develop robust business cases to secure funding from financial institutions. Businesses that are able to project future cash flows are able to understand the timing and level of funding required and as such can prepare adequately to ensure that the issues are addressed ahead of time with the banks.

“So in terms of running a budget or cash flow projection, it's highly, highly, highly important for any small business to look forward unless you are so cash positive that it doesn’t matter. So we look forward and come this month we know we might have a problem, so we will already address that 2 or 3 months before the time with the bank.” – Company G

Understanding the movement of cash in and out of the business and the flexibility involved in the procurement and manufacturing and the effective scheduling thereof can enable the business to minimize the use of external funding. By scheduling expensive purchases in the months that the business receives a cash injection enables the business to manage the funding gap

“What we do is we schedule our expensive purchases, and the only expensive purchase we need is steel right at the beginning. The rest of it we can schedule 2 weeks before it goes out. So we are able to get the expensive stuff in the same month that we get paid, and then we pay 30 days after that. So it's just the steel that is lagging, but it generally comes in the same month that we get paid” – Company F

Businesses that could determine their Sustainable Growth Rate (SGR) and managed demand to fit into that SGR were able to manage the rapid growth without steering the business into trouble. Businesses would have to generate high profit margins and would require minimum investment for growth to have a SGR greater than 20%, however, the ability to measure and track against this key performance indicator limits the business’s exposure to cash flow risk.

“One of our key performance indicators is sustainable growth, not growth. So we are basically looking at 20% sustainable growth.” - Company I

Outsourcing of Labour

It was interesting to find that outsourcing of labour was common practice amongst the rapid growth companies. The impact on cash flow associated with rapid growth demanded a delay in payout of operational expenses wherever possible. Outsourcing of labour provided this relief as labour brokers or contractors required payment on terms versus the weekly wages or monthly salaries that one was obligated to pay if the labour was employed internally.

> *"I can manage my cash flow better with them because they (labour brokers) would invoice me once the job is complete. And instead of having my own staff with that fixed monthly cost...so what would happen is they would get paid when I get paid, and that is how I've tried to manage the funding on that side" – Company D*

The additional benefit of outsourcing of labour is that it also enables the rapid growth company to scale quickly to meet the rapidly growing demand. Companies have also outsourced labour purely for the flexibility that it provides. Where intra-year demand is volatile, outsourcing of labour allows the company to mitigate the risk associated with paying employees during idle periods

> *"Because we sub contract, it is easily scalable. We sub contract most of our work and even where we didn't sub contract, we were forced to do so with the one product. On the one particular product we free issue the raw materials and we pay for labour" - Company I*

> *"If I don't get the order I don't pay for a labourer to stand around with a welding machine, so I've decided to go that route." – Company A*

Cash cow product lines

An interesting finding was the cross-subsidisation tactic that businesses employed to support the core business. The long cash conversion cycles associated with the core business often means that the business is at risk of being liquidated if external funding cannot be secured. To improve cash flow within the business, some companies have created alternate product lines that operate on a much shorter lead time than the core business and churn out cash quicker than the main product lines. The margins might be lower but the cash generated by these secondary lines was used to fund the working capital and operational expenses of the core business. Some businesses have used such a technique as a means to avoid taking on debt finance and this, essentially, is a bootstrapping technique.

> *"Two years ago having analysed my cash flows, I had a look at my cycles of sales through to payments. In order to try and shorten that period to free up cash flow for future growth, I diversified into a point of sale line...so the margin is a lot smaller, the volume is a lot higher, but your sales to payment time frame is a lot shorter and it frees up a lot more cash flow for us" - Company D*

> *"We've also tried to establish separate lines, we've got a separate line running through at the moment, it's on a much shorter lead time than the others, it takes us a week to complete a trailer. We put in 50 hours into a trailer instead of 400 hours into the main trailers. What we've done is we've sub-contracted the work out, and we pay those guys on 30 days. It a low margin unit, we absorb a low margin, but we turn them out quicker. And if we didn't have that line this year, and we've got some big trailers going through this year, we would have run into some serious cash flow and profit issues." - Company F*

Debtor Days

To ensure that the creditor days, as a source of funding, was used effectively businesses needed to ensure that their debtors paid them as soon as possible so as not to offset any benefit derived by paying creditors later. So focus on management of debtors was a key imperative to ensure that cash flow was effectively managed. Aggressive credit policies were effectively used by companies to reduce debtor days and increase creditor days in certain instances.

> *"We've got our debtors down to 34 days, and on that sort of book, with that sort of turnover you don't find too many companies with that, and our bad debts are basically zero. Again it's through very aggressive credit policies and management of the debtors' book and that sort of thing. That's really the secret of our success in terms of cash generated, is the working capital, it's the bread and butter of the business" – Company H*

Leveraging external relationships

The relationships that businesses have established with providers of funding can be strategically leveraged to ensure that the business maximises the value derived. From a banking relations perspective, certain companies have opted to deal with a single bank and develop a strong relationship which they have found to benefit them in terms of the deals that they have negotiated. In order to strengthen the relationship with the banks, these companies found that maintaining complete transparency and involving the bank more with the business proved to be quite effective.

> *"I've seen it with myself with certain relationships with the bank I get a certain deal, and I know it's a different discussion, but acquiring these partners, the funding and arrangement rates are day and night from a funding point of view" - Company C*

> *"So the only tactic that we have tried differently is more transparency, we try to get them involved more in our business. A lot of times the banks insist you visit them, we insist they visit us, let them physically see, and it unquestionably changes their level. Sitting in an office their level of your business is based on*

> *your financials. Coming to your business, seeing the business in operation, seeing what you are producing." – Company G*

Tax Avoidance

Tax has a negative impact on profitability of a business and avoiding tax seems to be a tactic that a lot of companies seem to employ as far as possible without impacting on the business' ability to secure funding. The avoidance of tax through the investment of any operating profit into growth has the benefit of limiting the amount of money paid to the receiver of revenue but can be a double edged sword in that a company reporting small profits or losses, as a result, will struggle to secure external funding in the near future.

> *"With a private business, you can limit your exposure in terms of paying millions on millions on paying it on tax, and re-invest your money." – Company G*

Value Added Tax (VAT) also imposes cash flow issues for certain companies and one of the companies highlighted the use of a second company, which is not VAT bearing, that they use tactically to manage operating expenses when dealing with clients that are not VAT vendors.

> *"The other issue with VAT is where we are dealing with VAT vendors it's fabulous we can claim VAT, but where we are not dealing with VAT vendors it pushes up the price of the product significantly. So you are dealing with a museum budget and it goes to R14 000 over a budget of R100 000. So we have actually established a second company, we do have some equity which is great. One companies is VAT bearing and one is not, so when we consult to private artists we don't have to charge VAT, so in a way I've cut the operating expense issue" - Company B*

Securities

In order to secure funding from financial institutions some form of security is required. Companies have found effective ways to leverage assets as security to achieve higher loan amounts. Using property as security can be far more effective than using depreciable assets as security.

> *"if I go and buy a building of R2 million for instance and I put my million down, I owe a million on it but the bank sees value of two million now depending where we sit, or they could see a value of R2.5, it's a tangible asset, they know they can attach something. But if I go and say I've got a million bucks, I need to buy equipment and I need another R500 000, they are going to say but the machine or the equipment or the stock that you buy is going to devalue so quickly, I'm not going to loan you R500 000 on that." – Company A*

Companies with strong turnovers have successfully managed to leverage their debtors book as security against loans from financial institutions.

> *"So I've been in a very fortunate position that my turnover has been such in terms of growth that I was looked on favourably by financial institutions. So initially for the property I had a book, so I ceded my book pretty early in my negotiations with the financial institutions, but I think they tend to do that. So my book has always been favourable and they have always asked for a loan value for 50% of my outstanding book" - Company D*

The study has uncovered rich findings within the theme of 'tactics'. There have also been some interesting findings such as the cash-cow product lines. The findings will help to partially fill the significant void in the literature relating to this topic. All of the findings provide useful and practical insights for rapid growth businesses.

4.8 Emerging theme: Factors enabling the business to sustain rapid growth

This section highlights the factors, both internal and external, that enabled the businesses to sustain rapid growth without the need for external funding. The findings of this section are important as they provide insight to the environmental conditions that allow a business to flourish when faced with a rapid increase in demand.

Figure 11: Enabling factors sub-categories (own compilation)

Capacity and capability

Mature businesses or businesses that had managed to develop adequate capacity in terms of infrastructure, operational practice as well as functional practice ahead of the growth curve were well poised to tackle the rapid growth. The increase in demand did not affect the stability of the organization as the organization was structurally capable of accommodating growth without a significant need for funding.

> *"So I think the rapid growth has allowed this business to realise it's true potential going forward, and we need to continue with that rapid growth because we've got the infrastructure, we've got the capacity, we've got the area, we've got the warehouse and it's all paid for in the sense that we don't have huge loans with the bank. So if anything we need to fund, which might be product, we can do that with securities we have around this business." – Company C*

The infrastructure and capability developed by businesses also makes them look more structured and reliable in the eyes of lenders which lowers their risk profile and promotes the ability of these businesses to secure external sources of funding.

> *"I think the more the business grows and the more the institutions see structure and reliability and your payment profile is acceptable, the funding becomes easier to obtain." – Company E*

Businesses that had naturally developed a highly responsive management culture where decisions were taken quickly were also able to effectively exploit increases in demand. Maintaining a dynamic organization is a strong capability that will enable any business to survive in the rapidly changing environment that a business may find itself in today.

> *"No, not at all and also because we are a private company and our decision processes are very quick. We don't have to go through all sorts of rigmarole to get decisions made. Our board is a fairly small board so we don't need too many levels of approval. So for example a capital expenditure decision is a couple of phone calls away. We are very aggressive in terms of our growth strategy and fortunately our shareholders are happy to support that strategy." – Company H*

The entrepreneur's or management credential also falls under the ambit of capability and can be an enabling factor during growth. Entrepreneurs with strong credentials are looked upon favourably by financial institutions. It would appear that a good track record and a history of business management are looked upon positively when attempting to secure loans.

> *"I had a good history in terms of corporate. I had been in trucking, road freight, I was the managing director of a company. In total I was there for 11 years, 8 of which I was the managing director. I had a good track history so the bank was very happy to look at me being the main person and obviously being the older of the two partners" – Company G*

Strong cash position

Businesses that have maintained a conservative approach over the many years, through the holding back of dividends or limiting the amount of withdrawals by shareholders for luxury purchases, managed to build up a strong cash position. Money in the bank provided these rapid growth businesses with a comfortable buffer against the demands associated with rapid growth. The cash could be used for capital purchases, operational expenses as well as managing the funding gap. It can take many years for a business to reach such a cash healthy position but once in the position it is very difficult for the business to crumble under the strain of rapid growth.

> *"Don't spend money on non core issues. **** is incredibly conservative this way. You don't see Porsches and luxury villas and aeroplanes and crap like that. Your spare cash, there is a certain amount that he wants as a back stop, and the balance is put to aggressively pay for assets" – Company E*

> *"So that conservative view and management style over the years has helped us nurture the business to allow us rapid growth in sales and marketing which we only realised now is the key to our success. So I think without having that*

background of conservative building slowly and acquiring this slowly over 20 years, you wouldn't have allowed that rapid growth." - Company C

Funding support

Family support has been a key enabling factor for a number of businesses in ensuring that the transition through the rapid growth phase was a smooth one. Companies that have had support from "sister" companies due to family relationships have managed to minimize the need for working capital funding enabling them to endure rapid growth easily. Entrepreneurs were also provided loans by family which enabled them to set the company up and also manage cash flow during periods of instability.

"But like I said, this business being unique and having the surrounding sister companies around us that have been here for a long time has provided a solid foundation to allow that rapid growth. From a funding point of view, from a service point of view and just from an infrastructure point of view. If these businesses had to be done at a rapid growth now there would be a huge amount of debt " - Company C

Structured rapid growth

Rapid growth can create instability in the business as was highlighted earlier. However, it was found that a good, structured growth can be managed relatively easier. The predictability of the growth allows businesses to forecast demand, inventory, operational and funding requirements with a greater degree of accuracy which makes planning easier. Businesses dealing with the manufacture of consumables found that the repeat business made forecasting simpler. It is the rate of growth of the customers segment of the market that drives growth for the supplier.

"It (rapid growth) is pretty stable, we are in the business of… it's not really capital equipment that we manufacture but consumables. So for the miners to continue

they really need our product and they need to continually replenish stocks of our product…so it's a repeat business, it's fairly predictable. We can forecast with a reasonable amount of accuracy what our sales are going to be and what stock we need to hold etc, so it makes planning quite easy.“ – Company H

Customer and supplier profile

As highlighted earlier, developing and leveraging relationships with banks as well as customers and suppliers can be a useful tactic. The nature of the industry and the profile of the customers and suppliers that businesses deal with, by default, can provide businesses with the support they require to endure the challenges associated with rapid growth. Large customers who could pay large deposits without a fuss proved to be a key factor in funding working capital. In contrast, dealing with smaller customers whose sole objective is to pay as late as possible can land the supplying business into serious cash flow issues.

“They don’t even blink an eye. We are dealing with guys like Anglo American, Sasol, if they want the equipment they pay the deposit, for them it's not a lot of cash. We haven’t had any issues with guys paying deposits, and that's with mining trailers in mining houses, so it's done us well” – Company F

Businesses would not, typically, be able to push the stockholding burden onto their suppliers as the suppliers would avoid increasing their own working capital. However, companies with a favourable position within the supply chain and who purchase a large portion of the suppliers output can leverage the relationship and share some of the risk such by pushing stockholding back onto the supplier. This enables the business to manage working capital more effectively in a rapid growth environment.

“So we give them big volumes, we give them consistent volumes because of the nature of our business, we can give them an order of 1000 every month, so they know they can rely on our business, it's almost like an annuity income, it's

> *consistent business and long production runs, so we are an attractive customer to them. And we say to them if you want us as a customer these are the benefits for you but you need to share some of the risk as well." - Company H*

Low Cash Conversion Cycles

Working capital was a central challenge across all the rapid growth at some point during their development. Some of the businesses have, tactically, managed the level of working capital down but for some the nature of the industry and supply chain will always lead to long cash conversion cycles. As such businesses with inherent low cash conversion cycles faced lower risk during rapid growth and are able to reinvest to scale the business during growth.

> *"The business is in a fortunate position, it's got a strong cash flow internally, and that is through really strict working capital management as well. So we are very careful with managing our working capital and a large part of that capital is reinvested into the business for growth." - Company H*

Niche markets

A fast growing and profitable market is an attractive market and competition will increase as companies raise their profile and become noticed. Where competition is already rife, the pressure on businesses to develop the capabilities to meet the growing demand is extremely high. Failure to do so will result in a loss of market share. The room for error is marginal and the probability for errors is high when the business is unstable. Companies in niche markets, however, have some breathing room and mistakes or low response times may not be detrimental to the business as the business does not face the risk of losing market share to competitors. One should not become complacent, as competition will materialise, however operating in a niche market is certainly a key enabler.

*"***** is a world leader in explosion proof hoists, not many other crane companies have the knowledge, the technology and the manufacturing capability of what they are doing. What they are doing is they are manufacturing 100 a year, ***** is doing 5000 a year of the explosion proof hoists, so it is a niche market in that instance." – Company A*

The findings contained in this section highlight the underlying factors that have enabled many of the businesses to endure and grow. Some of these factors may be controllable and others may not be. The findings will provide key insights for other rapid growth businesses and help them define their own inherent enabling characteristics.

4.9 Summary

A wealth of information has been extracted from the companies interviewed. The maximum variation sample has ensured that there was no bias to any particular sector or business stage of growth. It was interesting, therefore, to find that many of the challenges and solutions applied by the businesses are common across both small and large businesses. The data has produced findings for all of the research questions posed with a wealth of information found within the themes of 'sources of funding' and 'tactics'. Many of the findings have not been explicitly mentioned in the literature and there are key findings such as the bootstrapping behaviour of larger firms that are new and interesting.

The emerging theme 'factors enabling businesses to sustain rapid growth' provided key findings on the underlying factors that have enabled many of the companies to exploit the rapid increase in demand.

5 INTERPRETATION OF RESULTS

5.1 Introduction

The following section summarises the interpretation of the results produced from the data analysis. The findings, in the previous chapter, highlight key points related to the research problem but this section takes these findings to the next level of abstraction and seeks to determine what the findings really mean.

5.2 Critical finding and theory proposition

The goal of the research was to identify the funding strategies adopted by businesses at various stages of development in South Africa. With strategy being the operative word, it was interesting to find that the majority of the businesses did not, in fact, have a strategy when it came to the funding of their ventures. A strategy is, essentially, a pattern or plan that integrates the organisation’s major goals, policies and action sequences into a cohesive whole (Louw and Venter 2006). One should have a view of the future and a strategic view of the internal and external environment in which it operates. In order to do develop effective strategies entrepreneurs or management need to develop a strategic mindset. According to Liedtka (1998) a strategic thinker has a mental model of the complete end-to-end system of value creation, his or her role within it, and an understanding of the competencies that are contained within it.

However, from the outset it became evident that the majority of the entrepreneurs in this study did not display this strategic mindset within the context of the funding of their business. This is in contrast to the theory which states that the entrepreneur appears to be one who specifically intends to grow his or her business utilising strategic management as a method to facilitate and enhance growth and profit-making (Carland et al 1984; Naude 2010; Chan et al 2006; Gundry and Welsch 2001). Funding within the business appeared to be more of a reactive process than the formulation and development of a well researched strategy.

How then do businesses without a strategic approach to funding manage to endure and prosper within the rapid growth environment? Perhaps it is the intelligent opportunism that good entrepreneurial type businesses seem to possess. Intelligent opportunism is a competency which means being responsive to good opportunities (Liedtka 1998). This is a competency that even strategic thinkers should possess as using a well articulated strategy to channel organizational efforts effectively and efficiently must always be balanced against the risks of losing sight of alternate strategies better suited to a changing environment (Liedtka 1998). In order for businesses to demonstrate this intelligent opportunism the environment needs to present such opportunities. As such, the theory emanating out of this research is that rather than a well articulated funding strategy, there is a set of prevailing circumstances, sometimes unique to the environment a business operates in, that enables the business to fully capitalize on a rapid growth in demand. The literature by Nichter and Goldmark (2009) that refers to external factors driving rapid growth supports this theory.

Before this theory is further contemplated it is important to analyse the development of the business through the various stages of growth and the impact of the rapid growth environment.

5.3 Analysis of findings

Stages of growth

While the Greiner model (Scott and Bruce 1987) was adopted to categorise the businesses interviewed it was found that none of the businesses “neatly” fitted the distinctive stage of growth model and it was apparent that the organizations did not follow the sequence and order of the predetermined stages. The findings support the literature by Levie and Lichtenstein (2010) and Jacobs et al (2011) who criticise the practicality and lack of empirical evidence underpinning the theory on stages of growth models. The dynamic states approach proposed by Levie and Lichtenstein (2010) in the literature appears to be supported by the findings in this study. This approach states that organizations will most probably grow in a series of configurations and that there can be any number of dynamic states in an organization's existence and these can occur in any sequence.

This explains why a young business with only 10 employees does not display "survival" characteristics but displays "expansion" characteristics associated with a more mature business. Or why mature businesses display bootstrapping tactics commonly associated with a business at start-up or survival stages. The implication of this is that the stage a business will find itself in as it grows is not necessarily recognizable or predictable. This makes strategy development even more difficult and the competence of intelligent opportunism becomes even more significant.

Impact of rapid growth

Rapid growth adds to business uncertainty. While businesses have found that a good structured growth can enable them to forecast easily and gear the business effectively, rapid growth in itself as well as the impact it will have on the business is an area of uncertainty for many businesses.

The findings reveal that two things are certain, however, and that is rapid growth will create instability within the organisation and introduce inefficiencies for businesses that grow at a pace faster than they can restructure. This confirms the literature which states as a result of the constant change rapidly growing firms cannot realize the efficiencies that are enjoyed in more stable environments (Fischer and Reuber 2003). Fischer and Reuber (2003) go on to highlight that cash flow presents a serious challenge in a rapid growth environment and working capital requirements erode the profits generated by growth.

The findings support this argument as respondents, faced with cash flow challenges, have had to move to more flexible sources of supply which reduced the businesses cash conversion cycle but reduced profitability as a result of higher unit costs. The frenetic pace of growth has also meant that businesses have had to take quick decisions, and not necessarily the best, and have had to stretch resources resulting in a reduction in efficiency.

Funding requirements

The funding requirements for rapid growth business are essentially the same as the requirements for any business funding growth. The increased business activity will see an increase in operational expenditure, growth will require capital expenditure to expand the property, plant and equipment and increased volume will mean an increase in working capital. Rapid growth appears to merely exacerbate the funding challenge as funds will have to be secured and spent faster than usual. The interesting finding is that working capital and cash flow is the key funding challenge in a rapid growth environment. The working capital requirement is found to be higher than it would be in a normal growth environment due to the following features:

- The instability and uncertainty associated with a rapid growth environment means that businesses tend to hold more inventory to buffer against the instability.
- Businesses have had challenges converting orders into sales, due to a lack of capability, resulting in excess work in progress.

- The instability within the organisation creates a lack of focus resulting in debtor days' creep.
- The inefficiencies introduced into the system due to the pressure to take quick decisions have come at a price.

The working capital challenge was a central challenge for all the businesses and all have had to manage, or have indicated that they will have to manage, it at some point. The basic features of the Greiner Model (Scott and Bruce 1987) highlighted working capital to be a challenge during the earlier stages of growth. The findings, however, have demonstrated that even the most mature company interviewed has found working capital to be the most significant financial challenge. Scott and Bruce (1987) also stated that stage 1 companies' funding requirements are largely capital in nature, however, in contrast to the literature the nature of the industry and the business model dictates the level of funding rather than the stage of development. This once again highlights that the Greiner Model (Scott and Bruce 1987) is a conceptual model which does not accurately reflect the chaotic reality of business development.

The business environment has changed drastically over the last 20 years and the use of the internet alone has created a fundamental shift in the way we do business. Technology has also ensured that a start-up business can very quickly develop the systems and operate under the same processes and model as a mature business that has been around for a long time. Entrepreneurs can also run multi-million Rand businesses from their garage or acquire a mobile office service through companies such as Regus. As such, dynamic state theory as described by Levie and Lichtenstein (2010) is much more relevant to the modern day business.

Sources of funding and challenges

The findings have illustrated a number of sources of funding that the rapid growth businesses have utilized through their development. During start-up, entrepreneurs have been found to bootstrap the business to get it going. The entrepreneurs have used "owner financing methods" as described by the literature (Winborg and Landstrom 2000).

A very interesting finding is that while bootstrapping is commonly associated with businesses in their early stages of development, bootstrapping was found to be employed by some of the larger companies, including the largest company interviewed. Some of the larger business have minimized accounts receivable through aggressive discounting, have sought to delay payments to suppliers and have pushed stock back on to suppliers where possible to minimize stockholding. The literature classifies these three groups of bootstrapping methods as *minimization of accounts receivable*, *delaying payments* and *minimization of capital invested in stock* (Winborg and Landstrom 2000). Many of the companies have looked to satisfy their resource requirements without relying on long-term external finance, which bootstrapping is essentially about. Free cash flow or retained earnings is the preferred source of funding for many of the businesses. This supports the Pecking Order theory (Watson 2006) mentioned in the literature.

The smaller businesses, that do not have strong cash positions, were eager to take on more debt but found it difficult to do so without having a strong business history or assets to offer as collateral. Datta (2010), in the literature, confirms this finding and describes why the formal credit sector despises lending to small businesses. Some of the medium sized companies, even with strong cash positions, saw equity partners as a key source of funding. They believed that the equity partners would not only provide a cash injection to the business but would also bring in the skill-set and resources to take the business to the next level. This is, perhaps, one of the rare, truly strategic funding decisions taken by a respondent.

Another key insight was that none of the companies made use of private equity as a source of funding. Some opposed the use of equity funding while many were not aware of private equity firms or the benefits that this sort of funding could provide. It is evident that there is more that private equity firms could do to raise awareness within the market.

While much of the literature highlights the size and formality of the business as impediments to secure funding it was interesting to find that there were other behavioural factors that have inhibited the business's ability to secure either debt or equity finance. The family business dynamic and the emotional attachment of the owner manager to his business has been a major inhibitor to taking on either debt or equity finance. These have been driven by either the risk-averse nature of the family business, and the associated perceived risk of debt financing, or the desire to maintain full control and ownership of the entity than to sell off shares for an injection in cash.

Firms may have low debt ratios because they have little need for external capital, which is a demand constraint, or is liquidity constrained, which is a supply constraint. This supports the literature (Peterson and Rajan 1994).

Capital structure

Interestingly, even when securing equity was known to be the best decision for the business in the long run, (owner) management found it difficult to give up shares within the business due to their emotional attachment to the business. Family businesses also found it difficult to take on debt finance when it was needed due to the risk-averse profile that seems to be prevalent within these types of businesses. The decision to take on debt or to take on equity is a capital structure decision and the above findings echo the literature of Romano et al (2000) who state that the capital structure decision is influenced by the owner's attitude towards debt, risk propensity as well as the owner's need to be in control.

The literature also suggests that there is an optimal capital structure that maximises value of the company and that management aims to maintain this target debt-to-equity ratio which is based on the effects of taxes, agency costs and costs of financial distress (Romano et al 2000). This is referred to as the Trade–off theory and contrasts the Pecking-order theory mentioned earlier. Faulkender and Petersen (2006) add on to this theory by stating that firms with greater tax shields of debt, lower costs of financial distress and favourable mispricing of debt relative to equity are expected to be more highly levered.

The fact that nearly all of the businesses interviewed could not articulate what their target capital structure was and that the resultant capital structure was largely driven by emotion or a result of the most convenient funding decision brings into question, once again, the strategic orientation of these businesses.

To be fair, an optimal capital structure may not be a key driver for success in a rapid growth environment which is characterized by management complexity. The businesses acknowledge that changes in management structure and processes are central to the rapid growth challenge. This finding confirms the literature which states that change management is a key component enabling the business to sustain growth (Scott and Bruce 1987). The capital structure decision and the trade-off theory is essentially an optimization exercise. If we were to entertain the features of the Greiner model as depicted by the Scott and Bruce (1987) we will find that optimization is a feature of a stage 5 business. A stage 5 business is a business at maturity which none of the respondents claimed to be at.

Enabling factors

So, if not a result of key strategic decisions, what were the underlying factors that enabled these rapid growth businesses to secure funding or survive the rapid growth without the need for external financing?

Where the businesses had the necessary *capacity and capability* before the rapid growth curve commenced, this proved to be a key enabling factor. The literature, Nicholls-Nixon (2005), argues that rapid growth may be dealt with more effectively by developing the necessary knowledge and resources ahead of time before the pressures of growth forced a reactive response. This was supported in the current study as businesses who had developed adequate capacity from an operational perspective and those who had developed adequate capability from a management perspective were able to deal with rapid growth much more effectively than they would have been able to if they were to take a reactive approach.

The decision to increase capacity and improve capability, as highlighted in the findings, were not necessarily decisions taken in anticipation of rapid growth. Building excess capacity into the business may have been a conservative approach that meant that business would have been running inefficiently with a relatively low return on assets for many years. However, this has worked in the favour of businesses in a rapid growth scenario. A *strong cash position,* like a business with surplus capacity, is a function of the historical practice of the business and is a fortunate position to be in during a rapid growth phase. While most companies are battling to secure funding and having difficulty in managing the increased working capital challenges, companies with a strong cash balance have a comfortable buffer against the financial demands of rapid growth.

Based on the findings under enabling factors, it could be argued that when faced with rapid growth, businesses should only decide to grow once they have the adequate capacity and capability. This brings us to the next enabling factor – *low competition*. In the highly competitive business environment that most businesses operate in today, one does not have the luxury of delaying their response to the market's demands. The failure for one company to capitalize on growing market demand is the opportunity for many others. Operating in niche markets has therefore proved to be another enabling factor as highlighted in the findings. However, the stronger competition becomes the greater the risk is for the business that is slow to respond or chooses to remain at a constant level of output.

Foster and Davilla (2010) support the view that growth attracts attention and encourages new competition. The lack of competition has clearly provided breathing room for certain large businesses who, clearly stated, that they don't really have a strategy for the future and pretty much operate the way they always have over the years. These businesses have not placed any focus on creating a clear competitive advantage, however, do not lose market share when they cannot immediately respond to the market demand. A highly competitive market will create stress for management of such businesses.

Even when businesses decide that they need to react quickly to the market, funding may not always be readily available. The third enabling factor was found to be *funding support*. It was found that companies that used funding support from family also made use of this funding support during rapid growth and expansion which proved to be a key enabler. This confirms the literature which suggested that family, friends and relatives were more likely to be used by rapid growth businesses during start-up although there were no significant differences in the utilisation of that source during expansion (Gundry and Welsch 2001). This supports the key finding in that businesses will choose to bootstrap their business for as long as they are able to find means to do so.

It was highlighted earlier that the funding that businesses required was most common for working capital which appeared to be the most impacted area as a result of rapid growth. While working capital posed a serious challenge for many businesses, for some it was no challenge at all. This was an interesting insight. Businesses with *low cash conversion cycles* or even negative cycles appeared to be very comfortable within the rapid growth environment. Some of these businesses had taken active steps to reduce their cash conversion cycle, which was another rare strategic funding decision, and they had managed to do so successfully.

The nature of certain industries provides the opportunity for optimizing this cash conversion cycle. Some have seized these opportunities while others have not. It is important to note that for some businesses the nature of their industry, or the size of the business within the supply chain, does not provide it with much opportunity to reduce their cash conversion cycle. They have to look for creative ways to manage their cash flow issues which further increases the management complexity associated with rapid growth. Also linked to the nature of the industry are the *profiles of customers and suppliers* which have also proved to be a key enabler of managing the cash flow challenges of some businesses.

Along with the last enabler, which is *structured rapid growth* these factors have provided a platform which the businesses could leverage rapid growth off, and is the underlying reason for the success of these organisations. In the literature Nichter and Goldmark (2009) highlighted vertical linkages, horizontal linkages, supporting markets and contextual factors as factors driving rapid growth. These are largely external factors and some of the enablers highlighted do fit into two of these categories. The remaining enablers driving rapid growth are internal factors and were not mentioned in the literature.

Table 4: Management control over enabling factors (own compilation)

Can control	No Control	Can mitigate
Capacity	Strong cash position	Cash conversion cycle
Capability	Funding support	Competition
	Vertical linkages	
	Cash conversion cycle	
	Structured market growth	
	Competition	

The enabling factors may be defined as controllable or uncontrollable as illustrated in the figure above. Management have direct control over the capacity and the capability of the business and can choose to gear the business ahead of time. The rest of the factors are not in control of the management and is a function of the nature of the industry, the nature of the business and resources available to certain businesses. Two uncontrollable factors can be mitigated through the use of different tactics.

Tactics

Although not displaying a strong strategic orientation, many of the business did employ effective tactical manoeuvres to manage the financial requirements of the business. To reduce working capital and improve their cash conversion cycles businesses have used aggressive discounts on credit terms to buyers, pushed inventory back onto suppliers and so on. These tactics were essentially aimed at leveraging the “vertical linkages” that were mentioned in the literature of Nichter and Goldmark (2009). An interesting finding, that was not mentioned in the literature, was the use of secondary product lines or “cash cows” to alleviate the cash flow burden on the business.

As mentioned earlier, for certain businesses, there is no room to reduce cash conversion cycles and the working capital burden places large pressure on the flow of cash. To bootstrap their way through this challenge, some businesses have installed low margin, high volume, and quick conversion time product lines to generate cash to fund the working capital requirement of the core business. This has proven to be very successful and one of the businesses has alluded to creating secondary businesses to fund working capital of the core business.

Certain businesses have invested in technology to completely revolutionise production processes with the aim of reducing cycle times and increasing productivity. Such bold moves are characteristic of entrepreneurs who have a view of the future and are constantly looking for opportunities to create a competitive advantage and grow the business. This supports the literature which states that rapid growth entrepreneurs are likely to select strategies that emphasise market growth and technological change (Gundry and Welsch 2001). However, this was found to be true only for entrepreneurs displaying a strong strategic orientation.

What business strategy is all about, essentially, is competitive advantage. The sole purpose of strategic planning is to enable a company to gain, as efficiently as possible, a sustainable edge over competitors (Louw and Venter 2006). Therefore to mitigate against the risk of a highly competitive environment, as highlighted in the previous table, management of rapid growth businesses must develop a strategic orientation and look to develop a robust and sustainable competitive advantage.

Significant improvements to operational efficiencies may not completely solve the cash flow challenges of the business but can reduce the amount of funds required to fill the funding gap created by a positive cash conversion cycle. Businesses have used outsourcing of labour and certain operational activities as a much more effective way of dealing with the cash flow challenges. This of course is yet another bootstrapping tactic that businesses have used. The use of labour brokers or the outsourcing of operations means that the business will pay their supplier on terms which will help the business manage its cash flow more effectively. At a unit level, this may reduce profitability, as the supplier's margin will now be included in the cost. This may not always be the case, as the suppliers may have economies of scale which could enable them to deliver the service cheaper than what the business could have done on its own.

The point is that businesses will employ tactics that may drive up costs as long as it enables them to manage cash flows and increase their bottom line. Outsourcing of certain activities serves not only to improve cash flow but also helps the organization to reduce complexity by simplifying the venture's operations. This supports the literature which highlighted a variety of approaches that that can be used to cope with the increasing managerial complexity brought about by rapid growth (Nicholls-Nixon 2005).

6 CONCLUSION

6.1 Summary of the findings

Research Question One

The funding required for the businesses were for largely for working capital, operational expenditure and capital expenditure. There was only one anomaly where funding was required for the payment of VAT on sales and this was driven by the unique nature of the business. Funding requirements were not specific to a stage of growth with it being possible for both a stage one and a stage five company to require funding for the same cause.

Research Question Two

Most companies will look to bootstrap their businesses for as long as they are able to. Owner financing methods and internal sources of finance are preferred over the use of external sources and businesses will employ a range of tactics to leverage internal sources of finance. Short term debt in the form of overdraft facilities is almost always used to buffer against fluctuations in cash flow or to manage the funding gap created by a positive cash conversion cycle.

Research Question Three

Rapid growth’s biggest impact on the business was that it created instability and introduced inefficiencies within the organization. From a funding perspective this materialized in an increased working capital requirement which was all underpinned by management complexity and the inability for the organization to develop capacity, procedures and competencies quick enough to match the rate at which the organization was growing from a sales perspective.

Research Question Four

The challenges in securing funding were driven by strict lender policies, the age of the business and its ability to provide collateral, as well as through internal factors such as conservative directors and owner manager's emotional attachment to the business with the strong desire to maintain full control of the business.

Research Question Five

The consequences of not meeting funding were limited growth and inefficiencies introduced as a result of aged equipment, the inability to implement the required systems and double-handling through the use of intermediaries and outsourcing.

Research Question Six

The reasons underpinning the financing decisions were driven largely by the availability of finance and management's reluctance to take on external sources of funding. The funding decisions were rarely linked to a broader strategic initiative and were never taken as a result of optimizing the business' capital structure. The businesses, however, did make use of a range of interesting tactics to leverage their current sources of funding.

6.2 Recommendations

As opposed to robust funding strategies, it was found that there was a set of both internal and external factors that has enabled respondents to grow their businesses rapidly. The majority of these factors are out of direct control of the business and depend on certain industry characteristics as well as the business operating model and access to resources. If one or more of these factors are present then businesses need to ensure that they fully leverage the value that these factors have in enabling growth. If these enabling factors are not present then it becomes a key imperative that management develop a strategic orientation and take necessary steps to prepare the business while integrating the organizations major goals, policies and action sequences.

Some of the steps a business should take:

- Develop a strategic mindset and take a strategic approach to the financing of the organization.
- While having the necessary knowledge and resources ahead of time can assist the business tremendously during rapid growth, a view still remains that claims that rapid growth could more effectively be dealt with by creating an infrastructure that enables periods of self-organised change to occur (Nicholls-Nixon 2005). Businesses should therefore look to design their organizations with a dynamic structure that allows them to quickly and effectively adapt to the rate of growth of the organization.
- Businesses should avoid formalized processes that are wrought with bureaucracy. The rapid growth environment requires a quick response time and as such systems and processes should be designed for execution.
- Assess all possibilities for reducing working capital and a business' cash conversion cycle. The business' ability to meet its cash flow needs must be traded off against the drop in profitability associated with increasing flexibility.
- The cost of taking on external sources of finance must constantly be traded off against the decision to bootstrap the business through growth.
- Think creatively and innovatively. If access to external finance is not available, look at developing a portfolio that is able to cross subsidise or overlap cash cycles to maintain a smooth flow of cash.
- Develop a close relationship with financial institutions and reduce the asymmetry of information between the institution and the business.
- Take a strategic and unemotional view on the use of private equity to fund growth.

- Develop a planning culture (use scenario planning where the environment is filled with uncertainty) to provide the business with as much time as possible to prepare wherever possible.
- Develop and maintain a sustainable edge over competitors through unique and difficult to replicate capabilities.

All of this must be underpinned by management maintaining the dimension of intelligent opportunism which many successful entrepreneurs appear to possess and which is also one of the key strategic thinking competencies. Many of these steps, while on face value may not appear to have anything to do with funding, are the key building blocks upon which a financial plan will be laid.

Suppliers of funding have a role to play too. Companies, particularly at early stages of development, continue to experience insurmountable challenges in attempting to secure external finance. Some of the steps funders should take:

- Banks need to develop creative mechanisms to reduce the information asymmetry which, as a result, may reduce companies' risk profiles.
- Credit policies appear to be too stringent and are suffocating economic development. Government, financial institutions and the small business sector need to collaborate to develop more productive policies.
- Funders need to reduce the bureaucracy in their processes and develop more dynamic and responsive processes in order to provide a more effective service to rapid growth businesses.
- Providers of risk capital need to open communication channels with businesses and raise awareness within the SME sector.
- Large business and providers of risk capital have a pivotal role to play in the development of small businesses. Government and policy-makers need create incentives to encourage more of these types of funders to enter the market.

- Government needs to remove the obstacles that are preventing businesses from utilising the available funds and grants and create processes to make these sources of funding more accessible to high potential ventures.

Small business development and its benefit to economic growth has been most cited in all of the literature reviewed. Therefore it is critical for government to collaborate with financial institutions, providers of risk capital and the business sector to determine how to most effectively implement policies that truly aim to leverage the small to medium businesses and unlock the full economic potential of this sector.

6.3 Research limitations

This was an exploratory study and hence the depth of explorations or testing of hypotheses was not conducted. Some theories have emerged from the study but these will need to be verified through more focused quantitative studies.

The recommendations provided are generic and are at a high level. As such it will need to be unpacked and tailored for different businesses based on the business' environmental factors and business models.

All of the businesses interviewed have been successful in dealing with rapid growth and as such the enabling factors that have been highlighted should, ideally, be contrasted with businesses that have not been successful to understand the critical enablers.

6.4 Future research

- The key finding arising out of this study was the lack of strategic orientation of many of the businesses. Research into the effectiveness of strategic orientation for SMEs within growing markets could confirm the significance of this competency for business success.

- Conversely, one could examine the key competencies of successful entrepreneurs within competitive markets to determine if there are other non-strategic competencies that enable SMEs to endure and grow despite intense competition and dynamic market conditions.

- Government can design successful programs to address failures in the risk capital market. Research focussed on providing requirements for policy makers and developers of government programs could be highly beneficial for high growth SMEs in the long run.

REFERENCES

Ackerman, P. L. S. and Meyer, P. G. (2007) The identification of credit risk mitigation factors in lending to Black Economic Empowerment (BEE) companies in South Africa, *South African Business Review,* 11(1), pp. 23-44

Aryeetey, E. And Udry, C. (1995) The Characteristics of Informal Financial Markets in Africa, *Bi-annual research conference of the African Economic Research Consortium, Kenya, Nairobi*

Asah, F. and Fatoki, O. (2011) The Impact of Firm and Entrepreneurial Characteristics on Access to Debt Finance by SMEs in King Williams' Town, South Africa, *International Journal of Business and Management,* 6(8), pp. 170-179

Autio, E. (2007)*2007 Global Report on Rapid growth Entrepreneurship,* Global Entrepreneurship Monitor, London Business School, Babson College and Global Entrepreneurship Research Consortium.

Ayyagari, M.Demirguc-Kunt, A. and Maksimovic, V. (2010) Formal versus Informal Finance: Evidence from China, *Review of Financial Studies,* 23(8), pp. 3048-3097

Badulescu, D. (2010) SMEs Financing: the Extent of Need and the Responses of Different Credit Structures, *Theoretical and Applied Economics,* 17(1), pp. 25-36

Barbero, J. L., Casillas, J. C. and Fieldman, H. D. (2011), Managerial Capabilities and Paths to Growth as Determinants of High-Growth Small and Medium-Sized Enterprises, *International Small Business Journal,* 29(6), pp671-694

Britten, N. (1995) Qualitative Interviews in Medical Research, *BMJ,* 311, pp. 251-253

Carland, J. W., Hoy, F., Boulton, W. R. And Carland, J. A. C. (1984) Differentiating Entrepreneurs from Small Business Owners: A Conceptualization, *The Academy of Management Review,* 9(2), pp. 354-359.

Carrol, J. M. and Swatman, P. A. (2000) Structured Case: a methodological framework for building theory in information systems, *European Journal of Information Systems,* 9, pp. 235-242.

Chan, Y. E, Bhargava, N. And Street, C. T. (2006) Having Arrived: The Homogeneity of Rapid growth Small Firms, *The Journal of Small Business Management,* 44(3), pp. 426-440.

Collewaert, V., Manigart, S. and Aernoudt, R. (2010) Assessment of Government Funding of Angel Networks in Flanders, *Regional Studies,* 44(1), pp.119-130

Creswell, J. W. (2009) *Research Design: Qualitative, quantitative and mixed methods approaches,* Third ed., Sage Publications, California

Danielson, M. G. and Scott, J. A. (2006) The Capital Budgeting Decisions of Small Businesses, *Journal of Applied Finance,* 16(2), pp45-56

Datta, D. (2010) Small Business Finance – Implication of Delay in the Formal Sector, *International Journal of Economics and Finance,* 2(4), pp. 130-139.

Davilla, A., Foster, G. And Jia, N. (2010) Building Sustainable Rapid growth Start-up Companies, *California Management Review,* 52(3), pp. 79-105.

Dennis Jr., W. J. (2011) Entrepreneurship, Small Business and Public Policy Levers, *Journal of Small Business Management,* 49(1), pp. 92-106.

Diana, I. V. (2010) Self-Financing of the Firm – Profitable or Limitative, *Young Economists Journal,* 8(14), pp. 21-26

Dobson, W. (2002) A Guide to the Microeconomic Reform Strategy, pp. 1-25, Department of Trade and industry, Pretoria.

Dos Santos, B. L., Patel, P. C. and D'Souza, R. R. (2011) Venture Capital Funding for Information Technology Businesses, *Journal of the Association for Information Systems,* 12(1), pp.57-87

Eckhardt, J. T. And Shane, S. A. (2003) Opportunities and Entrepreneurship, *Journal of Management,* 29(3), pp. 333-349.

Ek, R. and Guerin, S. (2011) Is There a Right Level of Working Capital?, *Journal of Corporate Treasury Management,* 4(2), pp. 137-149

Elo, S. And Kyngas, H. (2008) The Qualitative Content Analysis Process, *Journal of Advanced Nursing,* 62(1), pp. 107-115

Faulkender, M. and Petersen, M. A. (2005) Does the Source of Capital Affect Capital Structure?, *The Review of Financial Studies,* 19 (1), pp. 45-76

Ferreira, E., Strydom, J. and Nieuwenhuizen, C. (2010) The process of business assistance to small and medium enterprises in South Africa: preliminary findings, *Journal of Contemporary Management,* 7(1), pp. 94-109

Fischer, E. And Reuber, R. A. (2003) Support for Rapid growth firms: A Comparison of the Views of Founders, Government Policymakers, and Private Sector Resource Providers, *Journal of Small Business Management,* 41(4), pp. 346-365.

Foster, G. and Davilla, A. (2010) ‘How to Structure companies for Rapid growth’, *IESE Insight*, pp. 13-20.

Garnsey, E. (1998) A theory of Early Growth of the Firm, *Industrial and Corporate Change,* 7(3), pp. 523-556.

Gundry, L. K. And Welsch, H. P. (2001) The Ambitious Entrepreneur: Rapid growth Strategies of Women-owned Enterprises, *Journal of Business Venturing,* 16, pp. 453-470.

Habib, Ahsan (2011) Growth Opportunities, Earnings Permanence and the Valuation of Free Cash Flow, *Australasian Accounting Business and Finance Journal,* 5(4), pp. 101-122

Hanks, S. H., Watson, C. J., Jansen, E. and Chandler, G. N. (1993) ‘Tightening the Life-Cycle Construct: A Taxonomic Study of Growth Stage Configurations in High-Technology Organizations’, *Entrepreneurship Theory and Practice,* Winter 1993, pp. 5-30.

Hathaway, R. S. (1995) Assumptions Underlying Quantitative and Qualitative Research, *Research in higher Education,* 36(5), pp. 535-556.

Jacobs, D., Kotze, P., van der Merwe, A. and Gerber, A. (2011) ‘Enterprise Architecture for Small and Medium Enterprise Growth’, In *First Enterprise Engineering Working Conference (EEWC 2011)*, Antwerp, Belgium, Springer-Verlag, pp. 61-75

Levie, J. And Lichtenstein, B. B. (2010) ‘A Terminal Assessment of Stages Theory: Introducing a Dynamic States Approach to Entrepreneurship’, *Entrepeneurship Theory and Practice,* March 2010, pp. 317-150.

Luiz, J. (2002) Small Business Development Entrepreneurship and Expanding the Business Sector in a Developing Economy: The Case of South Africa, *The Journal of Applied Business Research,* 18(2), pp. 53-67.

Manuel, T. (2007, 21 February 2007) *Budget Speech 2007,* 19 September 2010, http://www.info.gov.za/speeches/2007/07022115261001.htm

Markova, S. and Petkovska-Mircevska, T. (2010) Entrepreneurial Finance: Angel Investing as a Source of Funding High-growth Start-up Firms, *Annals of the University of Petrosani, Economics,* 10(3), pp.217-224

Marshall, M. N. (1996) Sampling for qualitative research, *Family Practice,* 13(6), pp. 522-525.

McPherson, M. A. and Rous, J. J. (2010) Access to Finance and Small Enterprise Growth: Evidence from East Java, *Journal of developing Areas,* 43(2), pp. 159-172

Modigliani, F. And Miller, M. H. (1958) The Cost of Capital, Corporation Finance and the Theory of Investment, *The American Economic Review,*48 (3), pp.261-197

Moon, D. and Tandon, K. (2007) The Influence of Growth Opportunities on the Relationship Between Equity Ownership and Leverage, *Review of Quantitative Finance and Accounting,* 29(4), pp. 339-351

Moro, A., Lucas, M. R. And Kodwani, D. (2010) 'Small and Medium Sized Enterprises (SMEs) and Their Cost of Capital', In *International Conference on Management of SMEs 2010,* Nagpur (India), Institute of Management Technology, pp. 3-15

Naude, W. (2010) Entrepreneurship, developing countries, and development economics: new approaches and insights, *Small Business Economics,* 34(1), pp. 1-12.

Nicholls-Nixon, C. L. (2005) Rapid Growth and High Performance: The Entrepreneur's "Impossible Dream?", *The Academy of Management Executive,* 19 (1), pp. 77-89

Nichter, S. and Goldmark, L. (2009) Small Firm Growth in Developing Countries, *World Development,* 37(9), pp. 1453-1464.

Olawale, F. and Van Aardt Smit, A. (2010) Business environmental influences on the availability of debt to new SMEs in South Africa, *African Journal of Business Management,* 4(9), pp. 1778-1789

O'Regan, N., Hughes, T., Collins, L. and Tucker, J. (2010) Strategic Thinking in Family Businesses, *Strategic Change,* 19(1/2), pp. 57-76

Peterson, M. A. and Rajan, R. G. (1994) The Benefits of Lending Relationships: Evidence from Small Business Data, *The Journal of Finance,* 49(1), pp. 3-37.

Ray, E. N. (2010) *Small and Medium Enterprise (SME) Finance in South Africa: Implications for Private Sector-led Development,* Master of Arts, Dalhousie University, Halifax

Reynolds, P. D. (2011) Informal and Early Formal Financial Support in the Business Creation Process: Exploration with PSED II Data Set, *Journal of Small Business Management,* 49(1), pp. 27-54.

Rogerson, C. M. (2001) Growing the SMME Manufacturing Economy of South Africa: Evidence from Gauteng Province, *Journal of Contemporary African Studies,* 19(2), pp. 267-291

Romano, C. A., Tanewski, G. A and Smyrnios, K. X. (2000) Capital Structure Decision Making: A Model For Family Business, *Journal of Business Venturing,* 16, pp. 285-310

Saublens, C. and Walburn, D. (2009) Smaller Firms, the Equity Gap, Regional Policy and Growth: Will We Ever Learn?, *Local Economy*, 24(6/7), pp. 620-624

Scott, M. And Bruce, R. (1987) Five Stages of Growth in Small Business, *Long Range Planning,* 20(3), pp. 45-52.

Siegel, R., Siegel, E. And Macmillan, I.C. (1993) Characteristics Distinguishing Rapid growth Ventures, *Journal of Business Venturing,* 8, pp. 169-180.

Sunday, K. J. (2011) Effective Working Capital Management in Small and Medium Scale Enterprises (SMEs), *International Journal of Business and Management,* 6(9), pp. 271-279

Temtime, Z. T. And Pansiri, J. (2004) Small Business Critical Success/Failure Factors in Developing Economies: Some Evidence from Botswana, *American Journal of Applied Sciences,* 1(1), pp. 18-25.Tomory, E. M (2011) Bootstrap Financing: Four Case Studies of Technology Companies, *International Journal of Management Cases,* 13(3), pp. 531-538

Truong, G., Partington, G. And Peat, M. (2008) Cost-of-Capital Estimation and Capital-Budgeting Practice in Australia, *Australian Journal of Management,* 33 (1), pp. 95 -122

Turner, R. (2006) Developing Fast Growth Companies, *Engineering Management,* 16(1), pp. 24-28

Uddin, M and Chowdhury, A. Z. R. (2009) Do We Need to Think More about Small Business Capital Budgeting?, *International Journal of Business Management,* 4 (1), pp. 112-116

Van der Berg, S. (1989) ‘Long Term Economic Trends and Development Prospects in South Africa’, In *African Affairs*, Vol. 88, The Royal African Society, London, pp. 187-203.

Vermeulen, M. and Smit, E.v.d.M. (2011) Dividend payout and future earnings growth: A South African study, *South African Journal of Business Management,* 42(4), pp. 33-46

Watson, J. (2006) External Funding and Firm Growth: Comparing Female- and Male-controlled SMEs, *Venture Capital,* 8(1), pp. 33-49.

Winborg, J. And Landstrom, H. (200) Financial Bootstrapping in Small Businesses: Examining Small Business Managers’ resource Acquisition, *Journal of Business Venturing,* 16, pp. 235-254

APPENDIX A: LETTER TO RESPONDENTS

Dear Respondent,

I am completing an MBA at the University of Witwatersrand, Johannesburg (Wits). My MBA thesis is on funding strategies of rapid growth businesses within SA. In order to gather data for this study I have identified 10 local businesses, at various stages of development that I wish to interview. Your company is one of these 10 companies that meet the requirements for my research. To this end, I would be grateful if I could arrange a 1 hour interview with you to understand the funding requirements and strategies adopted by your business through the various stages of its development.

Confidentiality will be maintained throughout the thesis process and the final report will be for academic purposes only. Copies of the final report will be made available to you and may provide you with some valuable insight into different funding strategies adopted within the rapid growth environment.

I will be available to meet with you at a location and time of your convenience.

Thanking you in advance.

Yours sincerely,

Keith Govender

Email: keith.govender@shell.com

Mobile: +27 82 714 9122

APPENDIX B: INTERVIEW SCHEDULE

Remember:
- Ask good questions
- Try not to interrupt interviewees response
- Listen carefully so as to ask good follow up questions
- Provide focus when interviewee goes off the plot
- Be unbiased and set aside prior notions
- Observe but do not judge

Part A: General

1. How long has the business been in operation?
2. What is the annual turnover of the business?
3. What is the management structure like? (i.e. How many layers?)
4. Does the business have formal structures? (E.g. MRP, Accounting systems etc)

Part B: Funding requirements at the various stages of growth

1. What are your current funding requirements?
2. How much funding do you require?
3. Are you meeting your funding requirements?
4. What are/have been the implications of not meeting funding requirements?
5. How have your funding requirements evolved through the development of the business?

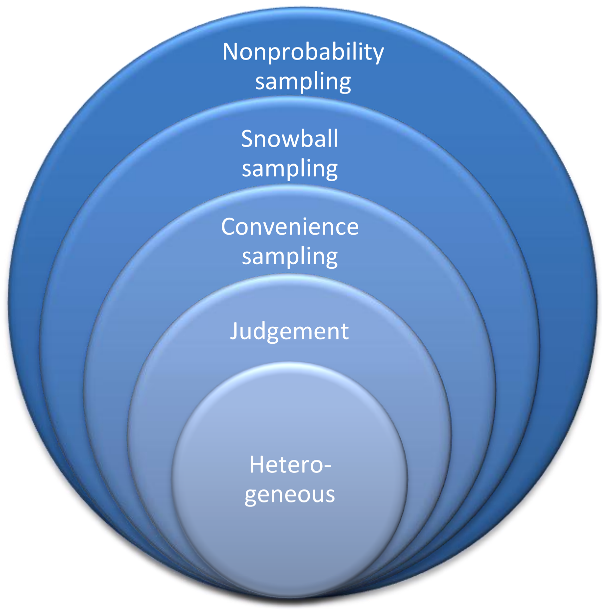
Part C: Funding requirements associated with rapid growth

1. What effect has rapid growth had on the operation of the business?
2. What funding requirements can you attribute to rapid growth?

Part D: Sources of funding and strategies

1. What are your current sources of funding?
2. Are these your desired sources of funding?
3. What is desirable?
4. What is your capital structure?
5. Is this your optimal capital structure?
6. What would be your optimal capital structure?
7. How have your sources of funding evolved since start-up?
8. How has your capital structure evolved since start-up?
9. What were the reason underpinning your sources of funding and capital structure at each stage?
10. What strategies or tactics did you employ to secure funding and to secure funding at good rates?

APPENDIX C: SAMPLING PARADIGM



Own compilation

APPENDIX D: COMPANY DESCRIPTIONS

Company A

This is a manufacturing company operating within the materials handling industry. The company is a distributor of a global crane brand. The company is still in the early stages of development. It is an entrepreneurial business and is managed by the owner.

Company B

This is an art project consultancy business. They work with contemporary visual art as agents and career consultants. This is a family business and is in the early stages of development. It is an entrepreneurial business and is managed by the co-owners.

Company C

This is a sales and marketing business of lubricants for a global brand which it has contracted with. It has strong linkages with a blending plant and local freight services business which is owned by members of the same family. Company C is an entrepreneurial business and is managed by the owner.

Company D

This is a manufacturing company that provides corporate and local businesses with signage. It is an entrepreneurial business and is managed by the owner.

Company E

This is a trucking business that moves items falling outside of the Road Traffic Act in terms of dimension and mass. The business has a managing director who is also a minor shareholder in the business.

Company F

This is a heavy duty trailer manufacturing and supply company. It is a family run business and is run by the founders sons who each take up a respective position on the board of directors.

Company G

This is a polyester converting business that supplies a variety of industries – from films on cables to packaging for food. The business is owned and directed by the three partners.

Company H

This is a manufacturing company that supplies roof products to the mining industry but are not in mining themselves. They supply safety critical products which are there to support a roof and overhangs to prevent collapses and prevent fatalities of miners. The business is led by a managing director and his board of directors.

Company I

This business provides process solutions to the mineral processing industry. Their equipment lends itself to being used in most sub industries of the mineral processing industry. They market themselves as a process solution providers rather than an equipment supplier. So they hire qualified engineers, primarily mineral processing, either chemical engineers, mineral processing engineers, metallurgical engineers. The business forms part of a group of companies and is led by a Managing Director and a team of General Managers.

APPENDIX E: CHARACTERISTICS OF DIFFERENT STAGES OF GROWTH

#	Greiner Description	Characterisation	Life Cycle Stage	Structural Form	Formalisation	Centralisation	Business Tasks
1	Inception	Creativity	Start-Up	Undifferentiated, simple	Very informal, personal, flexible, few policies; planning low or non existent	Highly centralised in founder	Identify niche (single operating unit, single market); Obtain resources; Build prototype; Set up task structure
2	Survival	Direction	Expansion	Departmentalised, functional (Operations, marketing, finance)	Formal systems (information systems) begin to emerge, but enforcement is lax	Centralised; limited delegation	Volume production and distribution; Capacity expansion; maintain a limited product line; drive growth through market expansion; Set up operating systems; marketing activity due to increased competition
3	Growth	Delegation	Consolidation	Departmentalised, functional	Formal, bureaucratic, planning and control systems are enforced	Moderately centralised	Make business more profitable; Expense control; Establish management systems
4	Expansion	Co-ordination	Diversification	Divisional	Formal bureaucratic	Decentralisation becomes entrenched	Budgetary control; management reports; systemisation of administrative functions; Identification of strong sources of competitive advantage; external focus becomes key behavioural imperative
5	Maturity	Collaboration	Diversification	Divisional	Formal bureaucratic	Fully decentralised	Diversification; Expansion of product market scope; Major investment within areas of marketing and plant upgrade and maintenance

Adapted from Greiner Model (Scott and Bruce 1987)

APPENDIX E: COMPANY STAGE OF GROWTH ASSESSMENT

Respondent	Structural Form	Formalisation	Centralisation	Business Tasks	Stage of Growth
A	1	1	1	2	1
B	2	1	2	2	2
C	3	2	2	2	2
D	3	2	2	2	2
E	2	2	3	3	2/3
F	3	3	2	3	3
G	3	3	3	4	3/4
H	3	3	3	4	3/4
I	4	4	3	4	4