



***“IMPROVING SMES ACCESS TO FINANCE AND GROWTH PERSPECTIVES
THROUGH VENTURE CAPITAL FINANCING. A CASE STUDY OF GROFIN
RWANDA”***

By

**MUTAJOGIRE ISHIMWE Jean-Claude
(Kigali-Rwanda)**

Registered Number: RWSFB/PM/0307005

Supervised by

Dr KOPPARHI SATYA MURTY

**THIS PAPER WAS SUBMITTED IN PARTIAL FULFILLMENT
OF THE REQUIREMENTS FOR THE DEGREE OF**

**MASTERS OF BUSINESS ADMINISTRATION
(MBA)**

AT

**MAASTRICHT SCHOOL OF MANAGEMENT (MSM)
MAASTRICHT, THE NETHERLANDS**

**MAASTRICHT SCHOOL OF MANAGEMENT
P.O Box 1203,6201 BE MAASTRICHT
THE NETHERLANDS**

September, 2011

DECLARATION

I, **Jean-Claude, MUTAJOGIRE ISHIMWE** hereby declare that this thesis entitled *“Improving SMEs access to finance and growth perspectives through venture capital financing. A case study of Grofin Rwanda”* is my original work and has never been submitted to any other University for the award of Masters in Business Administration (MBA) degree or any other degree.

.....

Jean-Claude MUTAJOGIRE ISHIMWE

September....., 2011

Thesis Supervisor:

.....

Dr KOPPARHI SATYA MURTY

DEDICATION

To the Almighty God,
To my wife, daughter and parents,
To my brother, sister and friends,
I dedicate this work.

ACKNOWLEDGEMENTS

My special gratitude goes to my Supervisor, **Dr KOPPARHI SATYA MURTY**, for his wise guidance and unceasing encouragement that led to the timely completion of this research. His intellectual support has been a tremendous source of inspiration. His assistance will always be remembered.

My gratitude also goes to all the academic staff who contributed to my training during the masters program.

I would like to express my gratitude to everyone who facilitated the realization of the present research.

I thank you all.

Jean-Claude MUTAJOGIRE ISHIMWE

ABSTRACT

Small and Medium sized enterprises (SMES) are the backbone of all economies and are a key source of economic growth and dynamism.

Rwandese SMEs have little access to finance, which thus hampers their emergence and potential growth. In fact, most SMEs in Rwanda don't often meet condition set by financial institutions, which sees SMEs as a risk because of poor guarantees and lack of information about their ability to repay loans.

Venture capital funds were identified as one possible way of addressing SMEs shortage of capital. The purpose of this research was then to analyze the ability of venture capital funds to improve SMES access to finance and growth perspectives with a more than finance solution.

We made a qualitative and quantitative evaluation based on interviews among Grofin-backed businesses in Rwanda. Discussions were also held with some key players supporting certain initiatives, both public and private, aiming at SMEs facilitating access to finance in Rwanda.

The general conclusion is that Grofin do have a substantial positive impact upon the access to finance and development of supported firms. Both subjective statements from venture-backed businesses and objective data of their performance render clear positive effect.

95% of investee companies responding to the survey said that they would either have not existed, be closed down or would have developed at a slower pace.

Evidence is found that both funding and managerial assistance explain the superior performance of Grofin backed companies. 80% of respondents declared the financier involvement in their business is a lot or very much. 65% of the respondents declared an increase in their sales during the period under financing.

Following the evidence found of the positive impact of venture capital funds on SMEs access to finance, a suggestion is made to policy makers to provide incentives to stimulate that activity. The government should also continue to invest in infrastructures to improve the business environment while Entrepreneurs must do more to improve the investment readiness of their businesses.

LIST OF FIGURES

Figure 2.1. SME sector contribution to employment and GDP across countries.....	8
Figure 2.2. The SME life cycle and financing need.....	16
Figure 4.3. Presentation of the respondents per sector of activity.....	24
Figure 4.4. Presentation of the respondents per business stage	25
Figure 4.5. Presentation of the respondents per age in the portfolio.....	26
Figure 4.6. Impact of the financing on the respondents businesses.....	27
Figure 4.7. SMEs constraints to access finance.....	21
Figure 4.8. Level of involvement of Grofin with respondents companies.....	29
Figure 4.9. Perception on Non-financial contributions.....	30
Figure 4.10. Financial performance change of respondents.....	31
Figure 4.11. Change in Employment level of respondent businesses	33

LIST OF TABLES

Table 2.1. SME definition	7
Table 2.2. Break down of private sector entities in Rwanda.....	16
Table 3.3. Population size and responding rate.....	21
Table 4.4. Presentation of the respondents per sector of activity.....	24
Table 4.5. Presentation of the respondents per business stage	25
Table 4.6. Presentation of the respondents per age in the portfolio.....	25
Table 4.7. Impact of the financing on the respondents businesses.....	26
Table 4.8. Level of involvement of Grofin with respondents companies	28
Table 4.9. Non-financial advisory services.....	29
Table 4.10. Respondents' financial performance.....	31
Table 4.11. Financial performance change of respondents.....	31
Table 4.12. Employment growth of respondent businesses.....	32
Table 4.13. Employment level change of respondent businesses.....	33

LIST OF ABBREVIATIONS AND SIGNS

ADB	: African Development Bank
BDF	: Business Development Fund
BDS	: Business Development Services
BRD	: Rwanda Development Bank
CBS	: Center for Business Solutions
EBITA	: Earnings before Interests, Tax, and amortization
EVCA	: European Venture Capital association
EU	: European Union
GDP	: Gross Domestic Product
MBA	: Masters in Business Administration
NBR	: National Bank of Rwanda
PSF	: Private Sector Federation
RDB	: Rwanda Development Board
SMEs	: Small and Medium Enterprises
US	: United States
%	: Percentage

TABLE OF CONTENTS

DECLARATION.....	ii
DEDICATION	iii
ACKNOWLEDGEMENTS	iv
ABSTRACT	v
LIST OF FIGURES.....	vi
LIST OF TABLES	vii
LIST OF ABBREVIATIONS AND SIGNS	viii
CHAPTER I: GENERAL INTRODUCTION	1
1.1. BACKGROUND OF THE STUDY.....	1
1.2. PROBLEM STATEMENT	2
1.3. OBJECTIVES OF THE STUDY	3
1.3.1. GENERAL OBJECTIVE	3
1.3.2. SPECIFIC OBJECTIVES	3
1.3.3. RESEARCH QUESTIONS	3
1.4. RESEARCH METHODOLOGY	4
1.5. SCOPE OF THE STUDY	4
1.6. SIGNIFICANCE OF THE STUDY	5
1.7. STRUCTURE OF THE STUDY	5
CHAPTER II: LITERATURE REVIEW.....	6
2.0. Overview	6
2.1. Definition of SMEs and Venture capital financing.....	6
2.1.1. SME concept	6
2.1.2. Venture Capital Financing.....	7
2.2. Importance of SMEs in socio-economic development.....	8
2.3. Access to finance related general issues.....	9
2.3.1. What does access to finance means?	9
2.3.2. SME growth phases and funding cycles.....	10
2.4. SMEs constraints to access finance.....	11
2.4.1. Lack of collateral.....	11
2.4.2. Lack of Technical and business skills	12

2.4.3. Asymmetry of information	12
2.4.4. Banks' lack of Know How	13
2.5. Good practices for addressing SME's financing constraints.....	13
2.5.1. Role of financial Intermediaries	14
2.5.2. Role of the Government	14
2.6. Overview of the SME sector in Rwanda	16
2.7. Background characteristics of GROFIN	16
2.7.1. Presentation of Grofin	16
2.7.2. GROFIN Profile	17
2.7.3. Grofin value Proposition	17
2.7.4. How is the process carried out?.....	18
2.8. Summary	19
 CHAPTER III: RESEARCH METHODOLOGY	 20
3.0. Overview	20
3.1. Research Design	20
3.2. Targeted population.....	20
3.3. Methods	21
3.3.1. Historical method	21
3.3.2. Comparative Method.....	21
3.4. Research techniques	22
3.4.1. Documentary Technique	22
3.4.2. Questionnaire.....	22
3.4.3. Informal interviews	22
3.5. Data analysis.....	22
3.5.1. Editing	22
3.5.2. Coding	23
3.5.3. Tabulation.....	23
3.6. Limitations of the study.....	23
3.7. Summary	23

CHAPTER IV: DATA ANALYSIS AND FINDINGS	24
4.0. Overview	24
4.1. Presentation of the respondents	24
4.1.1. Sector spread	24
4.1.2. Composition of the portfolio	25
4.1.3. Age in the portfolio	25
4.2. Operation of the venture backed companies	26
4.2.1. Access to finance	26
4.2.2. Active involvement of the venture capitalists	28
4.3. Post Investment performance	30
4.3.1. Financial performance	30
4.3.2. Employment	32
4.4. Other important public and private initiatives in improving SMEs access to finance ..	33
4.4.1. Government initiatives in Facilitating access to finance.....	33
4.4.2. Private Initiatives in Facilitating access to finance	36
4.5. Summary	37
CHAPTER V: CONCLUSIONS AND RECOMMANDATIONS	38
5.1. Summary of findings and conclusion.....	38
5.2. Recommendations	40
5.3. Further research.....	40
REFERENCES	41
APPENDICES	43
APPENDIX A: QUESTIONNAIRE TO FINANCED BUSINESSES.....	43

CHAPTER I: GENERAL INTRODUCTION

1.1. BACKGROUND OF THE STUDY

In Rwanda, the Vision 2020 is designed as a National Policy Framework that overrides all other government policies. It is argued on the foundation of an entrepreneurial, healthy, skilled and innovative population.

This is the vision that captures the aspirations of the entire Nation - a Nation that believes:

- ✓ In the Private Sector-led development;
- ✓ That Government plays the role of a facilitator by:
 - Putting the regulatory framework in place.
 - Building the infrastructure necessary for businesses to operate and prosper
 - Enticing the people with an entrepreneurial mindset through educational programs and inspiration from the leadership.

The Economic development of a country goes through development of its Medium and Small Enterprises (SMEs). In most developing countries, and particularly in Africa, most businesses fall in the category of SMEs. According to a business census realized by the PSF Rwanda, SME's employ more than 90 % of the active Rwandan population¹. But despite their large number, they still constitute a very narrow tax revenue base. From a FIAS study in Rwanda only 0.3% of tax payers contribute 48% of the Tax Revenue². SMEs are considered as key pillar in the Rwandan vision 2020 and are expected to transform the country from the current \$250 GDP per capita to \$900 by 2020.

Substantial efforts have been made in introducing reforms and creating a new business environment with lower cost of doing business and therefore greater competitiveness ability for businesses. The doing Business report of the World Bank ranked Rwanda as the world's top reformer in creating a business friendly environment in September 2009³. Nevertheless, there is still much that can be done to further reduce the costs of doing business in Rwanda.

¹ PSF (2008), Business and investment climate survey, PSF Rwanda, Kigali, page 7.

² FIAS (2006), Rwanda informal sector survey, FIAS, Washington DC, page 12.

³ IFC (2010), Doing business 2010, World Bank publications, Herndon VA, USA, page 2.

1.2. PROBLEM STATEMENT

Despite the SME sector's significant role to play in the economic development of the country, it continues to experience diverse problems which slower its growth and development. The sector needs more support to overcome problems and to be able to contribute more towards economic growth and development.

The ability of SMES to grow depends highly on their potential to invest in their productions means. All these investments need capital and therefore the possibility to access finance. Against this background the consistently repeated complaint of SME's about their problems regarding access to finance is a relevant constraint that endanger the Economic growth of the country.

SMEs are considered as high risk borrowers due to insufficient assets, low capitalization, vulnerability to market fluctuations and high mortality rates. They also present high Information asymmetry arising from lack of accounting records, inadequate financial statements or business plan; which makes the task difficult for creditors and investors to assess the credit worthiness of potential SME proposals.

As a consequence of the above, commercial banks are generally biased towards large corporate borrowers, who provide better business plans, have credit ratings, more reliable financial information, better chances of success and higher profitability.

On the other hand, Non bank financial intermediaries such as Micro-finance institutions, which could be of help to finance SMEs, can only support the smallest ones due to limited resources. They are however not able to continue to finance their growth.

Between these large and small firms, lies an important number of SMEs, in a so called "missing middle" which cannot access to appropriate finance for growth.

Other factors such as the fragility of the SMEs due to their lack of managerial capabilities and skills are also to be addressed in order to develop sustainable businesses and improve their access to finance. In fact, most of the discussion about SMEs revolves around money, and this leads people to assume that money is all that are needed. It is not always the case. To be successful SME need several other key attributes together with money for a successful outcome.

Venture capital has been identified as an important form of capital for SMEs which experience problems in accessing finance. Venture capital fund risk appetite, products offerings and financing mechanisms have shown the potentiality to improve SMEs access to finance while increasing their chances of success following the assistance provided.

Following the major role to be played Rwandan SMEs in the development of the country and the achievement of the vision 2020; we are going to analyze the ability of venture capitalists to improve SMEs access to finance and growth prospects.

1.3. OBJECTIVES OF THE STUDY

1.3.1. GENERAL OBJECTIVE

The major objective of this study is to highlight the role of venture capitalists in improving SMEs access to finance and growth prospects with a more than finance solution in Rwanda.

1.3.2. SPECIFIC OBJECTIVES

- o Identify the major challenges faced by SMEs to get access to finance;
- o Analyze the advantages offered by venture capitalist as alternative provider of capital to SMEs
- o Identify the different benefits gained by SMEs from non-financial advisory services provided by venture capitalist and the possible impact to their growth prospects ;
- o Analyze the environment in which those SMEs are operating to determine the enabling factors as well as limitation factors to their easier access to finance;

1.3.3. RESEARCH QUESTIONS

Given the major role played by SMEs in supporting the development of the country, we will attempt to reply to the following questions:

- What are major constraints that constitute barriers to financing for SMEs?
- Can venture capitalist financing method be one of the effective methods to improve SMEs access to finance?

- What impact could the advisory services provided by venture capitalist have on firms' growth perspectives?
- What changes in the business environment could be introduced to facilitate the access of finance of SMEs?

1.4. RESEARCH METHODOLOGY

A qualitative and quantitative research design is selected with the purpose of gathering enough and accurate data.

During the research, various methods and techniques were used. Primary and secondary data sources were utilized.

The study was carried out using questionnaires and informal interviews techniques of collecting data.

The population of this research includes 21 venture backed companies financed by Funds under management by Grofin Rwanda.

To come up with this population, we initially identified all the venture capital investors in Rwanda and Grofin Rwanda was found to be the only one to have already financed local businesses.

Unlike typical private equity fund that invest in 10 to 15 businesses, a more important number was identified in the portfolio under management.

1.5. SCOPE OF THE STUDY

The study will be carried out on venture backed SMEs and on other actors in the financial environment.

The researcher wants to come up with comments and perceptions of SMEs on the way in which venture capitalist contributes to improve the SMEs access to finance and growth perspectives. Suggestions on other possible means to facilitate SMES access to finance will be derived from other stakeholders.

1.6. SIGNIFICANCE OF THE STUDY

The outcome of this study will benefit the researcher and all the stakeholders and the community. The researcher will gain knowledge and information about the major barriers faced by SMEs in accessing finance, the opportunities offered by venture capitalist to SMEs and other environment changes which can facilitate SMES access to finance.

The SMEs by getting more access to finance will be able to grow their businesses and contribute more to the development of the country. The financial institutions on the other hand may be able to propose more tailored solutions and increase by the same their volume of activity.

1.7. STRUCTURE OF THE STUDY

The research is structured in five chapters: After a general introduction which discusses the problem statement, objectives, research questions, methodology, scope of the research and the structure of the study, the second chapter presents the literature review which refer to different researches on SMEs, venture capitalists and access to finance related topics.

The third chapter discusses how the research was conducted; presenting the methods and techniques for data collection, the population selection and how findings were come up with.

The fourth chapter presents the data analysis and interpretation, while the fifth chapter provides a summary of findings, recommendations and conclusions and suggested future research topics.

CHAPTER II: LITERATURE REVIEW

2.0. Overview

The purpose of this chapter is to present the literature review which refers to various researches on SMES, venture capitalists and access to finance related topics in order to set a theoretical framework for our research.

2.1. Definition of SMEs and Venture capital financing

2.1.1. SME concept

The concept SME has no universally agreed definition. It covers a wide range of definitions that varies from country to country depending on the socio-economic environment.

Some of the commonly used criteria are the number of employees, value of assets, value of sales and size of capital⁴.

Among those criteria, the most common definitional basis used is the number of employees because of the ease to collect information.

Currently the SME department of the World Bank works with the following definition⁵:

“micro enterprises up to 10 employees, total assets of up to Usd 10,000 and total annual sales of up to Usd 100,000; small enterprises up to 50 employees, total assets and total annual sales of up to Usd 3 millions; medium enterprises up 300 employees, total assets and total annual sales of up to Usd 15 millions”.

In developing countries, the number of employees, size of assets or turnover for SMEs tends to be much smaller compared with their counterparts in developed countries due to their relative size of business entities and Economies⁶.

The Rwandan SME policy provides the below definition for SME⁷:

⁴ Ayyagari, Meghana, Thorsten Beck, and Asli Demirgüç-kunt (2003), Small and Medium enterprises across the globe. A new Database, Policy research working paper 3127, Washington, D.C.: World Bank, page 3.

⁵ Ibid, page 3.

⁶ Bataa (2008), improving access to finance for SMEs: International good experiences and lessons for Mongolia, Institute of Developing economies, Tokyo, p 2.

⁷ Government of Rwanda (2010), Small and Medium Enterprise policy and strategy, Kigali, page 1.

Table 2.1. SME definition

Micro Enterprises	Firms employing less than 5 persons
Small Enterprises	Firms employing between 5 and 30 persons
Medium Enterprises	Firms employing between 31 and 100 persons

Source: SME policy and strategy

2.1.2. Venture Capital Financing

Venture capital financing was developed as a result of the need to provide non-conventional, risky finance.

Venture capital finance means many things to many people. Although the term is being increasingly used, there is yet no generally accepted definition.

The classic definition is that venture capitalist makes equity investment in small innovative and with high growth prospects firms⁸. This definition is however too narrow. In fact, although historically it started with only early stage financing, and although in recent years and particularly in US, high technology has been the main focus of most venture capital investors, the industry covers today a vast spectrum of interests.

Venture capital funds can provide seed, start-up, development and expansion financing to companies which have demonstrated the viability of their business and cannot have access to traditional source of finance⁹.

Venture capital means risk capital. It refers to capital investment, both equity and debt, which carries substantial risk and uncertainties.

Venture capitalists provide more than just money; which is a salient difference between venture capitalists and passive investors¹⁰. They monitor and assist in their portfolio firms. It is a partnership with the entrepreneur in which the investor can add value to the company because of his experience and contact base. The objective is to leverage this involvement to increase the recipient firm's probability of success.

⁸ Yusuf, Altaf and Nabeshima (2004), Global change and East Asian policy initiatives, Washington, D.C.: World Bank, page 393.

⁹ Ibanez (1989), Venture capital and Entrepreneurial development, Washington, D.C.: World Bank, page 1.

¹⁰ Leinschmidt (2007), Venture capital, corporate governance and firm value, Cabler Edition wissenschaft, Frankfurt, page 1.

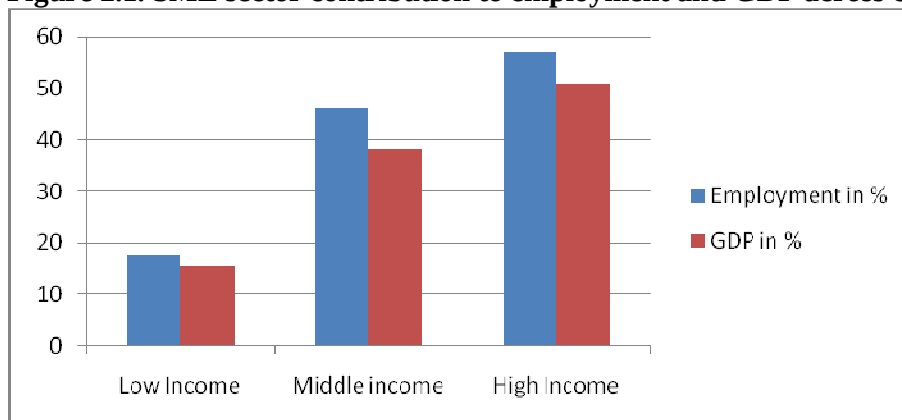
2.2. Importance of SMEs in socio-economic development

SMEs are considered to play an important role in countries' economic growth by generating employment, diversifying economic activities and making a significant contribution to develop exports and trade.

According to an OECD study, they account for over 95% of enterprises, generate two-third of employment are the main source of new jobs¹¹.

A world bank' research on SME' sector contribution to GDP and employment has analyzed the situation for a group of 54 cross countries, 13 of which are low income countries, 24 are middle income and 17 are high income countries¹².

Figure 2.1. SME sector contribution to employment and GDP across countries



Source: The World Bank, Development research group.

The figure 1 shows a significant increase in the SME sector's contribution to employment from the low income countries (17.56%) to the high income countries (57.24%). The SME' contribution to GDP follows a similar trend increasing from (15.56%) of the GDP in the low income countries to (51.45%) in the high income countries.

The lower contribution to employment and GDP of the SME' sector in low income countries does not necessarily mean that they play a less important role, but translate a different reality whereby the informal sector is very important in low income countries.

¹¹ OECD (2005), SME and Entrepreneurship 2005, OECD, Paris, page 7.

¹² Ayyagari, Meghana, Thorsten Beck, and Asli Demirgüç-kunt, opcit, page 4.

In fact, interestingly, the joint contribution of the informal sector and SME sectors to GDP remains approximately constant across income groups at around 65-70 percent¹³.

2.3. Access to finance related general issues

Many research studies have asserted that there exists a “financing gap” for SMEs. There is no commonly agreed definition of this gap, but the term is basically used to mean that a sizeable share of economically significant SMEs cannot obtain financing¹⁴.

This issue is important because it is felt that if those SMEs could have access to finance, those funds would make them more productive. But due to structural problems, the formal system does not provide finance to those entities.

2.3.1. What does access to finance means?

Financial inclusion, or broad access to financial services, is defined as an absence of price or non price barriers in the use of financial services¹⁵. This does not imply however, that all the entities should borrow unlimited amounts at prime rate. Prices, interest rates and size of loans on a market economy, will necessarily depend on the credit worthiness of a client¹⁶.

Access to finance should also be differentiated from the use of financial services. Access essentially refers to the supply of services, whereas the use is determined by the demand as well as the supply.

Nonusers are those who do not use financial services for cultural or religious reasons or because they do not see any need.

Nonusers do not really constitute a problem because their lack of demand drives their nonuse of financial services. On the other hand, are the involuntary excluded who, despite demanding financial services do not have access to them.

¹³ Ayyagari, Meghana, Thorsten Beck, and Asli Demirgüç-kunt, *opcit*, page 11.

¹⁴ OECD (2006), *The SME financing gap: Theory and evidence*, OECD, Paris, page 16.

¹⁵ Demirgüç-kunt, Thorsten and Honahan (2006), *Finance for all? Policies and pitfalls in expanding access*, Washington, D.C.: World Bank, page 27.

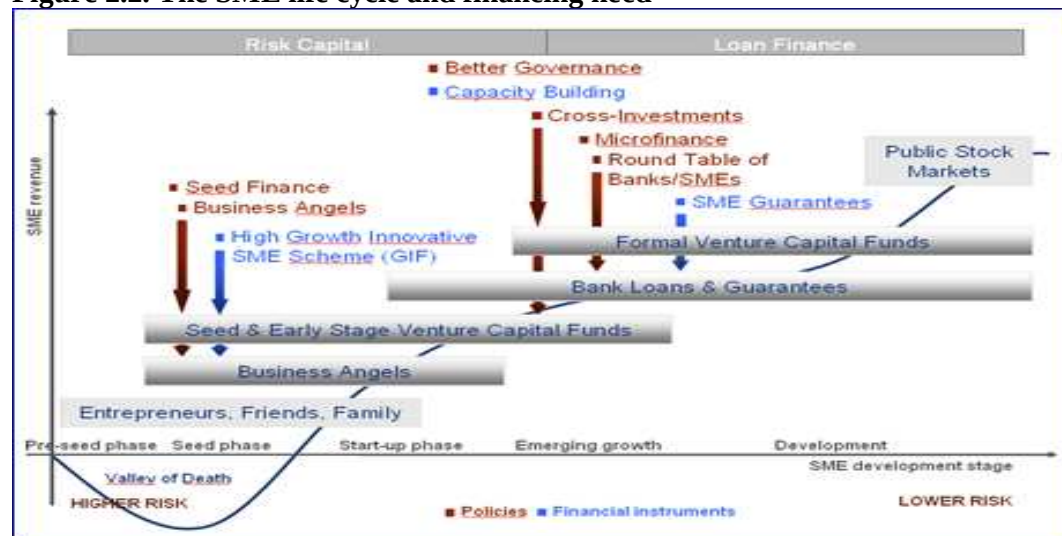
¹⁶ *Ibid*, page 11

2.3.2. SME growth phases and funding cycles

The source of finance most appropriate to fund SME growth and development varies according to the stage of development of the firm.

The growth cycle of typical SMEs can be divided into five stages¹⁷: Seed, start-up, consolidation, expansion and maturity. The length of each stage varies by industry or particular history of each business.

Figure 2.2. The SME life cycle and financing need



Source: DG enterprise, 2007.

At seed and start up stages, the commonly held view is that firms have difficulty accessing finance due to information opacity¹⁸. The most important and commonly used sources of finance at this stage are personal savings of the firm owner, and finance from friends and family. Some SMEs, especially fast growing firms, will also obtain more finance from business angels.

As successful firms survive nascent and start up phases, personal funding becomes limited and these SMEs will necessary have to consider external sources of finance as they progress through the development of their life cycle.

¹⁷ Brando and Macintosh (1999), Competitive industrial development in the age of information: The role of cooperation in the technology sector, Routledge, London, page 160.

¹⁸ Ciaran and Bhaird (2010), Resourcing small and medium enterprises: a financial growth life cycle approach, spring verlag berlin Heidelberg, berlin, page 24.

The external source of finance include traditional debt finance in forms of loans from banks and other financial institutions, micro credits, leasing and hire purchase. Other external financing sources include risk capital (venture capital, equity financing and mezzanine instruments), which may be appropriate for high growth firms, and trade credit¹⁹. Often, a combination of funding sources will be necessary depending on business sector of activity and the development stage of the business.

2.4. SMEs constraints to access finance

The literature on Economic development and corporate finance consistently demonstrates that inadequacies in relation to finance are key barriers to firm growth²⁰.

Traditional commercial banks and investors have been reluctant to service SMEs for a number of well known reasons, among which²¹: “

1. SMEs are regarded by creditors and investors as high-risk borrowers due to insufficient assets and low capitalization, vulnerability to market fluctuation and high mortality rates;
2. Information asymmetry arising from SMEs lack of accounting records, inadequate financial statements or business plans make it difficult for creditors and investors to assess the credit worthiness of potential SMEs proposals;
3. High administrative, transaction costs of lending or investing small amounts do not make SMEs financing a profitable business.”

Below more details:

2.4.1. Lack of collateral

It is well known that the use of collateral in credit contracts helps in dealing with various sources of market imperfections in financial transactions²². In addition to reducing the borrower’s temptation to default, and increasing motivation to devote efforts towards success, it also reduces bankruptcy costs for banks.

¹⁹ European commission (2009), Cyclicity of SME finance, EU, Brussels, page 14.

²⁰ Malhotra, Chen, Crismola, Fan, Hammel and Savchenko (2006), Expanding access to finance: Good practices and policies for Micro, small and Medium enterprises, Washington, D.C.: World Bank, page 8.

²¹ OECD (2002), Official development assistance and private finance: Attracting finance and development to developing countries, OECD, Paris, page 68.

²² ADB (2009), Enterprises in Asia: Fostering dynamism in SMEs, ADB, Philippines, page 46.

Macintosh states that banks are in the low risk lending business²³. Selection of customers is based on very strong prospects of success and the availability of collateral to provide for a back door means of recovering loan.

Therefore, the absence of tangible assets will be a major hurdle for banks to provide financing to SMEs.

2.4.2. Lack of Technical and business skills

Although regulatory improvements are necessary, they are by no means, the only factor to improve access to finance for SMEs. The lack of business skills, of technical skills and appropriate experience is a primary reason for failure of start-ups²⁴.

The issue related to the fragility of SMEs due to their lack of sufficient skills is an important constraint to their access to finance.

2.4.3. Asymmetry of information

The main information asymmetries that constrain SMEs access to finance are as follows:

Inconsistent SMES financial statements and audits: As SMEs are often not required to adopt international accounting standards when preparing their financial statements, large discrepancies arise in the ways firms prepare their financial positions²⁵. It also comes out that in developing countries, SMEs may have different set of books for different audiences. Auditing such statements can be labor and time consuming.

Lack of Access to third party information by providers in the market: Lenders' lack of sufficient knowledge of their clients and no information is available on their clients' credit histories. This lack of client' credit profile reinforces their perception of the high risk involved in lending to SMEs.

²³ Brando and Macintosh (1999), Competitive industrial development in the age of information: The role of cooperation in the technology sector, Routledge, London, page 161.

²⁴ The task force group of the policy board for financial services and regulation. SMEs' access to finance in South Africa: A supply side regulatory review. p204.

²⁵ Malhotra, Chen, Crismola, Fan, Hammel and Savchenko, opcit, page 13.

Lack of focus in the business plan development: SME's business plans are generally not strategic, but rather based on the specific goals or personal preferences of the entrepreneur²⁶. The SMEs objectives are also not clearly communicated in many cases.

As a result, commercial banks are generally more interested to finance large corporate borrowers, who provide better business plans, more reliable financial information, better chances of success and higher return for the institution

2.4.4. Banks' lack of Know How

SMEs typically require small loans compared with large firms. The transaction costs associated with processing and administering loans are, however, fixed, and banks often find that processing small SME loans is inefficient²⁷.

This is mainly because bank's make little or no distinction between large corporations and SMEs in term of product and procedures²⁸. SMEs lending requires a more individualized assessment of cash flows, because SMEs have often limited or inaccurate financial statements. As much as large volume, efficiency and portfolio quality are key to successful small business lending, banks lacks the techniques to increase volume and lower costs.

2.5. *Good practices for addressing SME's financing constraints*

Different initiatives have been conducted to resolve problems SMEs are facing to access finance. These actions can be divided into 2 broad categories showing respectively how financial intermediaries and the government have worked on the problems. In fact, well functioning and sustainable mechanisms for SMEs financing requires both institutions building and a market approach.

²⁶ European commission (2006), Access to finance for SMEs of North Africa region and Middle East, EU, Brussels, page 11.

²⁷ Malhotra, Chen, Crismola, Fan, Hammel and Savchenko, opcit, page 12.

²⁸ Nenova, Thiara Niang and Ahmad (2009), Bringing finance to Pakistan's Poor. Access to finance for small enterprises and the underserved, Washington, D.C.: World Bank, page 121.

2.5.1. Role of financial Intermediaries

In recent years, banks in developed countries have launched a number of initiatives that both improve the profitability of lending to SMEs and also provide SMEs with better access to finance and to financial products that are better tailored to their needs²⁹.

These initiatives include³⁰: «

- Reducing information asymmetry of SMEs and high perceived risk by using credit scoring, using external information providers, pricing to the level of risk, sharing the risk with third party and setting up special support units for high risks customers such as start-ups;
- Reducing costs of lending by applying latest information technologies, streamlining the organization and simplifying lending processes;
- Developing products better adapted to SMEs need;
- Improving financial services for SME through the segmentation of SMEs customers and training of bank staff;
- Cooperation with SMEs organizations and other business development providers in order to reduce risks and costs and combine financial with non-financial services.”

2.5.2. Role of the Government

Arguments for government intervention in the financial sector stress that financial markets are different from other markets because they rely heavily on information and produce externalities that cannot be easily internalized by market participants³¹.

Additionally to the role of insuring Macro-economic stability, the government has generally to intervene over the following elements of the business environment:

2.5.2.1. Regulatory and Legal framework

A country’s legal and judicial environment influences significantly the context in which loan contracting is conducted³². The existence of the necessary commercial laws and the extent to which these laws can be enforced, determines the confidence of the contracting parties in

²⁹ UNCTAD (2001), Improving the competitiveness of SMEs in developing countries: the role of finance to enhance enterprise development, presented at the intergovernmental expert meeting, held in Geneva on 22-24 October, page 5.

³⁰ Ibid, page 5.

³¹ De la torre, Gozzo and Schumler (2007), Innovative experiences in access to finance: market friendly for visible hands?” Policy research working paper 4326, Washington, D.C.: World Bank, page 11

³² Berger (2005), A more conceptual framework for financing small and Medium enterprises, Policy research working paper 3795, Washington, D.C.: World Bank, page 16

financial contracts. Ambiguous and incomplete commercial laws make the enforcement problematic and this may be associated with decreased access to credit.

2.5.2.2. Credit information service

A way of addressing the asymmetry of information consists in establishing a service that collects data about the credit history of borrowers to ease credit institutions decision making regarding the provision of loans³³.

However, for the system to be effective and useful, each credit institutions must accept to share information collected on its customers.

The monitoring of the government is then essential to achieve simple, stable and workable rule of the game.

The legislator must also define whether the system will be managed by the public sector (generally under the umbrella of the central bank) or managed by private players under binding specifications ruling their activities.

2.5.2.3. Credit Guarantee systems

Credit guarantee systems are mechanisms in which a third party, the guarantor, pledges to guarantee loans to a particular group of borrowers³⁴. Even if the probability of default remain unchanged, the guarantee system reduces the lender's expected credit loss; acting as a form of insurance against loss.

Government involvement in creating a guarantee scheme is often rationalized by the observation that SMEs commonly do not have the kinds of collateral that banks require³⁵.

Those guarantee funds seek to expend availability of credit to SMEs and are focused on specific sectors, regions, ownership group, etc. often with an employment, innovation or productivity growth objective.

³³ European commission, opcit, page 12.

³⁴ De la torre, Gozzo and Schumler, opcit, page32.

³⁵ Demirgüç-kunt, Thorsten and Honahan (2006), Finance for all? Policies and pitfalls in expanding access, Washington, D.C.: World Bank, page 169.

2.6. Overview of the SME sector in Rwanda³⁶

In 2007, a country wide census of business operators was conducted by PSF to identify the existing businesses of all sizes and sectors.

Table 2.2. Break down of private sector entities in Rwanda

<i>Family or mobile enterprises</i>	<i>Micro-enterprises</i>	<i>Small enterprises</i>	<i>Medium enterprises</i>	<i>Large enterprises</i>
Informal	Informal/formal enterprises – Units in transition to SMEs		Formal – organized enterprises	
Family or sole trader	Less than 10 employees	10-30 employees	30-100 employees	100 or more employees
Artisans; home-based food; banana beer, sorghum beer; basket weaving, hawkers, etc.	Organized artisans; formal & informal units; open air market place; retail shops	Organized operations in a specific building-factory type; associations, etc	Organized-structured formal enterprises; modern; registered companies	Organized-structured formal enterprises; modern; registered companies
~40,000 enterprises	21,000 enterprises	4,200 enterprises	240 enterprises	50 enterprises

Source: PSF, 2008.

This census found 25,500 businesses, informal businesses without premises not included. 17% of them are small businesses and 4% are medium sized businesses. Despite the relatively small proportion of SMEs, they contribution to the economy is more important.

The vast majority of the private sector employment, approximately 85% is in firms that are somehow informal. These small average size firms present a challenge for Rwanda, as these businesses typically suffers from a number of market failures including access to finance, information and infrastructure, why may constrain their growth.

2.7. Background characteristics of GROFIN

2.7.1. Presentation of Grofin³⁷

The developing world and Rwanda in particular, faces lack of risk capital that has and will continue to constrain growth.

³⁶ PSF, opcit, page 11.

³⁷ Grofin website: www.grofin.com

The venture capitalist industry in Rwanda is very young with only one company in operation up to recently. Grofin is the first risk financier that started operating in Rwanda in early 2007.

2.7.2. GROFIN Profile

Grofin is a multi-national financier and advisor to SMEs. In operation since 2004 at a group level, Grofin invest in the future value and potential of entrepreneurs who own businesses at any stage of development (from start up through growth to expansion) across all sectors.

Targeted clients are committed entrepreneurs operating in emerging markets who need finance from \$50,000 to \$1,500,000 for a period of 3 to 8 years.

Grofin Fact Sheet

- Investing in Nigeria, Ghana, Kenya, Rwanda, Uganda, Tanzania, South Africa and Oman
- Largest multi country growth financier with \$ 260 million under management in 5 funds
- 24 fund investors including CDC, IFC, FMO, Shell Foundation, AfDB, Norfund, etc.
- More than 100 staff in 10 offices in 9 countries
- Experience base of more than 270 transaction financed
- 24 % of all investees are start ups
- Low collateral cover of 57% on average, reflecting true SME risk financier
- More than 7000 jobs in the portfolio
- 76% increase in jobs since investment

2.7.3. Grofin value Proposition

GROFIN recognizes that the major obstacles that entrepreneurs face in growing successful businesses are lack of access to capital and a lack of management skill.

In order to overcome these obstacles, it helps entrepreneurs through:

- ✓ Accessibility: the model focus on the business 's long-term potential for success, making it easier for small and medium enterprises (SMEs) to access financial and business services;

- ✓ More than finance package: a tailored financial assistance is combined with expert business support and guidance for the duration of the relationship with the entrepreneurs.

GROFIN operates in Africa and in the Middle East, providing focused, local support through a team of specialists who understand the unique set of challenges facing businesses each particular market.

2.7.4. How is the process carried out?

Grofin has adopted a unique approach to assessing finance applications. When assessing an application, the following elements are looked at:

- The entrepreneurs' skills, knowledge and experience relevant to the business;
- Commitment of the entrepreneur to the business;
- The potential of the business; and
- The ability of the business to succeed in the long-term by making a profit year after year.

After satisfactorily checking the above elements, a finance package is structured according to particular business needs. Grofin works with the entrepreneurs to develop a financial plan that enables them to better understand and manage their operations for long term profit and growth.

Grofin's business experts assist entrepreneurs with every aspect of their businesses; from detailed business planning to cash flow analysis and financial forecasting even before the finance is approved. Later on, as a Grofin client, a business continues to receive value-added business support and guidance through analyses of monthly management accounts and assistance in developing appropriate plans to address any potential cash flow problem, in addition to helping them with any business needs that may arise.

By providing appropriate finance and empowering the business through knowledge sharing, Grofin increases the business' likelihood of success and profitability.

2.8. Summary

Key concepts for our study were discussed upon and the issues under analysis were also highlighted from the perspective of previous researches realized. Best practices in addressing similar problems were referred too and the case study introduced. The following chapter will present the methodology used.

CHAPTER III: RESEARCH METHODOLOGY

3.0. Overview

The purpose of this chapter is to present the methodological approach and techniques that were used in the collection process of data. The population selection, sampling techniques and Data processing approach are also detailed.

3.1. Research Design

A research design is a plan, structure and strategy of investigation so conceived as to obtain answers to research questions or problems³⁸. A research design expresses both the structure of the research problem and the plan of investigation used to obtain empirical evidence on relations to the problem.

It includes an outline of what the investigation will do from writing hypothesis and their operational implications to the final analysis of data.

A qualitative and quantitative research design is selected with the purpose of gathering enough and accurate data.

3.2. Targeted population

The population consists of all the individuals or things that the researcher want to describe³⁹. The population of this research includes 21 venture backed companies financed by Funds under management by Grofin Rwanda.

To come up with this population, we initially identified all the venture capital investors in Rwanda and Grofin Rwanda was found to be the only one to have already financed local businesses.

Unlike typical private equity fund that invest in 10 to 15 businesses, a more important number was identified in the portfolio under management.

³⁸ Ranjiq Kumar (2005), Research Methodology: A step-by-step guide for beginners, Sage publications, London, page 84.

³⁹ Bart L. Weathington, Christopher J.L Cunningham and David J. Pittenger (2010), Research Methods for the behavioral and social sciences, John Wiley & sons, New Jersey, page 199.

To insure accuracy and quality of data, the entire population was surveyed. After the distribution of questionnaires, all questionnaires were returned.

Below a summary of the population and sample size:

Table 3.3. Population size and responding rate

Respondents	Targeted population	Issued questionnaire	Rate of response
Venture backed companies	21	21	100%

Source: Primary data

3.3. Methods

3.3.1. Historical method

Historical research method is concerned with analyzing and interpreting the meaning of historical events within their context. It is also the process by which a researcher is able to reach a conclusion as to the probable truth of an event in the past by studying objects available in the present⁴⁰.

Using this method, the researcher was able to track the past performances of sampled businesses, identify the constraints they were facing to access finance and obtain information related to the environment in which SMEs were doing business up to recently.

3.3.2. Comparative Method

Comparative research method aims to make comparisons across different factors to trace possible similarities and differences.

This method was used in the current study to compare the operational style of venture capitalists to traditional financiers and the current performances of sampled companies with the ones of other locally based SMEs.

⁴⁰ Lynn S. Connaway & Ronal R. Powel (2010), Basic research Methods for librarians, Greenwood publishing group, California, pages 246.

3.4. Research techniques

Research techniques are instruments or tools used to collect data.

The below techniques were used:

3.4.1. Documentary Technique

Using this technique, the researcher was able to access different books and reports with relevant information for the research.

3.4.2. Questionnaire

A questionnaire can be described as a list of a research or survey questions asked to respondents and designing to extract specific information. A set of questions were designed to collect the necessary data to accomplish the objectives of the research. The questionnaire is made of multiple choices questions and was addressed to venture backed businesses sampled.

Before the questionnaire was delivered, a pilot group made of 4 respondents was designed to test it. This was intentional in order to check that questions were not ambiguous, that instructions were clear and that collected data were in line with needed information.

3.4.3. Informal interviews

This refers to informal discussions with people about the research topic. During visits at their organizations, information relevant to the topic of research was collected.

3.5. Data analysis

The data were analyzed to come up with conclusions concerning research questions.

The below techniques were used:

3.5.1. Editing

During editing, errors in returned questionnaires were identified. Editing was done to insure completeness, accuracy and uniformity of data collected.

3.5.2. Coding

Coding was used to categorize data by classifying the different responses received into categories for easy manipulation.

3.5.3. Tabulation

Tabulation was used to present data in form of both table and other summary format, achieved by counting the frequency of responses.

3.6. *Limitations of the study*

The researcher has encountered the below limitations in the course of the study:

- During the research, a number of reports accessed too were confidential and restricted to any publication. The ethical constraint, stopped the researcher from using some valuable information;
- In some circumstances, respondents were not willing to disclose some important information concerning their businesses despite the assured confidentiality. They were assured that the data was collected for academic purpose and information will be treated in group so that no individual information is disclosed.

3.7. *Summary*

This chapter was all about presenting methodological approaches and instruments used in data collection. The following chapter will discuss the findings.

CHAPTER IV: DATA ANALYSIS AND FINDINGS

4.0. Overview

This chapter deals with systematic presentation and analysis of data and discussions on resulting findings. The presentation and analysis of the findings are in accordance with the objectives set in chapter one.

4.1. Presentation of the respondents

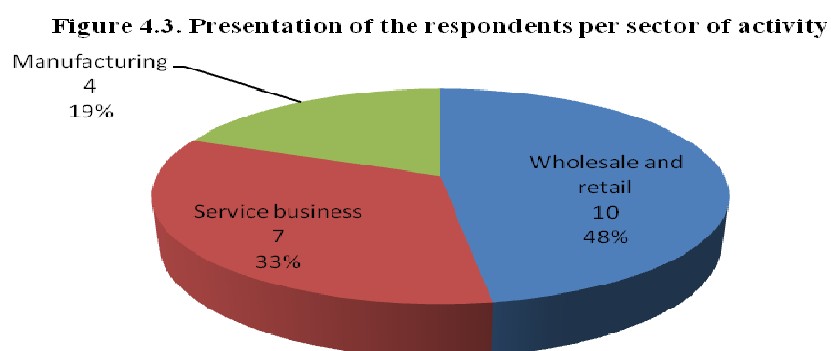
4.1.1. Sector spread

Grofin's model is not exclusive to a specific sector. Grofin Rwanda, has already reached 21 businesses, in contrast to typical private equity fund that invest in 10 to 15 businesses. The portfolio spread can be seen in the diagram below:

Table 4.4. Presentation of the respondents per sector of activity

Respondents Business industry	Frequency	Percentage (%)
Wholesale and retail	10	48
Service business	7	33
Manufacturing	4	19

Source: primary data



Source: Primary data

It appears from the diagram that more than half of the businesses supported are involved in the whole sale and retail sector. This is mainly following the small existing industrial sector in the country and the limited availability of natural resources to be exploited.

The second sector with largest support is the service business which is mainly represented by tourism related activities such as Hotels and restaurants.

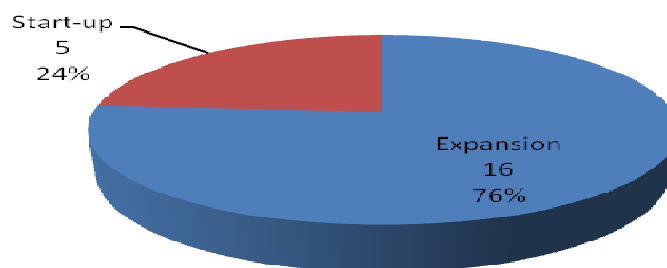
4.1.2. Composition of the portfolio

Table 4.5. Presentation of the respondents per business stage

Respondents business Stages	Frequency	Percentage
Expansion	16	76%
Start-up	5	24%

Source: Primary data

Figure 4.4. Presentation of respondents per sector of activity



Source: Primary data

The start up percentage of the portfolio is 24% and represents 5 businesses. The remaining businesses were existing ones seeking for fund for growth or to rescue their operations for business sustainability. The proportion is the same as at the group level which comprises more than 270 transactions. This reflects the position of a true risk financier, taking the beyond what a traditional financier could accept.

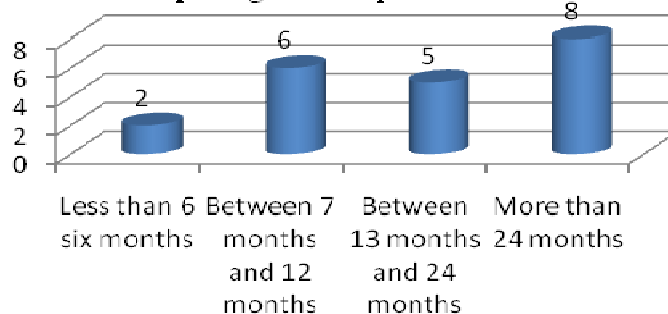
4.1.3. Age in the portfolio

Table 4.6. Presentation of the respondents per age in the portfolio

Respondents age in portfolio	Frequency	Percentage (%)
Less than 6 six months	2	10
Between 7 months and 12 months	6	29
Between 13 months and 24 months	5	24
More than 24 months	8	38

Source: Primary data

Figure 4.5. Presentation of the respondents per age in the portfolio



Source: Primary data

62% of the portfolio clients have received funds more than a year ago. Only 10% or 2 of them have received financing for less than six months.

The majority of the investee companies have been in relationship with Grofin for a period long enough to enjoy the benefits of both the finance and the expertise provided.

4.2. Operation of the venture backed companies

4.2.1. Access to finance

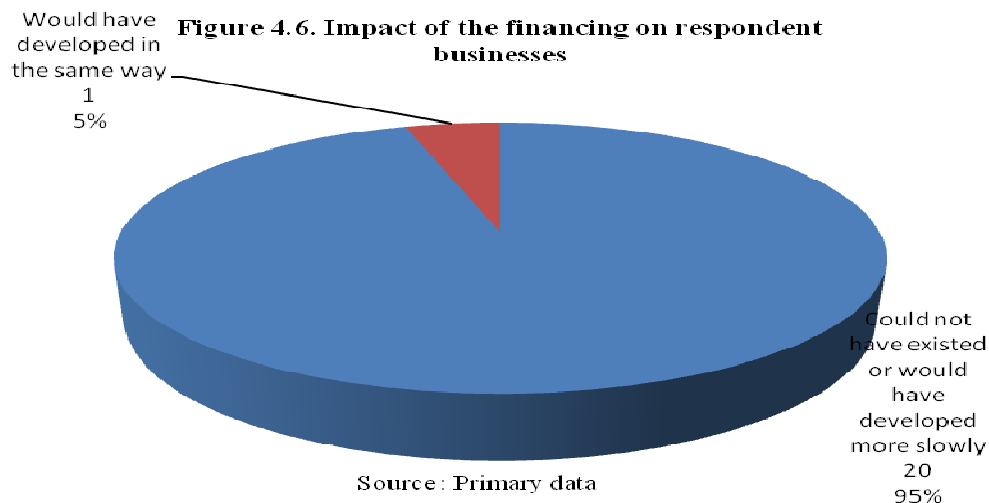
An attempt to identify the role of Grofin as an ingredient in the existence, survival or performance improvement of investee clients, through access to more finance, was made.

Companies were asked and hypothetical question: “Without the involvement of Grofin, would the firm then have not existed, be closed down or would have developed at a slower pace”.

Table 4.7. Impact of the financing on the respondents businesses

Perception of the respondents	Frequency	Percentage (%)
Could not have existed or would have developed more slowly	20	95
Would have developed in the same way	1	5

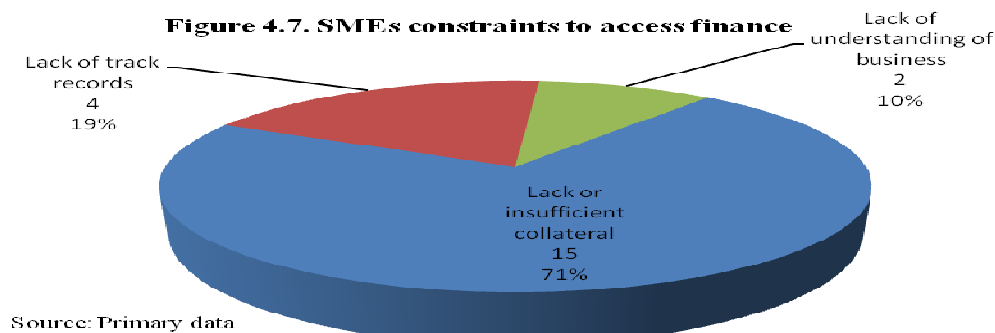
Source: Primary data



About 95% of the investee companies responding to the survey said that they would either have not existed, be closed down or would have developed at a slower pace without Grofin financing. Only 5% believe that they would have developed in the same way.

Another question went further to try to identify the reasons beyond the previous failures of those businesses in getting access to required capital.

At the question: "what were your main constraints to access finance?"



The large majority of investee firms or 71% identified the lack of collateral as their major barrier to access finance at the time. These findings are similar to the results obtained from the business and investment climate survey realized by the Private sector over local businesses which reported that 81% of local businesses (all company sizes, all sectors and in all locations) consider the lack of collateral as a major constraint to access to capital⁴¹.

⁴¹ PSF, opcit, page 26.

The other reported reasons that stopped some of those firms from getting access to capital are the lack of track record for 19% of respondents and the lack of understanding of the business by traditional financier for 10% of respondents.

Grofin overcame all the above constraints by enabling all the respondents to access finance.

4.2.2. Active involvement of the venture capitalists

One of the characteristics of the venture capital model is that venture capitalist besides supporting financially investee firms; also contribute to improve their managerial business competencies and technical knowhow.

The rationale of the provision of business assistance services by venture capitalists is due to that the majority of small and medium businesses do not have all the necessary resources and critical factors needed for business success⁴².

A somewhat different issue is the degree of involvement. An investor may only passively be providing capital or he may be heavily influencing the development of the firm⁴³.

It is expected, as per the venture capitalist definition, that some involvement would be reflected even if the degree of the perceived involvement may vary.

To the question “How involved do you think Grofin is in your business?” we received the below perception:

Table 4.8. Level of involvement of Grofin with respondents companies

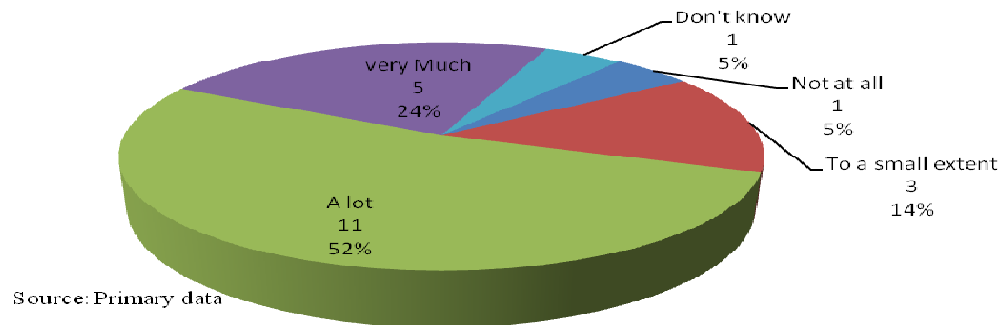
Perception of the respondents	Frequency	Percentage (%)
Not at all	1	5
To small extent	3	14
A lot	11	52
Very Much	5	24
Don't know	1	5

Source: Primary data

⁴² Abduh, D'souza, Quazi and Burley (2007), Investigating and classifying clients' satisfaction with business incubation services, Emerald publishing group Limited, page 2.

⁴³ Christensen, J.L. & Christensen C.E. (2002), The Impact of venture capital in Denmark, Report made for IKE seminar 30,10-2002, page 19.

Figure 4.8. Level of involvement of Grofin with respondents companies



According to the businesses which responded to our survey, an assessment of this impact varies from not at all active (5%) to very much active (24%). 76 % of the respondents declared that the financier involvement is A lot or more.

A related issue is the content of involvement, or in other words, what is it that Grofin provides in addition to capital.

It is clear that venture capitalists focus on monitoring financial performance and giving financial advice⁴⁴. However, their input often extends beyond these areas.

The question asked to companies was to identify what they can value (apart from the provision of finance) as an important additional contribution from Grofin.

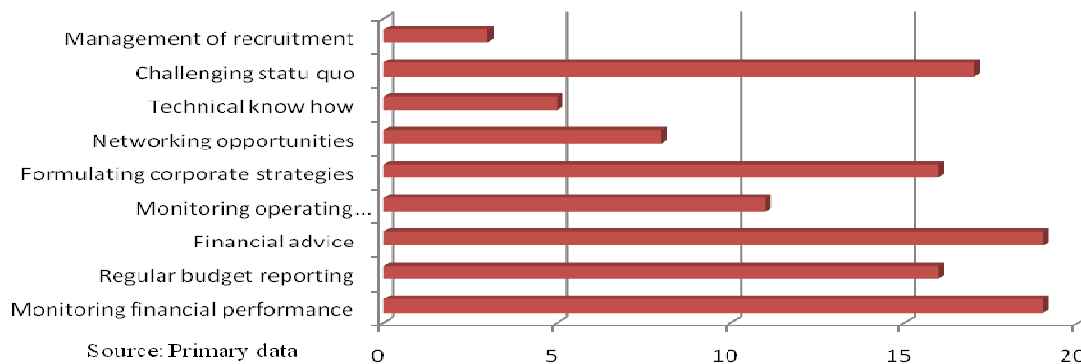
Table 4.9. Non-financial advisory services

Perception on non-financial advisory services	1: Strongly disagree	2: Disagree	3: Don't agree/Don't disagree	4: Agree	5: Strongly agree	Mean
Monitoring financial performance	0%	4%	4%	62%	30%	4.2
Regular budget reporting	0%	5%	19%	76%	0%	3.7
Financial advices	5%	5%	0%	71%	19%	4.0
Monitoring operating performance	0%	10%	38%	29%	23%	3.6
Formulating corporate strategies	5%	5%	14%	57%	19%	3.8
Networking opportunities	0%	19%	43%	38%	0%	3.2
Technical know how	14%	19%	43%	24%	0%	2.8
Challenging status quo	0%	5%	14%	81%	0%	3.8
Management of recruitment	57%	29%	0%	14%	0%	1.7

Source: Primary data

⁴⁴ EVCA (2002), Survey of the economic and social impact of venture capital in Europe, EVCA, Zaventem, page 14.

Figure 4.9. Perception on Non-financial contributions



The results from the survey indicate that investee businesses consider as the most important non-financial contribution the monitoring of financial performances and financial advices (Mean of 4.2. and 4).

In second position are mentioned the formulation of corporate strategies and challenging the status quo.

On the other hand, the technical knowhow, networking opportunities and management of recruitment are not seen as aspects of major contribution from Grofin. This witnesses a complementarily to compensate some areas of soft management SMEs generally lack.

4.3. Post Investment performance

4.3.1. Financial performance

Financial performance of businesses are analyzed by using 2 variables: The growth of sales as a measure of product market performance and the EBITDA (Earnings before interest, taxes, depreciations and amortization) as a measure of an ability to reduce cost in combination with product market development.

Changes in those variables are, of course, affected by general market conditions as well as by the individual company's performance.

Respondents were asked to provide details of the financial performance within their businesses from receipt of funds compared to date:

Table 4.10. Respondents' financial performance

AGGREGATE GROWTH RATE IN SALES OF VENTURE BACKED COMPANIES		
	Aggregate Growth rate	Sample
TOTAL SALES	35%	21
EBITA	22%	21

Source : Primary data

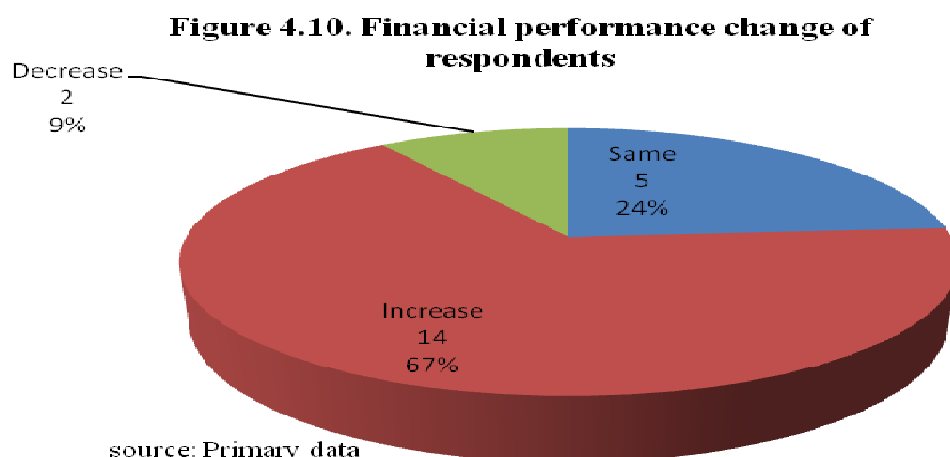
The aggregate growth rate of the turnover of the respondents venture backed companies for the period under financing (average of 19 months) is of 35%. This growth level is strong if compared with the turnover growth of large companies in industry and service sectors of 26.3% for 2010⁴⁵. No data on SMEs growth were available for comparison, but SMEs performance growth are generally by far less important than that of large companies.

An insight of individual performances revealed the results below:

Table 4.11. Financial performance change of respondents

Change in financial performance the respondents	Frequency	Percentage (%)
Same	5	24
Increase	14	67
Decrease	2	9

Source: Primary data



67 % of the respondents declared an increase in their sales during the period under financing. This depicts a better trend in sales growth than the results obtained from the business and

⁴⁵ BNR (2010), Quarterly bulletin. National bank of Rwanda, page 13.

investment climate survey realized by the Private sector over SMEs all around the country which reported that 42% of those SMEs were expecting a sale increase⁴⁶.

24 % showed the same level of sales, but 60 % of them were found in the age categories of having benefited of funds for less than 12 months. The shorter period under financing may not have allowed for the impact of additional capital to materialize on these businesses' performance.

9% reported a decrease in their sales, but 50% of them indicated a declining trend of activity in their sector of operation. General market conditions are important factors contributing to the improvement of a business.

The aggregate growth rate of the EBITA is less important than the one of sales but remain nevertheless substantial at 22 %. The growth rate was mainly affected by start-up businesses (24% of the portfolio) which initially have a negative EBITA, as the business generate more costs than revenue.

4.3.2. Employment

The creation and growth of venture backed companies is also expected to have had an impact in terms of new employment created.

Respondents were asked to provide details of the change in employment in their businesses since they benefited investment from Grofin:

Table 4.12. Employment growth of respondent businesses

AGGREGATE GROWTH RATE IN EMPLOYMENT OF VENTURE BACKED COMPANIES		
	Aggregate Growth rate	Number of job created
EMPLOYMENT	67%	203

Source: Primary data

The aggregate growth rate of employment of the respondents companies since their financing is of 67%. In all, 203 jobs were created by 21 companies. The average of 10 jobs created per company is particularly impressive in light of the fact that, before the investment, the average number of employee per company was of 14 which are also maintained.

PSF, (2008) PSF, opcit, page 18.

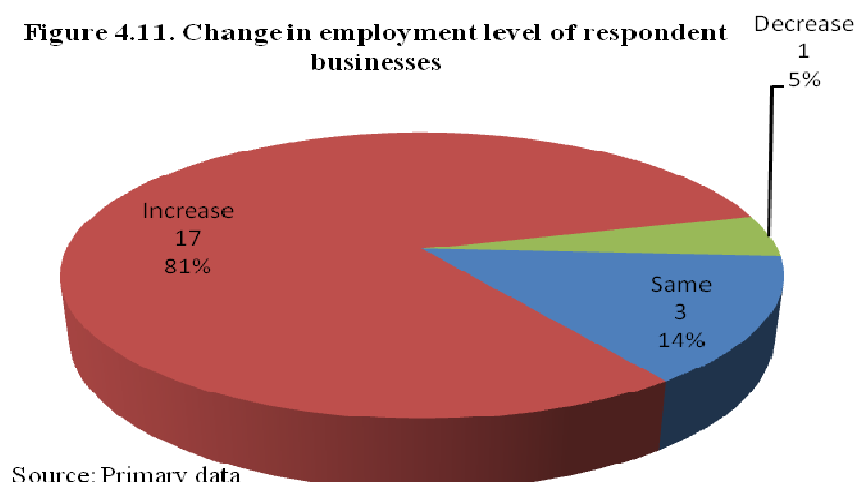
On an individual basis, almost all the surveyed companies reported that, as a result of the new investment, they had been able to create substantial numbers of new jobs.

Table 4.13. Change In employment level of respondent businesses

Change in employment level of respondents	Frequency	Percentage (%)
Same	3	14
Increase	17	81
Decrease	1	5

Source: Primary data

Figure 4.11. Change in employment level of respondent businesses



Source: Primary data

Around 84% of respondents declared an increase in number of employees, while 14 % and 3% respectively declared to have maintained the same number or decrease the number of employees for efficiency reasons.

4.4. Other important public and private initiatives in improving SMEs access to finance

4.4.1. Government initiatives in Facilitating access to finance

The Government has an extensive role in supporting, regulating and sometimes directly operating financial services providers.

4.4.1.1. Land reforms

Prior to 2005, Rwandans did not have ownership rights. The new land policy changed that, as it clearly gives ownership of land to people as opposed to the previous system where land was owned by government.

After the new land policy and the new organic law on land were enacted, a ministerial order established the office of the register of land titles to determine how land is registered and proceed with parcels registrations in the country.

Consequently, the office of the register of land titles embarked on land registration to secure ownership to the citizens of the 8 million parcels in the country of an area 26 thousands square kilometers. A systematic process has been put in place to demarcate each parcel of land.

This reform is going to resolve one of the problems faced by many SMEs of lack of formally registered collateral such as land and property, which can be used as security when accessing loans from financial institutions.

In fact, one of the arguments financial institutions advance to reject some loan requests is the inability of borrowers to offer collateral in an appropriate form and where the opportunity for enforcement is clear.

In addition, the process of registration of charges on assets that can be used as collateral, which was slow and inefficient, was remarkably improved.

4.4.1.2. Judicial reforms

A legal framework that clearly establishes the rights, responsibilities and liabilities of the parties to financial transactions and which provides means to enforce legal obligations efficiently is a key ingredient of a robust and stable financial system.

4.4.1.2.1. Establishment of commercial chambers in the court of justice

Following the limited capacity of the judicial system, civil and commercial disputes were adjudicated by the same judges. Long delays in resolving disputes resulted from this situation, as huge backlog of cases were pending; mostly criminal cases in relation with the genocide.

A judicial reform was done including an arbitration center and the establishment of commercial chambers within the court of justice to faster the process of resolving commercial disputes.

4.4.1.2.2. Replacement of outdated and incomplete commercial laws that affected adversely the settlement of commercial disputes

The new insolvency law, for the first time establishes a legal regime for bankruptcy and creditor protection in the country.

Companies have previously been operating in an environment that allows their establishment but without clear rules and procedures on how companies can close business in case of bankruptcy or voluntary close of business.

Getting credit was made easier with the new established insolvency act. It includes out-of-court enforcement of collateral that has become available to secured creditors, who also now have top priority within bankruptcy.

4.4.1.3. Credit bureau

A credit reference bureau was created to help Rwandan financial institutions to use expert evaluation before making lending decisions.

The credit reference bureau is charged with collecting and compiling information concerning the behavior of individuals and businesses.

Credit reference bureau Africa ltd was mandated by the central bank and started operations in April 2010. Currently, all commercial banks and 30 Micro finance institutions are registered with them.

Credit providers in the country have been depending on the central bank's "central des risques et des impayés"; a public credit bureau operated by the central bank. That report was used as a supervisory tool, focusing mainly on monitoring of large loans, the default of which could weaken the financial service industry.

With limited data about the history of borrowers, it was taking long to financial institutions to assess the credit worthiness of potential borrowers.

4.4.2. Private Initiatives in Facilitating access to finance

4.4.2.1. Business Development Fund (BDF)

SMEs with a viable business plan, but without collateral, can consider helpful to get the recognition of their credit worthiness under the form of guarantee from a third party.

The Business Development Fund (BDF) was created in the course on 2011 to support the established and growth of local SMEs.

With Funds under management of 11 billion, from the Government of Rwanda and BRD, the guarantee fund is divided in 2 broad categories; namely the SME guarantee fund and the Agriculture guarantee fund.

4.4.2.2. Business Development Services Program (BDS)

Training of SMEs is critical. The lack of appropriate trainings is adversely affecting the ability of SMEs to acquire finance following the major skills gap.

Under the auspices of the Private sector Federation, a private and public partnership was created to offer Business Development Services to SMEs. Since the beginning of the program in 2006, it has expanded its presence in the country and its services are available today in 16 Districts.

The BDS centers offer a range of business services such as: business health checks, access to markets, access to information, SMEs training, consultancy, facilitated networking and also mini exhibitions.

Much as the BDS services were completely free, the business community failed to adequately own the program.

A new approach was then introduced whereby BDS services have become demand driven rather than supply driven. BDS centers are now managed by consultants that offer the above services at highly subsidized fees.

4.4.2.3. Incubation center (CBS)

The center for business solutions (CBS), offers services to Rwandan businesses to help them overcome challenges inherent to business.

The center offers the following services: Business Incubation (a facility that is dedicated to helping young businesses start/expand in Rwanda by offering the most affordable rates for workstations/offices space and technical assistance); Business development services; access to market related information and facilitation to access finance.

CBS is also the sole certified Partner of IFC in managing, localizing and distributing the SME toolkit as well as Business age in the country.

SME toolkit offers free online business management information for SMEs, while Business Edge is an international range of management training products for owners of SMEs.

4.5. Summary

This chapter analyzed data collected. The findings showed that SMEs are facing important constraints to access finance and venture capitalists could be an alternative provider of capital given their products offerings. It also appeared that the combination of finance and non financial advisory services result in higher performance and employment growth of venture backed businesses.

CHAPTER V: CONCLUSIONS AND RECOMMANDATIONS

5.1. Summary of findings and conclusion

The importance of SMES in all economies as well as in Rwanda and the challenges they face were highlighted. Venture capital funds were also identified as one of the possible ways of addressing SMEs shortage of capital following their product offering. Through a systematic a systematic methodology presented in line with research objectives set, the ability of venture capital funds in improving SMEs access to finance and growth perspectives was assessed.

The below findings were arrived at:

- The responses of Grofin-backed businesses prove that the investment obtained was crucial to their existence, survival or performance improvement.
95% of investee companies responding to the survey said that they would either have not existed, be closed down or would have developed at a slower pace.
- The main constraints to access finance, prior to receive finance from Grofin, was reported to be the lack of collateral for 71% of respondents and the lack of truck record for 19% of them. Grofin overcame these constraints and financed all the respondents.
- Grofin adopts a hands-on strategy in its working relationship with its investee businesses and as a result of that investee businesses value also strategic input in-non financial area of their businesses.
80% of respondents declared the financier involvement in their business is a lot or very much.
This depicts the fact that Grofin is not only providing capital passively but is also influencing the development of the investee businesses.
- The most important non-financial contributions from Grofin indicated by the survey are the monitoring of financial performances and financial advices. The survey mentioned in second position, with almost equal importance, the formulation of corporate strategies and challenging the status quo. This witnesses a complementarily to strengthen some areas of soft management in which SMEs are generally weak.

- The large majority of responding companies reported an improved competitive position in terms of both market share and profit.

The aggregate growth rate of the turnover of the respondent companies is of 35%. This growth is strong if compared with the turnover growth of large companies in the industry and service sectors of 26% for 2010. No data on SMEs growth were available for comparison, but SMEs performance growth are generally by far less important than that of large companies.

On an individual basis, 65% of the respondents declared an increase in their sales during the period under financing. Despite the fact that 60% of those which reported an unchanged level of sales, were found in the age categories of having benefited of funds for less than 12 months, the growth trend of Grofin backed businesses was better than the one of other SMEs reported in the investment climate survey realized by PSF of 42%.

- The aggregate growth rate of EBITA is less important than the one of sales, but remains nevertheless substantial at 22%. The growth rate was mainly affected by start-up businesses which initially have a negative EBITA.
- Grofin investment enabled investee companies to create an average of 10 jobs per company.

The aggregate growth rate of employment of the respondents businesses since their financing is of 67%.

On an individual basis 84% of the surveyed companies reported that, as a result of the new investment, they had been able to create new jobs.

Furthermore, a review of the important public and private initiatives in improving SMES access to finance has revealed important efforts from the government to improve the legal environment, the land registration system, the availability of information on borrowers' credit worthiness and the creation of guarantee funds. The private sector is also bringing its contribution by creating different initiatives aiming at boosting the capacity of SMEs.

5.2. Recommendations

Improving SMEs access to finance can be achieved through expanding the financial sector, improving business conditions and boosting the capacity of SMEs.

The following recommendation can be done:

- Since our findings provide evidence that the positive effect of venture capital funds on the economy can be explained by the money supplied and the managerial assistance provided, policy maker should go ahead in providing incentives in favor of the venture capital activity and facilitate their operations, to attract more players in order to foster the economy;
- The government should continue to invest in and promote credit bureaus, land registries and accounting standards in order to avail proper information and formally registered collateral;
- The government should continue to improve the legal system and update the available commercial laws in order to fasten settlement of legal disputes;
- The government should support more guarantee funds, to pay in case of default. But rigorous selection of investments should accompany this facility;
- The government should act to improve the awareness among entrepreneurs of the range of financing options available to them within all the financial sector;
- Entrepreneurs must do more to improve the investment readiness of their businesses. Available facilities should be properly utilized;
- Banks, as the most important local provider of capital, must look at innovative ways of providing unsecured lending to small and growing firms;

5.3. Further research

At the end of our research, the objectives set were achieved. However, the challenges of access to finance for SMEs can only be minimized using different initiatives from all the key financial players. The role of other players can also be assessed as proposed, but not limited to the below:

- Assessment and impact of innovative ways used by commercial banks in providing unsecured lending to SMEs;
- Assessment of government initiatives in facilitating SMEs access to finance.

REFERENCES

1. Abduh, D. Q. (2007). *Investigating and classifying clients' satisfaction with business incubation services*. Emerald publishimh group.
2. ADB. (2009). *Enterprises in asia: Fostering dynamism in SMES*. Philippines: ABD.
3. Ayyagari, M. T.-k. (2003). *Small and Medium enterprises accross the globe. A new data base*. Washington D.C: World bank.
4. Bart L. Weathington, c. J. (2010). *Research methods for the behavioral and social sciences*. New jersey: John wiley & sons.
5. Bataa. (2008). *Improving access to finance for SMEs: international good experiences and lessons from Mongolia*. Tokyo: Institute of Developing economies.
6. Berger. (2005). *A more conceptual framework for financing SMEs*. Washington D.C: World bank.
7. Bhaird, C. a. (2010). *resourcing small andn medium enterprises: a financial growth life cycle approach*. Berlin: Spring verlag berlin heidelberg.
8. BNR. (2010). *Quaterly bulletin*. kigali: BNR.
9. Christensen, J. &. (2002). *The impact of venture capital in Denmark. Report made for KIE seminar 30-10*.
10. commission, E. (2006). *Access to finance for SMEs of North africa region and middle east*. Brussels: EU.
11. commission, E. (2009). *Cyclicalitiy of SME finance*. Brussels: EU.
12. De la torre, G. a. (2007). *Innovative experiences in access to finance: market friendly for visible hands*. Wshington D.C: World bank.
13. Demirguc-kunt, T. a. (2006). *Finance for all? Policies and pitfalls in expanding access*. Washington D.C: World bank.
14. EVCA. (2002). *Survey of the economic and social impact of venture capital in europe*. Zaventem: EVCA.
15. FIAS. (2006). *Rwanda informal sector survey*. Washington DC: FIAS.
16. Ibanez. (1989). *Venture capital and entrepreneurial development*. Washington D.C: World Bank.
17. IFC. (2010). *Doing business 2010*. Herndon VA: World bank publications.
18. kumar, R. (2005). *Research methodology: A step-by-step guide for beginners*. London: sage publications.

19. Leinschmidt. (2007). *Venture capital, corporate governance and firm value*. Frankfurt: cabler edition wissenschaft.
20. Macintosh, B. a. (1999). *Competitive industrial development in the age of information: The role of cooperation in the technology sector*. London: Routledge.
21. Malhotra, C. C. (2006). *Expanding access to finance: Good practices and policies for micro, small and medium enterprises*. Washington D.C: World bank.
22. Nenova, T. N. (2009). *Bringing finance to Pakistan's Poor. Access to finance for small enterprises and the underserved*. Washington D.C: World bank.
23. OECD. (2002). *Official development assistance and private finance: Attracting finance and development to developping countries*. Paris: OECD.
24. OECD. (2005). *SME and Entrepreneurship 2005*. Paris: OECD.
25. OECD. (2006). *The SME financing gap: theory and evidence*. Paris: OECD.
26. Powel, L. S. (2010). *Basic research methods for librarians*. California: Green publishing group.
27. PSF. (2008). *Business and Investment climate survey*. kigali: PSF.
28. regulation, T. t. *SMEs' access to finance in south africa: A supply side regulatory review*.
29. Rwanda, G. o. (2010). *small and medium entreprise policy and strategy*. kigali: Government of Rwanda.
30. UNCTAD. (2001). *Improving the competitiveness of SMEs in developping countries: the role of finance to enhance enterprise development. Presented at the intergovernmental expert meeting Held in Geneva 22-24 october*. UNCTAD.
31. Yusuf, A. a. (2004). *Global change and East asian policy initiatives*. Washington D.C: World bank.

APPENDICES

APPENDIX A: QUESTIONNAIRE TO VENTURE CAPITALIST BACKED BUSINESSES

We are conducting a research on Improving SMEs access to finance and growth perspectives in Rwanda through Venture capitalist funds with the case study of Grofin.

You have been selected as one of the beneficiary of the funds to participate in this research.

The information which you will provide will be treated confidentially and will be used only for the purpose of this study.

Thanks for accepting to participate in this research.

Please kindly provide the following information to support this research:

PART A: Personal Information

- I. When was the business created?
- II. What is the Business sector of activity?
- III. How many employees do you have?
- IV. What is the size of the investment received?
- V. What is your current annual turnover?

PART B							
VI. Which of the following services offered by Grofin have you benefited?							
Loan		Advisory services		Loan & advisory services			
VII. How involved (In term of providing support) do you think Grofin is in your business							
Not at all		To a small extent		A lot		Very Much	
VIII. Since when have you received your funding from Grofin?							
1 to 6 months		6 to 12 months		13 to 24 months		More than 24 months	
IX. What was your main constraint to access finance?							
Lack or insufficient collateral		Lack of truck record		Lack of understanding of business			
X Without the financial involvement of Grofin, what would have been the status of the business?							
Could not have existed		would be closed down		Would have developed at a slower pace		Other	
XI. What is the trend of growth in your sector of activity?							
Continuous growth		Stagnant / saturated		Declining activity		I don't know	
XII. Please tell how the annual turnover of your business has changed over the period under financing from Grofin?							
Increased		Remaining unchanged		Decreased		Mention initial employee number if any change	
XIII. Please Indicate how the annual EBITA of your business has changed over the period under financing from Grofin?							
Increased		Remaining unchanged		Decreased		Mention initial turnover if any change	
XIV. Please tell how the employee number of your business has changed over the period under financing from Grofin?							
Increased		Remaining unchanged		Decreased		Mention initial EBITA if any change	

PART C

On a scale to 1 to 5, where 5 is strongly agree and 1 is strongly disagree, How would you answer to the following question? Please select one of the proposed options describing best your opinion.

		5 : Strongly agree	4 : Agree	3 : Don't Agree / Don't Disagree	2 : Disagree	1 : Strongly disagree
XV	What I can value (apart from financing) as an important additional contribution from Grofin is:					
	Challenging status quo					
	Management of recruitment					
	Technical know how					
	Networking opportunities					
	Formulating corporate strategies					
	Monitoring operating performance					
	Financial advice					
	Regular budget reporting					
	Monitoring financial performance					