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Analyzing Small and Medium Enterprises' Perception towards Private Equity as an Alternative Source of Finance in Lusaka District

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ABSTRACT: As guided by the Capital Structure theory, in order to obtain external financing, SMEs may either select debt type of financing or equity type of financing. Since the typical SME cannot meet the requirements to be listed on the Lusaka Stock Exchange, Private Equity remains an attainable source of finance for SMEs who do not want to be financed with debt. This study aimed to analyse the perceptual preference of private equity as an alternative source of financing for SMEs. To meet this objective, an assessment was conducted on the preference of Private Equity to Debt finance. Further, the perception of SMEs towards private equity was explored and themes that influenced the various perception were investigated. A qualitative study was undertaken to meet the above-mentioned objectives. The study employed a grounded theory approach and interviews were used as the primary data collection tool. Fifty-five (55) SMEs who hold accounts with Zambia Industrial Commercial Bank under the Wholesale and Retail trade industrial sector were interviewed and a purposive sampling method was used. From the interviews conducted, the emerging theme was SMEs preferred private equity finance to debt finance mainly in cases where the SMEs interviewed were faced with economic uncertainty, limited collateral, intended to grow quickly, and required technical assistance. However, loss of control, lack of a legal framework and unavailability of Private Equity firms in Lusaka hindered SMEs from utilizing this type of financing. This finding is derived from SMEs preference to Private Equity over debt finance and a largely positive perception SMEs have towards Private Equity finance. Negative perceptions of Private Equity were also noted. This study, therefore, went further to analyse both the factors that influence positive and negative perceptions. These factors included technical assistance, loss of control, payment mechanisms, and duration of the financing methods. The conclusion drawn from this study is that Private Equity is preferred to debt finance because of the lack of high-interest rates and collateral requirements for Private Equity. This study also concludes that there are mainly positive attributes to private equity, though negative perceptions also exist. Loss of control, decision-making concerns, technical assistance, lack of availability of this type of finance, repayment mechanisms, and non-requirement of collateral were noted as factors that were attributed to the conflicting perceptions of SMEs towards Private Equity. Due to this situation, it is recommended that Financial Services Providers take a keen interest in this mode of financing as there is a potential market in this field. Additionally, it is recommended that researchers may focus on conducting a feasibility study to extend the mandate of firms that have been historically providing debt to also include Private Equity Finance for SMEs. Lastly, it is proposed that studies are carried out to assess the legal landscape of Private Equity in Zambia.

KEYWORDS: SMEs, Perception, Private Equity, Lusaka.

1. INTRODUCTION

Small and medium-sized enterprises (SMEs) are often regarded as the economic backbone of any country, and Zambia is no different. The majority of today's large corporations arose from SMEs. The small and medium-sized sector is the backbone of a county's economy, operating as subcontractors, suppliers of manufacturing materials, and customers for large organizations (OECD, 2018). SME employment accounted for 60% of total formal manufacturing employment in both established and emerging nations, according to research (Angulo -Guerrero et al, 2017). The contribution of the SME sector to job generation is even more crucial for African countries. SME employment accounted for around three-quarters of overall manufacturing employment due to informal sector participation (Angulo-Guerrero et al, 2017). Access to finance is an essential element in the development of the SME sector. According to a World Bank document titled "The Determinants of Financing Obstacles," a key barrier to doing business is a lack of access to credit (Beck, Demirguc-Kunt and Martinez, 2010).

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Finance has been proven in several studies to be a more serious barrier for SMEs than for larger organizations, particularly in developing nations. It has also been found that low access to finance has a detrimental impact on SMEs' growth when compared to large corporations (Herr and Nettekoven,2017). Furthermore, data reveals that during a financial crisis, SMEs are more likely than large corporations to be rejected for additional loans (Ganlin et al, 2021). In most developing nations, banks are not under pressure to implement rules that reduce the risk of lending to small customers due to a lack of competition in the banking sector. For example, the high risks and transaction costs associated with commercial lending to this portion of the market limit SMEs' access to the formal financial system. Lenders confront a lack of trustworthy information about borrowers, challenges enforcing contracts (due to ineffective legal frameworks and judicial systems), and a lack of risk management tools. Regulators and capital adequacy rules penalize banks for lending to enterprises that are under-collateralized, exacerbating the situation (Cailloux, et al, 2014).

Due to the importance and difficulties facing SMEs in Zambia, the Zambian Government past and present has tried to respond to these issues raised with SMEs such as the 2016 law that was passed called Movable Assets Act (2016) which is a legal framework that enables financiers get movable assets as security and these assets are registered as being collateral at Patent and Companies Registration Agency (PACRA). But despite these initiatives, SMEs continue facing challenges with accessing financing mainly due to the issues raised earlier in this chapter. Because of this, alternatives to traditional financing such as Private Equity financing may be explored. Private Equity has been an important element in the development of western civilizations from as early as the 18^{th} Century (Nicholas,2019). In a Private Equity transaction, a private equity firm purchases shares in another entity. Or alternatively, Private equity refers to an asset class in which investors purchase the illiquid equity (or equity-like) securities of operating companies (Nicholas,2019). This equity is not publicly traded, but instead held in private hands. Private equity firms hold ownership stakes in companies ranging from a concentrated minority to majority ownership in exchange for their cash. Private equity investors often keep these assets for three to seven years, with the goal of producing high-risk-adjusted financial returns when the investment matures. Private Equity funds often use a "capital plus" approach, in which they help the companies in their portfolios build managerial competence, improve market focus and penetration, strengthen governance, and manage growth, in addition to providing vital funding. Despite the fact that private equity investing techniques differ, many firms seek financial returns by assisting and financing the growth of the companies in their portfolios. As a result, these businesses are closely related to job generation (Divakaran Et al 2014).

1.1. Problem Statement

A World Bank Report on Private Equity and Venture Capital in developing countries (Divakaran Et al, 2014) highlighted the positive impact Private Equity has on SMEs in developing countries as it does not only involve providing the much needed financing an SME requires, but it also provides Technical Assistance to the firms receiving funding and improves that firm's governance structures. However, the World Bank Report also stated that many entrepreneurs may tend to shy away from Private Equity financing due to: a lack of familiarity with equity and exit mechanisms, differing views on valuation, resistance to governance structures, an unwillingness to cede control to external partners, and a reluctance to change the owner manager culture at their firm. According to the World Bank report referenced, (Divakaran Et al, 2014) these factors combine to make sourcing of quality SME investments far more challenging for investors in developing countries with Zambia not being an exception, hence the current study's pertinence in exploring the perception of SMEs towards this mode of business finance.

1.2. Study Objectives

- To explore the factors that influence SMEs' consideration towards Private Equity Finance.
- To describe the financing preference between debt finance and equity finance by SMEs in Lusaka.
- To examine the perception of SMEs towards private equity finance.

2. LITERATURE REVIEW

2.1. Empirical Review

In his book "The Private Equity Playbook," Coffey (2019) compares Private Equity businesses to mutual funds, where money is pooled from a range of investors. Investments are often undertaken for a period of more than five years. The investor, on the other hand, has no say over the fund manager's investments. In a Private Equity Fund, however, the investors are referred to as Limited Partners, and the Private Equity firm serves as the general manager and has complete authority over the investment. Limited partners pledge funds for a set period of time and hence cannot buy and sell on the heat of the moment. There is normally little liquidity, and a private equity fund have a charter, or life span, of ten years. This means that capital is retained for up to ten years.

To make an informed investment decision, private equity funds often actively watch the evolution of technology and the market in their area of expertise. They investigate the founders and their business strategies before investing. When they invest, they offer financial expertise to the contract structure and the arrangement of appropriate incentives/compensation schemes (Cumming, 2012a). Following the initial investment, Private Equity firms are often highly active in obtaining more cash for the companies in which they have invested. Private equity firms regularly oversee their companies, both formally through board membership and informally through managerial responsibilities (Achleitner et al, 2011). Private equity financing may also serve as certification to outside stakeholders and provide counselling to the companies in which they have invested, acting as mentors, and providing strategic advice to entrepreneurs. Furthermore, they assist companies in which they have invested by offering business contacts and recruiting top management. Private equity firms play a crucial role in ensuring that the company in which they invest has robust corporate governance frameworks, and they may even go so far as to replace the original founder as CEO. They also play an active part in advising when a firm should go public (Cumming, 2012b), or, in Zambian nomenclature, list on the Lusaka Stock Exchange (LUSE). With this in mind, we investigate the practicality of this sort of funding on the African continent, by assessing the demand side of this type of finance.

Academics and policymakers have argued for the past two decades that enterprises backed by private equity expand faster, are more innovative, and create more jobs than enterprises that are funded using other means (Puri and Zarutskie,2012). Numerous research comparing sales growth, employment, or total assets of Private Equity-funded and Non-Private Equity-funded enterprises have used matched pair methodologies or cross-sectional regression to examine the effect of Private Equity investments on business growth (Puri and Zarutskie, 2012; Alemany and Marti, 2005). In general, there is a favourable association between Private Equity capital and growth, although the results can vary. Because of the immaturity of European private equity markets, Bottazzi and Da Rin (2002) discovered that private equity backed companies in Europe do not develop and create jobs as quickly as non-private equity backed enterprises.

In Africa, the private equity industry is still in its infancy. According to the Emerging Markets Private Equity Association (EMPEA), between 2008 and 2019, sub-Saharan Africa received only 3% to 6% of all money raised. Nonetheless, it has had remarkable growth since 2005 and has routinely outperformed the national average. South African private equity funds delivered pooled net internal rates of return of more than 20% during a ten-year period, according to a study done by RisCura and the South African Venture Capital Association (2019). The International Finance Corporation (IFC) and the CDC Group are the two most active investors in this space, with their African portfolios outperforming their emerging markets portfolios (Choi 2011; CDC,2011).

A number of recent studies have found that investment is improving as a result of improved perceptions of Africa and private equity. Africa has the largest investment potential of all frontier regions in the world, according to a poll of 158 institutional investors performed by the Economist Intelligence Unit (EIU) in late 2011 (EIU, 2012). When asked which asset class in Africa offers the best investment prospects over the next three years, the majority of respondents (47%) say private equity, followed by infrastructure (38%) and commodities (33%). (EIU, 2012).

Zambian pension fund restrictions appear to limit local investment in Public Equity funds. As of June 2013, Zambian pension funds had invested $9 million in Public Equity funds out of a total of $2 billion in assets under administration. The Registrar must approve a pension fund's investment in PE before the discretionary conditions for the investment may be decided. Because no particular allocation class for public equity has been established, it may come under unlisted securities or, more likely, collective investment plans. The Investment Guidelines forbid funds from making speculative investments, making Public Equity funding problematic (Ashiagbor et al, 2014). Private equity funds were only recognized as collective investment schemes by the Securities and Exchange Commission in 2016, and there is still more to be done in terms of regulatory reform (The Securities and Exchange Commission, 2016).

Zambian local Private Equity investment professionals from Inside Capital Partners, CDC and Phatisa (Valentine Chitalu and Bright Nundwe) have encouraged SMEs to broaden their funding scope and strategy beyond debt financing in an attempt to tap into the rapid growth and expansion that Private Equity financing offers (Mulambia,2015). The long-term outlook for Private Equity financing in Zambia is positive. Zambia ranked 78th in the world in the 2018 IESE Business School Annual Venture Capital and Private Equity global attractiveness index. This index examines economic activity, depth of capital markets, taxation, investor protection and corporate governance, human and social environment, and entrepreneurial culture and deal opportunities in arriving at their scores. There are 125 countries in the world that form the attractiveness index. In Africa, Zambia was the 7th most attractive country for Private Equity and Venture Capital investments (Groh et al., 2018). As stated in the text above, there have been limited studies that have been taken to establish the preference of Private Equity finance to debt finance from an SME perspective.

On debt finance, a survey of the extant literature in Africa particularly reveals the existence of a finance gap in the SME sector (Sowa et al., 1992; Daniels and Ngwira, 1993). Aryeetey et al. (1994), for example, reported that 38% of the SMEs surveyed mentioned credit as a constraint. It is also established that most SME loan applications in Africa are not granted (Osei-Assibey, 2013; Dawson, 1993; Bani-Hani, et al, 2012). In this vein, Aryeetey (1998) observed that only half of the SMEs’ applications for formal finance such as bank loans have any chance of success, and about two-thirds of loan applications by micro-enterprises were likely to be unsuccessful, while Bigsten et al (2000) observed that about 90% of small firms are denied credit from the formal financial sector due to their inability to fulfill conditions such as collateral. Consistent with this, Osei-Assibey (2013) showed that about 95% of SMEs depend solely on personal resources and loans from friends and relatives.

Furthermore, according to Berg and Fuchs (2013), the share of SME lending in banks' overall loan portfolios in five Sub-Saharan African nations ranges from 5% to 20%. According to Hansen et al. (2012), access to capital was reported as a barrier to SME expansion by 39.6%, 18.3%, and 8.5 percent of small businesses in Ghana, Kenya, and South Africa, respectively. Kuntchev et al. (2012) examined SMEs’ access to finance using data from the World Bank's Enterprise Survey, which included 13,685 companies from 38 sub-Saharan African countries. The authors discovered a strong link between a company's size and its access to credit, with smaller companies being more likely to be credit "constrained," illustrating the challenges faced by small business owners in obtaining loans from commercial sources.

2.2. Theoretical Framework - Modigliani and Miller Approach

Capital-structure irrelevance is a leading theory of capital structure. This idea is based on Modigliani and Miller's early studies from the mid-1950s. According to their research, corporate valuation and investment decisions are made independently of financing decisions. While the choice between debt and equity is not inconsequential, it does have an indirect effect on actual decisions. Modern theory of optimal capital structure begins with Modigliani and Miller (M-M) (1963) demonstrating that in perfect capital markets, financing decisions are irrelevant. Their evidence asserts that the market prices of the firm's debt and equity, respectively, sum up to the firm's total value. Value is constant regardless of the proportions of Debt and Equity, given that the balance sheet's assets and growth potential remain consistent. Financial leverage or gearing ratios are immaterial (i.e., the ratio of debt financing to equity capital). As a result of this irrelevance, the firm issues a variety of instruments. According to this view, financial actions cannot improve or diminish the value of a transaction regardless of who finances it. M-M propositions are used in corporate finance as benchmarks, not as end products. In comparison to investment and operating decisions, the majority of financing decisions affect value: eccentric financing decisions may not be detrimental, and managers may be unable to recognize the impact of financing on fluctuating stock market values. M-M arguments are predicated on the complete efficiency of capital markets and, thus, on the perfect behaviour of enterprises and the rational behaviour of managers whose interests coincide with those of the financier. If this were a proven approach, private equity operators and venture capitalists would be treated similarly to other financial institutions and would be evaluated only when the left side of the balance sheet experienced dependable value growth. Replacement and vulture financing may be used only when reorganizing finance sources results in an increase in the firm's worth. Modigliani and Miller (1963) argued that increased debt leads to more financial risk, thereby increasing the required return by shareholders. The assumptions made are the same as in the first proposition. By deriving the WACC formula (Weighted Average Cost of Capital), the authors show:

$$r_E(Levered) = r_E(Unlevered) + \frac{D}{E}(r_E(Unlevered) - r_D)$$

$r_E = cost\ of\ equity$ $\qquad \frac{D}{E} = debt\ to\ equity\ ratio$

$r_D = cost\ of\ debt$

3. METHODOLOGY

The study used a qualitative approach. According to Merriam and Tisdell (2016), the qualitative approach focuses more on trying to understand and interpret processes, responses, and contexts. Qualitative research methods and non-numerical analysis are aimed at eliciting and comprehending participants' experiences, viewpoints, and thoughts. It is, by definition, subjective. It is beneficial for determining a person's abilities, opinions, and knowledge capacity. On the other hand, the study adopted a descriptive research design in order to strike a balance between SMEs' preference towards Private Equity Finance and factors influencing the preferences. According to Saunders et al. (2019), descriptive research creates a detailed narrative of individuals, events, or situations. This approach offers researchers with a characterization of the key principles underlying the stated events from a personal, organizational, and industry-focused perspective.

The study population consisted of SMEs that operate in the Lusaka Central Business District and have a Bank Account with Zambia Industrial Commercial Bank. To select representative SMEs in the Lusaka population, the types of the SMEs considered varied but guidance was obtained from the International Standard Industrial Classification of All Economic Activities (ISIC), Rev.4 (United Nations, 2008). The population of SMEs in the retail trade subsector was difficult to identify due to the absence of literature and regulatory data on this subject. However, Zambia Industrial Commercial Bank has about 500 active SMEs that have active accounts that are operating in the Lusaka Central Business District. Out of this total population (N), 55 SMEs were used as the sample size (n) who were interviewed through semi-structured interviews with data being analysed thematically. The interviewees were purposively selected.

4. FINDINGS

4.1. Preference of Private Equity to Debt

When asked what the preference was between PE and Debt, most of the SMEs contacted stated that Private Equity is a great source of financing especially during economic uncertainty because the financed SME would not have to make monthly interest payments especially when business was not good due to low economic activity. Due to this, SMEs advised that with Private equity finance, there was a "time to grow the Business" as there was an option to reinvest profits made to take advantage of a market boom. This was unlike debt financing where the financed ought to make constant monthly repayments regardless of the performance of the business.

Despite the advantages, Private equity was not found without fault. For a start, SMEs were aware of the loss of control that comes with Private Equity. SMEs understood that the external investor would bring conditions to the newly acquired companies. However, this was also identified to be an advantage in the long run especially if the investor had expertise in the business. Further, SMEs indicated that this may cause them to be more disciplined as they couldn't make irrational decisions.

Debt financing was only seen to have advantages over Private Equity when the SME owner was overly concerned with losing ownership. Despite this, debt finance was viewed as having excessive collateral requirements and having a very rigid repayment mechanism. When collateral was not requested, money advanced would not be enough to have a meaningful contribution to the business as compared to Private Equity. Despite having this collateral requirement, some SMEs pointed out that allowing an investor to finance your business may open the business to political interference especially in cases where a politically exposed person loses favour of the ruling government, thus the funds invested may be deemed as proceeds of crime, thereby interrupting the operations of the business

Most SMEs pointed out that control was the most important element of running their business. These preferred that they could quickly pay off their debt and proceed to running their business. However, other SMEs had a similar appreciation, but their conclusion of the phenomenon was that debt can be obtained in the short term as no business wants to constantly be in debt, however, when a key strategic partner is found, it can be the source of finance for the long run which is preferred. Not surprising from the fore mentioned, most SMEs preferred Private Equity as a source of financing over debt, however there were some SMEs that were attracted to the short-term nature of debt finance.

4.2. Perception of SMEs towards Private Equity

All the SMEs interviewed understood that Private Equity involves the exchange of shares for a capital injection into the business. Further all the SMEs interviewed appreciated that Private Equity investment is long term in nature and since the Investor becomes part of the business, they may influence the running of certain aspects of the business.

When asked if SMEs feel that Private Equity overcomes the shortfalls of Debt financing, the unanimous response was in the affirmative adding that for any meaningful amount of money to be borrowed, there is a requirement of landed property by the Banks and this requirement is not present in Private Equity finance. This was seen as an attractive feature for SMEs as they did not always have the collateral to access the type of financing that they needed to expand. In addition to this, many SMEs interviewed during the study advised that they felt that debt financing had high interest rates and a short payback period. These conditions were present regardless of if the business made money or not. Private Equity was praised in this instance as its model only allowed to distribute profits after money was made by the business. Thus, Private Equity was praised for its long-term focus. SMEs interviewed also advised that they expected the investors to have some level of expertise in the industry they were invested in, therefore they would have tools that would help with the effective running of the business.

Not surprisingly, there were also pockets of SMEs especially in the grocery trades that were sceptical towards Private Equity investors. One of the main areas of concern for this was that the investors may gain valuable insider information from partnering with an SME and use this knowledge to start a similar business once they exit the relationship with the SME.
Despite these positive perceptions of Private Equity, most SMEs interviewed expressed some reservations towards Private Equity finance which were loss of control, potential conflicts in decision making, technical assistance/ non-cash investments, financial factors and psychological factors. These factors are addressed in detail in the next section.

4.3. Factors Influencing SMEs Perception towards Private Equity Finance

There are both positive and negative perceptions that SMEs have towards Private Equity. On one hand, most SMEs welcomed the long term nature of PE finance and the absence of a collateral requirement. And on the other hand SMEs had concerns about decision making, potential conflict, need for technical skill in their business and costs of this type of investment. It is important to note that some of the influencing factors were guided by the literature highlighted in the literature review.

4.3.1. Decision Making and Private Equity Finance

Decision-making in the Private Equity finance model raised conflicting views by the SMEs interviewed. There were perhaps two sets of respondents. The first type of respondent was concerned about the welfare of the company and welcomed investor decision-making only if the decisions being made by the Private Equity investor were for the benefit of the organisation. This group however set up some perquisites for them to enter this type of financing. The most mentioned prerequisite was that the SME owner could always remain with the majority of the shares after a Private Equity transaction. The importance of this was explained as it enabled the SME owner to have the final say in regards to any suggestion that was raised by the investor because they were the organisation's vision carrier. This group of SMEs also stated that to have a smooth partnership with an investor, clear agreements that would govern the relationship between the investor and the SME had to be signed. Issues that were pointed out as to be important when setting up this type of financing were articles of association, non-disclosure agreements, non-compete agreements, and basic operations guidelines. These were deemed to be important as they were perceived to reduce conflict.

4.3.2. Technical Assistance and Private Equity Finance

When interviewees were asked which type of financing they would prefer, between one where they were given ZMW10 million by a Bank or Microfin and another type of finance where they were given half of that amount (ZMW5 Million) but the Private Equity investor was willing to provide technical assistance to the SME by ways of taking the SMEs owners/ staff through business training and providing consultancy. Unsurprisingly, most of the SMEs interviewed opted for the Private Equity financing option and stated that training was a fundamental area where SMEs required assistance to compete with larger firms. The SMEs also stated that in this ever-changing world, they needed to be equipped with the latest information to navigate their business. SMEs that were inclined towards Private Equity also stated that giving their staff technical skills would make it easier for them to have confidence that their business is in safe hands when they leave their business premises to explore other ventures and their business would be more structured. Other SMEs who also supported this option stated that the technical assistance would make them use the money more prudently and they expressed confidence in the quality of training with the majority of respondents saying that the Private Equity Investor would not want to lose his investment therefore they could ensure that they give high-value training to the SMEs. A smaller section of SMEs however, indicated that they would select the ZMW10 million as they could source their own training from books and the internet.

4.3.3. Financial Perception Toward Private Equity Investment

The question, "Between Debt and Equity financing, which one do you think is cheaper in the long run? Any reason for your thoughts?" was asked to gain the financial perception of SMEs towards Private Equity. The consensus was Private Equity was convenient while debt finance was cheaper in numerical terms. Therefore, for a firm to select Private Equity the benefit of continence is valued higher than the potentially indefinite share of profits. This can be obtained from some of the responses by firms that said Private Equity is cheaper than debt in the long run as Private Equity finance does not involve frequent loan repayments and does not involve interest which is perceived as high by SMEs. Responses stated that non-repayment of interest would result in reinvesting larger amounts of returns and making the business grow faster than when debt is used. As one respondent advised, frequent withdrawal of funds from a trade business makes it difficult for the business to grow due to the small margins from sales. However, despite being cheaper, debt finance delays this from happening especially in a typical trading business.

5. DISCUSSION OF FINDINGS

5.1. Corroboration of Findings

In the theoretical framework, we reviewed the Modigliani and Miller approach which stated that in perfect capital markets, financing decisions are irrelevant. Their evidence asserts that the market prices of the firm's debt and equity, respectively, sum up to the firm's total value. Value is constant regardless of the proportions of Debt and Equity, given that the balance sheet's assets and growth potential remain consistent. Financial leverage or gearing ratios are immaterial (i.e., the ratio of debt financing to equity capital). M-M arguments are predicated on the complete efficiency of capital markets and, thus, on the perfect behaviour of enterprises and the rational behaviour of managers whose interests coincide with those of the financier. But as seen from the findings, SMEs have a clear preference for one financing option over another. Hence confirming the accessions that we are not in a perfect market as the M-M approach was based on a perfect market. However, this theory correctly states that the two choices of finance for a firm are either a debt structure or an equity structure.

When we analyse the debt structure, we see that it is perceived as not giving room for borrowing SMEs to grow due to the high-interest rates and short tenors of this type of finance. As Puri and Zarutskie (2012) found in their research enterprises backed by private equity expand faster, are more innovative and create more jobs than enterprises that are funded using other means. Further, the absence of collateral requirements in Private Equity was attractive to SMEs confirming the study conducted by Aryeetey (1998) where it was observed that only half of the SMEs' applications for formal finance such as bank loans have any chance of success, and about two-thirds of loan applications by micro-enterprises were likely to be unsuccessful. Additionally, this finding also confirms findings by Bigsten et al (2000) who observed that about 90% of small firms are denied credit from the formal financial sector due to their inability to fulfill conditions such as collateral.

Additionally, this type of finance was preferred over debt especially when the economic outlook was risky such as when entering a new market or during an outbreak of a deadly disease. The main reason why private equity is preferred may be explained by Brealey et al (2016) who stated that the Mechanism of remuneration i.e banks are compensated from interest payments but Private Equity firms are compensated by either capital gains when the PE firm exists or through dividend payments, both cases imply that private equity only gets compensated when the SME also gets compensated. Further as discussed by the author, not paying interest on a recurrent basis was also advantageous for SMEs as they would only make repayments when they had a return. Thus, this implies that SMEs that have growth potential and need to reinvest most of the returns prefer private equity finance.

On the other hand, when PE is viewed from the perspective of the Private Equity firm, one notices that the investor becomes a shareholder and according to the Zambian Company Act CAP 388 of the laws of Zambia states that in the event of a bankruptcy, stockholders may not receive the full amount invested. Therefore, Technical Assistance is administered as can help with crucial business tasks like governance and financial planning, both of which are necessary for obtaining fresh capital. TA refers to a set of services offered to the types of companies in which PE and VC funds invest, also known as portfolio companies or investee companies, in the context of this research. These services help investee organizations develop skills or capabilities in areas including debt finance, management, technology, and strategic planning (Divakaran Et al, 2014). Additionally, Cummings (2012a) states that when a business is looking for specialized competencies, either hard or soft, it can approach a private equity investor. While hard skills can assist a business in managing its operations and these sets of competencies vary by industry, soft skills passed down by private equity can assist a business in managing its operations regardless of the industry in which it operates.

Finally, the potential loss Private Equity firms may face if the investee company declares bankruptcy leads to the private equity firm participating in the SME's decision-making process and frequently serving on its Board of Directors or assigning authority to someone else (Brealey et al., 2016). This has the undesired result of control concerns. To begin with, the theory of pecking order as explained by Brealey et al (2016) states that financial decisions help to limit the risks associated with conflicts between insiders (managers) and outside investors. In general, there are many different ways to think about risk. Huggins and Thompson (2015) present a concept from management theory that defines a riskier state as one in which a) expected outcomes are more uncertain, b) goals are more difficult to achieve, and/or c) the potential outcome set includes extreme consequences. Applying this approach to PE financing, all three dimensions appear to be important in the view of PE finance by SME owners and managers: For starters, there are various indicators that suggest that private equity financing causes earnings and cash flow to fluctuate more. Second, SME owner-managers describe a number of problems that they believe will obstruct their target achievement, such as reduced management action margin owing to leverage, which is often a result of PE engagement (Wen et al, 2015). The fear of losing key staff (whether because PE investors want a workforce reduction or because key employees are uncomfortable with PE involvement) is also a significant concern (Wen et al, 2015). Third, PE investors typically increase operational and financial risk by expanding into new countries, introducing new products, raising debt, and/or removing surplus assets and cash from the balance sheet, among other things. As a result, the risk of insolvency and illiquidity may increase as a result of a PE investor's engagement

(Kaplan, 2014). As previously stated, because they have concentrated their personal wealth in the company and frequently put up personal guarantees, owner-managers are prone to be risk-averse.

5.2. Study Contribution and Implications

Private Equity in Zambia remains largely unexplored academically. This study however highlighted the perceptions that PE firms have towards private equity, and it concludes that SMEs are for the most part, open to PE finance though they have reservations to certain aspects of this mode of finance such as loss of control and decision-making conflict. It should however be emphasised that openness of SMEs towards PE finance presents a potential to transform the Zambian SME landscape. This is based on the findings that SMEs prefer PE to debt. This assertion is also strengthened by the finding that SMEs have a positive perception towards PE due to the lack of collateral requirement, repayment mechanism and a belief that PE values a business higher than debt finance. This study also highlights the factors that raise concerns from SMEs such as implications of loss of control, implications on the potential conflicts of decision making and unfavourable business practices such as receiving illicit funds and the PE investor establishing a similar company to the investee company. These factors provide building blocks for Regulators, the Government and Financial Service Providers to build upon and tap into this market as this study has established that there is demand for this type of finance. This contribution is valuable as there are multiple papers that highlight the inefficiencies of debt finance on SMEs especially in developing countries. Therefore, this study offers a potential solution that will enable Zambian SMEs grow and rival multinational corporations that have dominated the local business landscape.

In addition to the above, this research also challenges the Theory of Planned Behaviour regarding the importance of social norms for SMEs when making financial decisions. This study concluded that SMEs in Lusaka do not have any social influences when it comes to selecting a finance source. Therefore, further studies are recommended that will focus solely on this aspect. Further, this research also adds more context to the World Bank report highlighted in the problem statement which addresses the dynamics that affect SMEs willingness to acquire PE finance. Additionally, the study also challenges the general statement the World Bank report used in the study when it stated that the majority of SMEs shy away from PE finance due to, resistance to governance structures, a lack of familiarity with equity and exit mechanisms, differing views on valuation and a reluctance to change the owner-manager culture at their firm. Further research is thereby encouraged.

6. CONCLUSION AND RECOMMENDATIONS

6.1. Conclusion

This paper has confirmed that external financing was very important to a business looking to expand. Therefore, for SMEs seeking to expand, may choose between debt financing and equity financing. It was found in the study that Private Equity was preferred as a source of finance over debt financing in instances where the investee firm seeks to grow quickly, was facing an uncertain market outlook, and had limited collateral. It was also observed that SMEs that had adequate collateral and were overly concerned about losing control of their entity for an extended period of time preferred debt finance. From the study, it was observed that SMEs perceived PE as being long-term and the PE firm taking up some ownership of the business, this was viewed in a positive light by SMEs seeking to expand quickly or having large competitors in their sub-sector. SMEs also perceived PE as not requiring collateral therefore more financing would be obtained from PE than from other types of financing. SMEs also perceived PE type of financing as resulting in reduced bankruptcy risk due to the repayment mechanism of this type of finance. Despite these positive perceptions towards PE, SMEs in this study expressed mistrust towards Private Equity. Factors that influence the conflicting perceptions on PE stem from the following; loss of control, decision-making concerns, technical assistance, lack of availability of this type of finance, and repayment mechanisms of private equity finance. Therefore, it was concluded that SMEs welcomed the idea of private equity finance mainly in cases where the SMEs were faced with industry/market uncertainty, intended to grow quickly, and required technical assistance. However, this study also concluded that loss of control, lack of legal frameworks, and unavailability of Private Equity firms in Lusaka hindered SMEs from utilizing this type of financing.

6.2. Recommendations

Firstly, as it was concluded that PE was largely preferred to debt financing due to the factors stated, it is recommended that Financial Services Providers take a keen interest in this mode of financing as there is a potential market in this field for growth and business expansion.

Secondly, as the study established that the perception of SMEs towards PE is mostly positive though it contains some negative aspects, this demand for PE presents an opportunity for academicians to research the supply side of Private Equity and the feasibility of extending the mandate of firms that have been historically known to issue debt to also include Private Equity Finance for SMEs.

Finally, after assessing the factors that influence perceptions towards Private Equity, it is recommended that the Patents and Company Registration Agency (PACRA) carries out sensitization campaigns on company-related issues such as duties and powers of shareholders, directors, and management as established by the companies act of 2017. This is hypothesized to address issues raised such as concerns with decision-making after including an external partner in a business.

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