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SMEs Financing Issues in Malaysia: Youth Entrepreneurs Perspective

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Abstract:
The youth unemployment rate in Malaysia is three times higher than the total population. Unemployment among youth can have negative effects on the economy and social landscape if not curbed. It is widely accepted that entrepreneurship is capable to reduce unemployment rate as well as stimulate economic growth. However, new business entry in Malaysia has stagnated in the past 10 years and remained lower than the OECD average. Access to financing is one of the most prominent challenges facing by SMEs. The situation becomes worse for youth entrepreneurs as they are considered high risk profile and unable to secure financing especially from financial institutions. A survey by Khazanah Research Institute highlighted that only 6% of youth entrepreneurs in Malaysia are getting financing from financial institutions even though financial institutions are considered as predominant source of funds to SMEs. This study aims to understand the challenges facing youth entrepreneurs in Malaysia in accessing financing from financial institutions. In line with the present aims, an attempt is made to identify sources of financing used by youth entrepreneurs, challenges encountered in accessing financing and reasons for not applying for financing. The findings are based on a sample of 260 youth entrepreneurs in Malaysia through questionnaires. The results revealed that youth entrepreneurs use informal financing sources like personal savings. The most pressing problem among youth entrepreneurs who had experiences in accessing financing assistance from financial institutions is lack of track records while interest rate is the main reason for youth entrepreneurs who never had experience in accessing financing assistance from financial institutions.

***Keywords**: Youth entrepreneurs, challenges, financing, financial institutions*

1. Introduction

Youth unemployment is regarded as a major issue worldwide including Malaysia. The youth unemployment rate in Malaysia is three times higher than the total population. Unemployment rate among youth can have negative effects on the economy and social landscape if not curbed. It is widely accepted that entrepreneurship is capable to reduce unemployment as well as stimulate economic growth. Youth entrepreneurship may generate employment opportunities for youth, raise income for them and alleviate poverty (Chigunta, 2002). Hence, youth entrepreneurs have been known to play an important role in the process of economic development and guarantee sustainable growth (Sitoula, 2015). Recently, Malaysian government has launched the National Entrepreneurship Policy 2030 (NEP2030) and the Shared Prosperity Vision 2030 (SPV2030) where among the main objectives is to encourage the development of youth entrepreneurs in Malaysia.

The government of Malaysia has placed serious emphasis on the development of youth entrepreneurs and considers it a key element in positively contributing to the country's gross domestic product (GDP). The Malaysian government has always provided support to youth entrepreneurs including assisting them in terms of financing, physical infrastructure, and business advisory support through the establishment of various agencies like, the Malaysian Global Innovation and Creativity Centre (MaGIC) and the Graduate Entrepreneurship Fund which were initiated by the government to expand the development of youth entrepreneurs in Malaysia (Nor, Masdek and Maidin 2015). Despite the importance of youth entrepreneurs in the national economy and the considerable support from the government, the results are rather disappointing when the impacts of these extensive support systems are found to be insignificant. This is evidenced by a survey conducted by Khazanah Research Institute (2018) where only 8% of young job seekers are self-employed. The Graduates Tracer Study (2018) conducted by the Ministry of Higher Education (MoHE) found that there is a total of 170,105 graduates and only 6.5% are self-employed. According to Ridzwan et al., (2017), there are 107,306 cases of bankruptcies among entrepreneurs in Malaysia from January to April 2015, where 948 of them are youth. Furthermore, new business entry in Malaysia has stagnated in the past 10 years and remained lower than the OECD average (OECD Report, 2016). All these are evidences that youth involvement in entrepreneurial activity is not high as expected (Samah, Omar, Bolong and Hassan, 2018).

Youth entrepreneurs face many obstacles that hinder their development; one of which is evident in the aspect of financial access (Chik et al., 2015; Khan, Noor and Anuar 2016; Mokhtarrudin, Masrurah & Muhamad, 2017; Amesheva et al., 2019). Youth entrepreneurs can obtain financing either from formal sources such as financial institutions or informal sources like family and friends to increase their capital. In Malaysian context, financial institutions play a major role as predominant source of funds to SMEs, providing more than 90% of total financing (SME Annual Report 2015/2016). However, there are evidences that youth entrepreneurs have less access to formal sources. A study by Khazanah Research Institute (2018) reported that 72% of youth entrepreneurs in Malaysia rely on their own saving and savings from family as their sources of financing while only 6% are getting financing from financial institutions. In a same note, a study by Chik et al., (2015) reported that only 6.2% secured financial assistance from commercial banks. This scenario indicates that financial institutions even though as predominant sources of funds to SMEs yet remain as weak potential role in channelling financing to youth entrepreneurs.

As far as the authors is concern, there are considerable amount of studies that examined the challenges faced by SMEs in getting financial assistance. However, very few studies had focused specifically on financing issues faced by youth entrepreneurs. This present study fills the gap by addressing the challenges faced by Malaysian youth entrepreneurs in accessing financial assistance from the financial institutions that may hinder the sustainability and development of their businesses as an avenue towards the achievement of NEP 2030 and SPV 2030.Before discussing the findings, a brief review of prior research in this area will be provided. The methodology used in this study will then be described. The analysis and interpretations of the responses are presented, followed by concluding remarks and recommendations.

2. Literature Review

2.1. Youth Entrepreneurs

Youth entrepreneurs can be defined as business creators below the age of 25 and spirited to pursue entrepreneurial activities as a career (Hulsink and Kock, 2014). While Chik et al (2015), described youth entrepreneurs as 'an entrepreneurs between 18-40 years old and making full use of their own abilities without regard to the resources they currently control'. Hence, in the context of this study, youth entrepreneur is defined as any young person between the age of 18-40, at an early stage of businesses in any sector who has the capacity to identify an opportunity to establish and run a business successfully.

2.2. Youth Entrepreneurs and Sources of Financing

Financing sources which are available for youth entrepreneurs can be divided into two, namely, internal sources which include personal savings, family and friends and external sources such as venture capitalist, business angels, financing from financial institutions, financing from the government.

Personal savings of an entrepreneurs have become the most important sources of financing especially for new establishment of businesses (Abdesamad and Wahab, 2014; Chik et al., 2015; Waked, 2016). In Malaysia, 61.3% of youth entrepreneurs are using their own personal savings during their early stage of businesses (Chik et al., 2015). However, entrepreneurs normally experienced shortage of cash making an entrepreneur struggling in running their business (Waked, 2016). Thus, entrepreneurs often borrow from family and friends. In Malaysia, a study by Chik et al., (2015) reported that 44.78% of youth entrepreneurs ranked sources of financing from family and friends as second important after personal savings at their start-up phase. Once entrepreneurs are exhausted of these sources of financing, they need external financing (Cohen, 2017).

The main sources of external financing offered in Malaysia come from financial institutions, namely Banking Institutions (BIs) and the Development Financial Institutions (DFIs) (Mohamad et al., 2015). Unfortunately, it is often not readily accessible for SMEs as financial institutions provide financing for businesses particularly successful ones and those which continue to grow (Abdesamad and Wahab, 2014). Youth entrepreneurs face greater challenges in accessing financing assistance from financial institutions due to lack of collateral, lack of convincing business plan, fear of risk by financial institutions and others that will hinder the national and regional economic growth and development (Biney, 2019; Zamzam, 2018; Bobic, 2017; Irungu, Sitoula, 2015; Uddin, Chowdhury and Ullah, 2015; Jakubczak, 2015; Chik et al., 2015; Sharu and Guyo, 2013).

2.3. Youth Entrepreneurs and Financing from Financial Institutions

In Malaysia, Banking Institutions (BIs) and the Development Financial Institutions (DFIs) are in the front position to support the growth of SMEs (SME Annual Report, 2016/2017). However, the access to financing provided by financial institutions is determined by the creditworthiness of the borrower such as collateral, financial forecast, credit rationing, high interest rate, and guarantors requirement (Rahman, Duasa, and Kamil, 2016; Chik et al., 2015; Khan and Anuar, 2016; Duasa and Thaker, 2016; BNM Annual Report, 2016). In the SME annual Report (2017/2018), it shows that loan approval rate has decreased from 90.1% in 2016 to 89.8% in 2017. Among the reasons for loan rejection are business too young, no or poor track record and difficult to evaluate application.

The situation becomes worse for youth entrepreneurs when they are normally been considered as riskier borrower due to their inability to meet the lender's expectation such as providing collateral and guarantor, insufficient cash flow, and lack of reliable credit history (BNM Annual Report, 2015/2016).

2.4. Existing Literature in Accessing Financing Assistance from Financial Institutions of Youth Entrepreneurs

Youth entrepreneur's inability to have financing access through financial institutions can be explained through some reasons such as such as shortage of collateral, lack of track record, high interest rate, and long waiting periods (Harif, Hoe and Zali, 2017, Chik et al., 2015, Carrington, 2006). All these obstacles may limit the potential of youth entrepreneurs in securing financing in order to transform their considerable ideas and skills into a viable business.

Past studies (Biney, 2019; Zamzam, 2017; Bobic, 2017; Uddin et al., 2015; Situola, 2015; Jakubczak, 2015; Sharu and Guyo, 2013) highlighted that majority of youth entrepreneurs faced difficulties in accessing financing from financial institutions due to lack of collateral. Lack of trust obliged the bank to require high collateral of which youth entrepreneurs cannot afford. Collateral plays a vital role in eliminating the banks' risk associated with adverse selection and moral hazard problems caused by information asymmetries between the bank and the borrower (Haron, Said, Jayaraman and Ismail, 2013; Stiglitz and Weiss, 1981; Boot, Thakor, and Udell, 1991).

Track record is one of the screening items employed by financial institutions to distinguish the quality of loan applications (Parker, 2018). In the early stage of businesses, youth entrepreneurs find it is difficult to provide solid track records. This situation affects youth entrepreneur's position and makes it difficult for them to present their trustworthiness. Hence, banks perceive them as unstable and risky (Zamzam, 2017). Thus, one of the strategies to counterbalance the higher risk profile of this type of entrepreneurs (Majkova, 2016), financial institutions employed higher interest rate. Higher interest rate employed by financial institutions would make it a big financial burden for youth entrepreneurs (Gitari, 2012). From the Islamic perspective, many Muslim entrepreneurs consider the interest rate being practiced by conventional banks as unethical because it is equivalent to rib which is strictly prohibited in Islam (Aida and Imen, 2014). Even though Islamic banks do not charge any interest, in reality, Islamic banks still use the same pricing benchmark of interest as what had been used by conventional banks. The borrowers still need to pay high profit amount that needs to be guaranteed upfront (Rahman, 2017; Azmat, Skully and Brown, 2015).

Business plan, long loan processing time, transaction cost, viability of business, relationship with bank, unethical charges, lack of knowledge, loan duration too short and insufficient amount of loan approved have also been highlighted as challenges in accessing financing among youth entrepreneurs. For example, Youth entrepreneurs in Egypt need to submit a full and complete business plan as they approach financial institutions from financing (Zamzam, 2017). However, these documents are normally very hard to fulfill, especially by youth entrepreneurs due to lack of experience, thus, prevent them from approaching financial institutions. Youth prefer financing option that are less hectic and made available without wasting their time (Schoof, 2006). This is because lengthy procedures hinder them to start their business on time.

In Malaysia, a study conducted by Khan et al (2016) stated that only 32 out of 438 youth entrepreneurs get their financing from bank due to youth entrepreneurs' financial credibility do not match with the application requirement. This study shows that the figures of youth entrepreneurs reaching out to financial institutions remain minimal. Another study conducted by Chik et al., (2015) highlighted the challenges associated with the application of financing among 591 youth entrepreneurs. Their study shows that youth entrepreneurs lack of track record, lack of collateral, inability to provide financial statements and other strict terms and conditions that banks or financial institutions consider essential for evaluating creditworthiness.

Abundant studies examined the challenges faced by SMEs in getting financial assistance. However, studies focusing specifically on financing issues faced by youth entrepreneurs despite the importance of youth entrepreneurs in the economy development are still scarce. Youth entrepreneurs felt that they are being discriminated because most of the available financing products are not targeted for younger generation (Chik et al., 2015). Thus, youth entrepreneurs still face challenges in accessing financial assistance from financial institutions. To address this gap, this study identifies specific challenges in accessing financial assistance from financial institutions among youth entrepreneurs so that the appropriate financial instruments can be developed in order to solve the issues of youth entrepreneur facing problems in accessing financing from financial institutions.

3. Research Objectives

This study aims to achieve the following research objectives:

- To identify the financing sources used by youth entrepreneurs when first started their business.
- To determine the challenges faced by youth entrepreneurs when applying for financial assistance from financial institutions.
- To find out why some youth entrepreneurs do not choose financing assistance from financial institutions.

4. Research Method

The purpose of this study is to examine youth entrepreneur's specific challenges in accessing financial assistance from financial institutions so that the appropriate financial instruments can be developed in order to solve the issues of youth entrepreneur in accessing financing from financial institutions.To achieve this, a quantitative design in the form of survey questionnaire was adopted. The questionnaires were developed from literature review pertaining issues in financing and focuses on (i) youth entrepreneur's background; (ii) sources of financing; (iii) youth entrepreneurs experience with accessing financing from financial institutions; (iv) challenges in accessing financing assistance from financial institutions and (v) reasons for not applying for financing assistance from financial institutions from those who never experience in applying financing assistance from financial institutions. The population of this current study consists of youth entrepreneurs in Malaysia aged 18-40 owning SMEs at early stage business up to three years. The sample for this research involved youth entrepreneurs from three main sources, namely, the 'Perbadanan Usahawan Nasional Berhad' (PUNB), the Majlis Amanah Rakyat (MARA) and the Malaysian Global Innovation and Creativity Centre (MAGIC). These three organizations were chosen because they are responsible for the development of youth entrepreneurs in Malaysia. A total of 700 questionnaires were sent out, with 260 youth entrepreneurs responded to the survey. The analysis was conducted using descriptive analysis using the Statistical Package for Social Sciences (SPSS) software. Data collection procedures and analysis used in the study are shown in Table 1.

Research Objectives	Instruments and Sample	Data Analysis
What are the financing sources used by youth entrepreneurs when first started their business?	drop-off questionnaire survey 260 youth entrepreneurs	Frequencies and Percentage
What are the challenges faced by youth entrepreneurs when applying for financial assistance from financial institutions?		
Why some youth entrepreneurs do not choose financing assistance from financial institutions?		

Table 1: Research Questions and Data Analysis

5. Results and Discussion

5.1. Respondent Background

Table 1 provides several basic personal information such as gender, age, race, and education level were acquired from the respondents as well as youth entrepreneur's business background including, duration of involving in business, types of business, number of employees, and sales turnover.

Majority of the respondents are male (53.8%) compared to female (46.2%) aged around 21 to 30 years old (45.4%), followed by 31 to 40 years (33.1%) and 18 to 20 years (21.5%). Most of the respondents are Malay (95.8%) due to the respondents selected from PUNB and MARA that are well-known for Bumiputera entrepreneur's development. Others religion comes from MAGIC which focus on multiracial entrepreneur's development. However, there is low response rate from MAGIC that leads to small amount of contribution from the Chinese and Indian. with regard to education level, majority of the respondents are diploma holders (44.6%), with bachelor degree graduates as the next in line (30.8%), follows by upper secondary school leavers (SPM/STPM – 16.9%), master degree graduates (5%) and other qualifications (2.7%). This fact mirrors the inclination of educated generations to participate in the business.

All respondents are still at the early stage of their business with three years being the majority (43.8%). There are also a fair number of respondents who have run their business for two years (32.3%) and a year (22.3%). Most respondents own service sector business (83.1%). These figures are in line with what has been reported in the SME Annual Report (2018/2019) where 89.2 % of SMEs involved in services sector. Lastly, based on the definition of SMEs (SME Corporation Malaysia, 2013), it is evidenced that all 260 respondents are SMEs.

Information	Frequency	Percentage	Cumulative Percentage
i) Gender			
Male	140	53.8	53.8
Female	120	46.2	100.0
Total	260	100.0	
ii) Age (years)			
18 to 20	56	21.5	21.5
21 to 30	118	45.4	66.9
31 to 40	86	33.1	100.0
Total	260	100.0	
iii) Race (head)			
Malay	249	95.8	95.8
Chinese	8	3.1	98.8
Indian	2	.80	99.6
Others	1	.40	100.0
Total	260	100.0	
iv) Education Level			
SPM/ STPM	44	16.9	16.9
Diploma	116	44.6	61.5
Bachelor Degree	80	30.8	92.3
Master Degree	13	5.0	97.3

Information	Frequency	Percentage	Cumulative Percentage
Certificate and Others	7	2.7	100.0
Total	260	100.0	
v) Duration of Business (years)			
0.5	1	.40	.40
1.0	58	22.3	22.7
1.5	2	.80	23.5
2.0	84	32.3	55.8
2.5	1	.40	58.2
3.0	114	43.8	100.0
Total	260	100.0	
vi) Types of Business			
Services	216	83.1	83.1
Manufacturing	29	11.2	94.3
Construction	11	4.2	98.5
Agriculture	2	.80	99.2
Mining & Quarrying	2	.80	100.0
Total	260	100.0	
vii) Number of employees (head)			
None	1	.40	.40
1 to 4	196	75.4	75.8
5 to 10	63	24.2	100.0
Total	260	100.0	
viii) Sales Turnover (RM)			
Less than 300, 000	188	72.3	72.3
300, 000 and less than 3 million	51	19.6	91.9
3 million and less than 15 million	16	6.2	98.1
15 million and 50 million at most	5	1.9	100.0
Total	260	100.0	

Table 2: Respondent's Background

5.2. Sources of Financing

This question was developed under six broad categories namely: personal savings, friends and family, borrowing from financial institutions, venture capital, angel investors and government schemes. The respondents were asked to indicate which sources of finance they employed when they first started their businesses. The questionnaire in this part was purposely designed with multiple selections as the researcher believes most entrepreneurs employed more than one sources of financing in starting their business. Table 3 presents a summary of the findings.

Source	Frequency	Percentage
Personal Saving	213	81.9%
Friends and family	105	40.4%
Government Schemes	51	19.6%
Borrowing from Financial Institutions	30	11.5%
Venture Capitalist	8	3.1%
Angel Investors	7	2.7%

Table 3: Sources of Financing

An inspection of the data presented above, it shows that 81.9% of youth entrepreneurs rely on their personal savings while 40.4 % are on friends and family. This study confirms the results of previous studies such as Abdesamad and Wahab, 2014; Chik et al., 2015; Waked, 2016 and also the report as per SME Annual Report (2018/2019) where entrepreneurs at early stage of businesses tend to rely on internal financing. However, they would turn to external financing once the internal financing is exhausted or as the business grows. This study shows a different view when financing from the government constitutes the biggest portion and financial institutions comes second. The less popular sources of financing among youth entrepreneurs are venture capitalist and angle investors. As stated by Nor (2015), in Malaysia, venture capital financing is considered relatively new while angel investors are more interested to invest in business ventures at the growth stage (Tariq, 2013).

5.2.1. Youth Entrepreneurs Experienced and Challenges in Accessing Financing Assistance from Financial Institutions

From the survey, it shows that only 36% of youth entrepreneurs had applied for financing assistance from financial institutions while 64% did not apply for financing assistance from financial institutions. The low percentage of youth entrepreneurs accessing bank financing is in line with the findings of Chik et al., (2015), Khan et al., (2015) and a survey conducted by Khazanah Research Institute (2018). 36% of youth entrepreneurs who had applied financing support from financial institutions were also requested to indicate their experiences with regard to applying and obtaining financing assistance from financial institutions and it can be easily concluded that all the 36% of youth entrepreneurs had encountered difficulties in applying and obtaining financing assistance from financial institutions. Youth entrepreneurs who had encountered difficulties in applying and obtaining loan from financial institutions were asked further to indicate what challenges they faced during the process of applying and obtaining financing from financial institutions. The questionnaire in this part was purposely designed with multiple selections as the researcher believes most entrepreneurs faced more than one challenges in accessing financing from financial institution. Those challenges according to their responses are presented in Table 4.

Challenges in Accessing Financing from Financial Institutions	Frequency	Percentage
Track Records	45	48.0%
Long Loan Processing Time	36	38.7%
Business Plan	35	37.6%
Stringent Requirement	34	36.5%
High Interest Rate	33	35.4%
Collateral	26	27.9%
Cost of Transactions	22	23.6%
Lack of Relationship with Financial Institutions	9	39.1%
Insufficient Amount Approved	8	8.6%
Viability of Business	3	3.2%

Table 4: Challenges in Accessing Financing

The three main challenges cited by youth entrepreneurs are lack of track record, long loan processing time and lack of convincing business plan. Of these three, most of youth entrepreneurs feel that the biggest problem they faced is the lack of track record. This is consistent with Zamzam (2017), when youth entrepreneurs in Egypt find it is difficult to provide solid track records in order to present their trustworthiness. In Malaysia, majority of the financial institutions tend to adopt the 5'C's strategies as one of the common evaluation techniques in assessing the creditworthiness of an entrepreneur. In this strategy, track records are among the main factors considered by financial institutions when evaluating business financing (Harif et al., 2011).

5.2.2. Reasons for Not Applying Financing Assistance from Financial Institutions

64% of youth entrepreneurs who did not apply for financing assistance from financial institutions were required to indicate the reason that prevented them from approaching financial institutions. Table 5 below presents a summary of the results.

Reason for Not Choosing Financing Assistance from Financial Institutions	Frequency	Percentage
Interest rate	81	48.5%
Could not meet bank requirements	63	37.7%
Lack of track records	52	31.1%
Lack of convincing business plan	40	23.9%
Lack of collateral	25	14.9%
Lack of Relationship with Financial Institutions	21	12.5%

Table 5: Reason for Not Choosing Financing Assistance from Financial Institutions

Based on the results, the most important reason as to why youth entrepreneurs had not applied for financing from financial institutions was high interest rate. There might be two reasons regarding this matter; either the interest rate charged is beyond the capability of youth entrepreneurs or due to religion factor. Consistent with study revealed by Gitari (2012), interest rate is a financial burden that prevents entrepreneurs from applying for financing support from financial institutions.

6. Conclusions

The research's main aim is to find out youth entrepreneur's specific challenges in accessing financial assistance from financial institutions so that the appropriate financial instruments can be developed to solve the issues of youth entrepreneur in accessing financing from financial institutions. The findings showed thatonly 36% of youth entrepreneurs had experience in assessing financing assistance from financial institutions and they indicated that the process in applying and obtaining financing from financial institutions is difficult. Among their challenges are lack of track record, long processing time, lack of promising business plan, stringent requirements and high interest rate as their top five challenges encountered by youth entrepreneurs. Meanwhile, for those youth entrepreneurs (64%) who had never applied for financial assistance from financial institutions stated that high interest rate, could not meet bank requirements, lack of track records, lack of convincing business plan and lack of collateral as the reasons for them not applying financing assistance from financial institutions. Thus, this study provides evidence that youth entrepreneurs in Malaysia are getting very little financial assistance from financial institutions. Due to the above challenges, it may limit the potential of youth entrepreneurs to grow and develop.

Practically, the findings of this research provide information to Malaysian government to pro-actively understand the specific financing challenges facing youth entrepreneurs and implement appropriate financing instruments to facilitate youth entrepreneurs financing need. Youth entrepreneurs need a youth-focused financing solution which is more accessible to them and offer lower cost of capital as compared to the financial institutions. Theoretically, since there are limited studies conducted in the area of youth entrepreneurs financing, the findings will expand the existing literature particularly in Malaysia. It will provide new empirical evidence on the topic of access to finance as this study expands the financing avenue for youth entrepreneurs through designing a youth-focused financing instrument as alternative financing mechanism for youth entrepreneurs.

There are several limitations when conducting the current research. Firstly, the unit of analysis of this study was restricted to youth entrepreneurs who are at the early stage of life-cycles and ignored other components of SMEs in other life-cycle stages. Secondly, the sole focus on youth entrepreneurs that participated in the three main organizations may limit the generalizability of the findings. Despite these limitations, the present study has successfully accomplished its research objectives and has made important contributions theoretically and practically.

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