

WORKING CAPITAL FINANCING PREFERENCE AMONG SMALL BUSINESSES IN CAMBODIA

Muhammad M. Ma'aji¹⁺, Phouneta Sok² and Chanramy Long³

¹ CamEd Business School, Phnom Pehn, Cambodia

² Royal University of Law and Economics (RULE), Cambodia

³ Ernst & Young (Cambodia) Ltd, Cambodia

+ Corresponding author: muhammad@cam-ed.com

Abstract

The purpose of this paper is to investigate working capital financing preference among small businesses in Cambodia using a quantitative and qualitative approach. Small business often relies heavily on internal finance as a major source of short-term finance for working capital needs. This is because small businesses are likely to face problems associated with their size when accessing external finance, such as information asymmetry and higher agency costs. Interestingly, using descriptive statistics and inferential statistics, the findings lead us to believe that these firms mostly relied on internal sources (retained profit, early settlement discount, delayed payment to suppliers) of finance as compared to external sources (bank loan and equity). In some cases, they have to rely on informal sources (private, family, friend, money counting/lenders, funds/wealthy families, rotating savings and credit associations) to finance working capital requirement. These results suggest that firms experience significant information costs that prevent them from gaining access to traditional sources of financing. The findings of the study will be useful to the financial institutions that fund SMEs and can help the policymakers to formulate strategies and programs that will support SMEs at different stages of the financial chain in Cambodia.

Keywords: *working capital finance; small business; financing preferences; pecking order*

JEL Codes: *G30; G39*

Received 11 Apr 19. Revised 4 Nov 19. Accepted 5 Dec 19.

Introduction

Every business needs adequate liquid resources to maintain the day-to-day cash flow. It needs enough to pay wages, salaries, accounts payable, and other liabilities if it is to keep its workforce and ensure its supplies. Therefore, money is needed to fulfill these transactions. This term of event is known as the financing of working capital (WC). Maintaining adequate WC is not just important in the short term. Adequate liquidity is needed to ensure the survival of the business in the long term. Even a profitable company may fail without adequate cash flow to meet its liabilities. Working capital refers to the resources a business needs to carry out its operation smoothly in the short term. Good management of WC increases the level of a company's liquidity and greatly reduces the risks of insolvency of the company. Firms in different industries have different requirements of WC; thus, businesses can determine the ideal level by comparing the current results with those in previous years or with other businesses that operate in the same industry. Therefore, choosing a way to finance WC is a financing decision that finance managers will have to deal with, and it is crucial to the long

term success of any company because it is a part of the investment in total assets that requires an appropriate financing investment (Bhunia, 2010).

Businesses fund working capital in different ways. This can be achieved by employing long-term and short-term sources of funding. Long-term sources of funds consist of capital (equity from owners) and long-term debt. According to finance theory, non-current (fixed) assets and some part of permanent current assets are long-term assets from which an organization expects to derive benefit over a number of periods and, as such, should be supported by long-term financing (Gitman, 2000). In this case, a company is said to be adopting a conservative WC policy. The policy of holding high levels of WC aims to reduce the risk of insolvency and, at the same time, ensure smooth operations with no stoppages to achieve a high level of customer satisfaction. On the other hand, short-term sources consist of trade credit, short-term loans, bank overdrafts, tax provisions, and other current liabilities that can be used to finance temporary working capital needs. Some part of permanent current asset and fluctuating current assets, which vary according to normal business activity, should be financed using short-term funds. In this case, a firm is said to be adopting an aggressive WC policy (Bhattacharya, 2001). Short-term sources of funding are usually cheaper and more flexible than long-term ones. However, short-term sources are riskier for the borrower, as interest rates are more volatile in the short term, and they may not be renewed. Therefore, easy access to finance plays an important role when businesses select the sources of financing for WC, and the trade-off between risk and return that occurs in policy decisions cannot be ignored (Gitman, 2000). Thus, effective working capital management lies at the heart of a successful company, playing a crucial role in increasing shareholders' wealth and the achievement of benefits from capital investment. In fact, poor management of working capital is one of the more common reasons for corporate failure. It is, therefore, essential that company managers have an understanding of this key area of corporate finance.

Pecking order theory by Myers (1984) explains the financing preferences of listed companies; however, the theory is equally applicable to small firms. Small businesses often rely heavily on trade credit as a major source of short-term finance for WC needs. This is because small businesses are likely to face problems associated with their size when accessing external finance, such as information asymmetry and higher agency costs (Burcu, 2018). As a result, small firms prefer to use internal financing first. This is followed by accessing credit, and then issue equity is the last resort. Accordingly, medium-sized textile firms with limited access to the long-term capital markets tend to rely more heavily on owner financing, trade credit, and short-term bank loans to finance their operations (Olomi, 2008). The few studies that have addressed the financing and capital structure of SMEs are mostly conducted in developed countries (Watson & Wilson, 2002; Zoppa & McMahon, 2002; Hussain & Matlay, 2007); only a few addressed the topic in developing countries (Aidis, 2005; Bhaird & Lucey, 2011). Research into this area for small developing economies is scant, particularly research that investigated the working capital finance of SMEs. Therefore, this paper investigates the working capital finance practices of small businesses in an attempt to bridge this gap and add to the growing literature on the financing decisions of SMEs.

In recent years, small businesses are viewed as one of the leading contributors to the national economic development in creating employment opportunities, developing indigenous skills and technologies, building market competitiveness, and realizing a poverty-free society. More than 95 percent of the established enterprises across the globe are SMEs, contributing approximately 60 percent of the private sector manpower (Ayyagari, Demirgüç-Kunt & Maksimovic, 2011). In general, the contribution of SMEs has triggered state and regional

initiatives to further strengthen the growth of small businesses around the globe (EU, 2013). As such, most policymakers consider the health of the SME sector to be highly important to an economy. Cambodia is not an exception to this concern as between 2000 and 2011, the number of SMEs increased by 268 percent. Of the 510,000 registered firms in Cambodia, more than 90 percent were SMEs (Pisei, 2019), generating 50 to 98 percent of the total employment (Forsinetti, 2012). However, despite their significant contributions to the overall economy of Cambodia, one of the impending challenges SMEs face is getting the relevant access to finance and support in various aspects. Limited access to finance is one of the predominant challenges for these enterprises. According to World Bank data, as shown in Figure 1, only 1 percent of SMEs' investments were financed by banks in 2016 compared to 4 percent in 2013. This is remarkably below the average in lower-middle-income economies, which is around 12 percent. Additionally, the percentage of firms using banks for investment financing also declined: 2.5 percent in 2016 compared to 8 percent in 2013, and is significantly lower than the average of comparator economies (22%) (World Bank, 2016). This is because many entrepreneurs are discouraged or even unable to take out loans due to high levels of requirements, high-interest rates, and delays in processing loans (Fuentes, 2018).

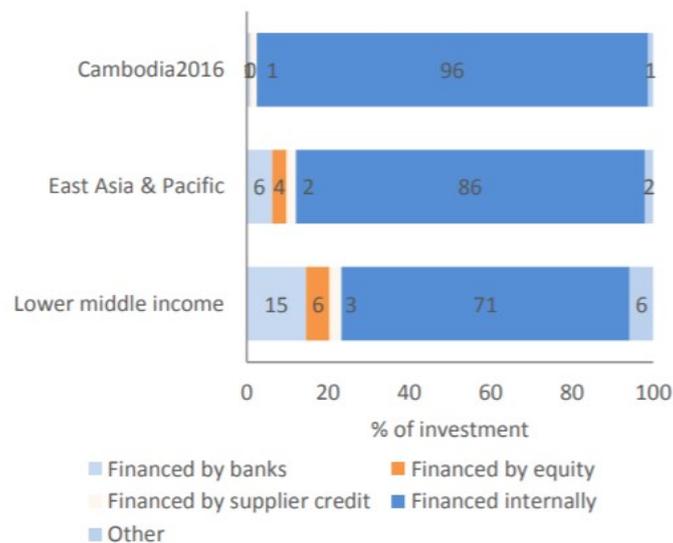


Figure 1: Sources of financing for purchases of fixed assets
Source: World Bank (2016)

The objective of this study is to examine the working capital financing preferences of small businesses in the manufacturing sector from diverse industry groups. The second objective of this study is to identify the main factors influencing the demand for WCF from the sample firms and highlight the use of informal sources of financing. The paper is organized into four main sections. The primary literature surrounding the topic is discussed, and the methodology is described along with the profile of the interviewees. After that, the results are discussed and the implications for practitioners and policymakers are highlighted.

Literature Review

Long-term investment and financing decisions give rise to future cash flows which, when discounted by an appropriate cost of capital, determine the market value of a company. However, such long-term decisions will only result in the expected benefits for a company if attention is also paid to short-term decisions regarding current assets and liabilities. Thus, current assets and liabilities are assets and liabilities with maturities of less than one year and

need to be carefully managed. This is because a company must have or be able to generate enough cash to meet its short-term needs if it is to continue in business and make sure idle funds are efficiently managed to reduce the opportunity cost. Net working capital is the term given to the difference between current assets and current liabilities: current assets may also include inventories of raw materials, work-in-progress and finished goods, trade receivables, short-term investments, and cash. On the other hand, current liabilities may include trade payables, overdrafts, and short-term loans. The level of current assets is a key factor in a company's liquidity position. A company must have or be able to generate enough cash to meet its short-term needs if it is to continue in business. Therefore, working capital management is a key factor in the company's long-term success: without the 'oil' of working capital, the 'engine' of non-current assets will not function. The greater the extent to which current assets exceed current liabilities, the more solvent or liquid a company is likely to be, depending on the nature of its current assets.

In many countries, empirical studies have indicated that small business managers experience problems in raising capital for the development of their businesses. Different studies (e.g., Holmes & Kent, 1991; Winborg, 2000) have frequently referred to the concept of a financial gap to explain why many small businesses face this type of problem. Access to finance has been identified as a key element for SMEs to succeed in their drive to build productive capacity, compete, create jobs, and contribute to poverty alleviation in developing countries. Despite their dominant numbers and their importance in job creation, SMEs have traditionally faced difficulty in obtaining formal credit or equity. Hughes's (1997) study of the financial structure of large and small U.K. businesses found that small businesses tend to rely more on short-term debt in comparison with large businesses. The result showed that small businesses have a higher proportion of debt, such as trade credit. This is attributed to the fact that small firms face greater problems in attracting long-term debt than large businesses. However, the difference could also be explained by the mere preferences and attitudes of the business owner and the manager towards debt capital. The study of Bhaird and Lucey (2011) brought evidence that connected the life cycle theory to the financing of firms' capital structures.

Pecking Order Hypothesis

Pecking order theory was first suggested by Donaldson (1961), who went against the idea of companies having a unique combination of debt and equity to minimize the cost of capital. Donaldson (1961) argued that when companies become more profitable, the keenness for external financing reduces since internal funds would be available to execute long-term projects. If only internal finance proves insufficient, bank borrowings and corporate bonds become the preferred source of external financing. The least preferred source of financing is the issuance of new equity. These preferences are subject to the cost of issuance and the ease of accessibility of the sources of financing. Retained earnings are readily accessible with no issuance costs. As for the choice between debt and equity, the cost of issuing debt is lower than the cost of issuing equity. It is also possible to raise small amounts of debt, whereas it is not usually possible to raise small amounts of equity (Donaldson, 1961).

Myers (1984) extended Donaldson's (1961) pecking order theory by postulating that the cost of financing increases with asymmetric information. He proposed that the order of preference stems from the existence of asymmetry of information between the company and the capital markets (Myers, 1984). Pecking order theory starts with asymmetric information as managers know more about their companies' prospects, risks, and value than outside investors. Asymmetric information affects the choice between internal and external financing and

between the issue of debt or equity. Therefore, there exists a pecking order for the financing of new projects. For example, assuming that a company wants to raise funds for its new project, and the capital market has underestimated the benefit of the project. The company's managers, with their insider information, will decide to finance the project with retained earnings. This is because retained earnings are the least information that is sensitive to the source of financing. However, if retained earnings are insufficient, managers will choose debt financing in preference to issuing new shares, specifically when the market undervalues the equity. The issuance of equity would signal a lack of confidence in the board as they would feel that the share price is overvalued. The market would perceive it negatively, which may lead to a drop in the share price.

However, in the case of small businesses, the order would relate more to retain earnings and debt finance. This is because the majority of the firm managers tend to be business owners, and they do not normally want to dilute their ownership claim. Therefore, the theory's application to small businesses implies that external equity finance issues may be inappropriate. Furthermore, since small businesses are not listed in the stock market, the issuance of equity would mostly be internal equity finance that is among the existing managers (Zoppa & McMahon, 2002). This type of issuance would probably not surrender control.

Methodology

Financial and other information on small businesses is easily accessible in developed countries where government or private corporation databases provide such information (information provider or credit rating agencies). However, information on small businesses in developing countries is limited to government agencies databases as they are not required to make their financial accounts publicly available. Therefore, data were collected as part of a comprehensive survey on the financial and working capital management practices of small businesses in Cambodian manufacturing firms. The study was confined to the manufacturing sector because working capital management is more significant in this sector than that in the service sector. Also, the manufacturing sector is an important sector of the economy in job creation and contribution to economic growth. The manufacturing, as well as other industrial sectors, account for 59 percent of the total GDP, while the services sector's contribution to the GDP is 41 percent (World Bank, 2016). The manufacturing sector, especially the garment industry, is the foremost driver of Cambodia's economic activity expansion. Thus, this led to the selection of the manufacturing sector as the subject of this study and, more specifically, companies within the Phnom Penh province. Phnom Penh is home to the majority of SMEs, where 51 percent, 61 percent, and 77 percent of the respective small, medium, and larger firms are located (World Bank, 2016).

A total of 58 questionnaires were distributed to the financial managers/CFOs/business owners because they are most likely to be involved in evaluating the working capital requirement of their respective companies. A simple random sampling was used to cull a smaller sample size from the population of SMEs in Phnom Penh. A cover letter attached to each questionnaire served as an introduction to the purpose of the survey and assured the confidentiality of the information supplied by each participant. The survey was conducted from July 2018 through January 2019. It must be noted that the Cambodian business community is not used to this type of survey. Despite their non-familiarity with survey instruments, the questionnaires were presented in-person, and appointments were scheduled in advance to increase the response rate. Thirty-two usable responses were received, giving a response rate of 55 percent, which is comparable to similar surveys. Therefore, this paper focuses on the financing variables and

examines the financing preferences of the firms requesting WC finance. Data collected were presented and analyzed using descriptive statistics and inferential statistics (including mean and percentage analysis) using the Statistical Package for Social Sciences (SPSS). Additional rigor in the analysis was possible through an interview conducted with eight of the survey participants. In the interview, data on the extent of trade credit, short-term borrowing, traditional sources (bank loans and bank overdrafts), equity finance, retained profits, and informal finance as sources of finance among the Cambodian manufacturing firms were gathered and examined.

Findings and Discussion

Descriptive Statistics

The findings of this study showed that, when it comes to WC financial decision-making, no small business is the same. All business owners have their own financial goals, concerns, perceptions, and funding sources. The financial issues of the participants and their background characteristics are summarized in Table 1. The survey instrument contained a number of variables to test for significant differences based on the firms' characteristics.

Table 1. Legal Entity and Ownership Type

Legal entity	No. of companies	% of companies	Ownership	No. of companies	% of companies
Sole proprietorship	18	55	Family owned	20	63
Partnership	11	35	Non-family owned	12	37
Private Limited Co.	3	10			
Total	32	100		32	100

Source: Survey Data

Ownership and Structure

The findings presented in Table 1 showed that 55 percent of small businesses are owned by sole proprietors, followed by partnership ownership accounting for 35 percent, while private limited companies represent 10 percent of the sample. Sole proprietorship ownership has become the common ownership structure among small businesses in Cambodia. The culture in Cambodia is that most people prefer to fully own their businesses or have people whom they know very well, such as friends, especially relatives, to join them because of trust issues and the fear of losing control of their enterprises. More so, they perceive it as being safer for their businesses. Furthermore, the majority of the companies (63%, n=20) are family-owned businesses, and some 37 percent (n=12) are non-family owned businesses. The informal and family organization of most SMEs in Cambodia constitutes a barrier for potential investors that find the lack of information and professionalism in Cambodian SMEs to be a major constraint (Forsinetti, 2012).

Size, Age, and Industry

The sample was spread across five main industry groups, as shown in Table 2. Sixty percent of the companies are in the textile and wearing apparel industries, 25 percent in the food products industry, while the remaining 15 percent are in the chemical products industry. The sampled companies were classified by the number of years they have been operating in the business. The years were classified into four categories as shown in Table 3. Based on the participants' feedback, 47 percent of the companies have been in business between 6 and 10

years (n= 15), 19 percent for more than 20 years, while 8 companies (25%) are considered to be newly established businesses that have been operating for less than 5 years. For long-established companies, operating in Cambodia market for many years will give them a competitive edge by becoming more efficient over time and gaining customers loyalty as firms discover what they are good at and learn how to do things better (Arrow, 1962; Jovanovic, 1982; Ericson & Pakes, 1995). It is also important for these companies to be specialized and find ways to standardize, coordinate, and speed up their production processes, as well as reduce costs and improve quality. This, in return, will enable the companies to make informed decisions on their working capital management.

Table 2. Type of Industry

Industries	No. of companies	% of companies
Wearing apparels	10	30
Food products	8	25
Furniture	-	-
Textile	10	30
Chemical product	4	15
Total	32	100

Source: Survey Data

The result showed that 25 percent (n=8) of the companies have total assets of over \$1 million, while 55 percent (n=18) has an asset base of between \$100,000 and \$500,000. However, 20 percent (n=6) have an asset base of up to \$100,000. For companies with a large asset base, the amount of assets group that the company holds is of significant focus. This is because the efficiency level of distribution and application of the assets influence the profitability and risk level of the firm in general.

Table 3. Classification of Companies by Age and Size

Age of Company	No. of companies	% of companies	Total Assets	No. of companies	% of companies
1 – 5	8	25	Up to \$100,000	6	20
6 – 10	15	47	\$100,000 to \$500,000	18	55
11 – 20	3	9	\$501,000 to \$1 million	-	-
More than 20	6	19	More than \$1 million	8	25
Total	32	100		32	100

Source: Survey Data

Financing Preferences

The sample firms were asked the reason why they require WC finance to help achieve the main objective of this study. Table 4 shows that 53 percent associate the need with irregular demand or increase demand for their goods. When a company is experiencing increased demand for their goods, usually they tend to invest more in its operation to meet the customers' demand. Hence, more WC financing will be required. The finding also showed that 40 percent of the sample firms believe that irregular payment of debtors is a major determinant of WC financing need.

Table 4. Reasons for the Need of Working Capital Finance

Reasons	No. of companies	% of companies
Irregular demand or increase demand	17	53
Irregular production	2	7
Irregular payment of debtors	13	40
Irregular delivery by creditors	-	-
Fluctuating policies of the government	-	-
Total	32	100

Source: Survey Data

Furthermore, the participants were asked questions about the WC policy, and their responses regarding these different policies provide an indication as to their financing pattern or what their financing preference will likely be. In financing their working capital, the companies undertake different approaches. According to the responses, 50 percent (n=16) use an aggressive approach, 40 percent (n=13) use a conservative approach, and the remaining 10 percent use the matching approach (Table 5). On the one hand, the conservative approach bears a low risk and low profitability as the working capital is mainly financed by long-term finance sources that require higher interest payment. On the other hand, the aggressive approach mainly uses short-term funds to finance working capital. Therefore, it bears high liquidity risk along with high profitability. It is not surprising for small businesses to adopt an aggressive policy of WC as the majority of them rely on short-term sources of finance. Short-term sources could provide potential benefits or cost-saving to small businesses, some of which are the nominal interest rate on short-term debt and are generally lower than the interest rates on long-term debt. Furthermore, using short-term debt, firms will be able to borrow only the amount needed for the period, and, therefore, the interest cost is only paid on the money that is actually used (Burcu, 2018). This is especially important for firms that have seasonal fluctuations in their current assets. However, this policy represents an increased risk of liquidity and cash flow problems. In addition, potential returns will be increased if short-term financing can be obtained more cheaply than long-term finance.

Table 5. Working Capital Policies

Policies	No. of companies	% of companies
Aggressive approach	16	50
Conservative approach	13	40
Matching approach	3	10
Hedging approach	-	-
Total	32	100

Source: Survey Data

The sample firms were also asked about their sources of funds used during the start-up phase and financing their current needs. Consequently, their responses regarding these different sources of funds should provide an indication as to whether the financing pattern follows a pecking order. Small businesses use different financing patterns at various stages of the business cycle. As previously indicated, prior studies suggest that small businesses tend to use private sources of financing at the start-up due to the difficulty of accessing external sources of funds. This is as a result of their inability to provide a viable business plan or collateral, especially at the start-up stage. Our results supported this notion. The findings in Table 6 show that 47 percent (n=15), which is the majority of the start-up funds for small businesses in Cambodia, comes from loans from family/friends, 41 percent (n=13) of the

funds comes from the owner's savings, while 12 percent of the funding comes from bank loans and compensation received from the previous job. The survey results demonstrated a clear preference for using loans from family and friends and the owner's savings to finance the start-up phase. Consistent with the literature (Beck, 2007), the findings showed that venture capitalists and business angels are not common sources of funds at the start-up stage of small businesses in Cambodia. This could be because businesses at the start-up stage are in a conceptual phase and exist only on paper, and there are few in Cambodia. The findings also showed a lack of government support initiatives on small businesses at the start-up stage.

Table 6. Start-up Capital Sources

Sources	No. of companies	% of companies
Compensation from previous job	2	6
Owner's savings	13	41
Loan from family/friends	15	47
Bank loans	2	6
Empowerment fund from Government	-	-
Start-up grant scheme	-	-
Business angels	-	-
Bank overdraft	-	-
Trade credit from suppliers	-	-
Venture capitalists	-	-
Total	32	100

Source: Survey Data

The survey results in Table 7 demonstrated that small businesses rely mostly on retained profit with the lowest mean score of 1.56. This indicates that it is the most preferred source of financing the current WC needs. The second most preferred source is by offering trade discounts to customers to encourage early settlement with a mean score of 2.41. Also, receiving payment from customers on time will reduce the amount of investment that will be required to finance receivables, thus reducing the WC requirement. Small businesses in Cambodia also use suppliers' funds to finance working needs by delaying payments with a mean score of 2.87. This would enable the companies to fund some of their working capital requirement without the need for external funding. In some literature, this financing pattern is known as bootstrap financing (bootstrap finance includes trade credit, leasing/hire purchase, gift/grants, and selling of properties) (Eric, Godfred, & Daniel, 2012). Short-term borrowings (bank overdrafts and bank loans) are also used (but ranked below the internally generated source) to finance the current needs of the business. The participants perceive that financial institutions insist on collateral as part of their short-term borrowing. This finding is consistent with that of Chittenden and Hutchinson (1996), where access to short-term and long-term debt for SMEs was found to be strongly related to collateral. Therefore, firms that have low fixed assets base and or more intangible assets would find it difficult to access bank loans (Myers, 1984). The findings also showed that the least preferred source to fund WC is by issuing more equities.

Table 7. Sources of Finance for Current Needs

	Sources	Mean Rank
1	Retained earnings (reinvest the profits from operations)	1.56
2	Trade discounts for customers to make prompt payments	2.41
3	Trade credit (delayed payment to suppliers)	2.87
4	Bank overdraft	3.61
5	Short-term bank loan	4.75
6	Sell some of the fixed assets	5.10
7	Long-term bank loan	5.56
8	Issue more equity finance	5.79

Source: Survey Data

This evidence is consistent with Myer's (1984) pecking order, in that firms would generally use retained profits, followed by debt and, as a last resort, raise external equity capital. These findings accord well with previous studies (Hussain & Matlay, 2007). Among the common reasons cited for the observed financing preferences of SME owners is the desire for independence and to maintain control of their enterprise (Chittenden & Hutchinson, 1996; Padachi, Howorth, & Narasimhan, 2012). The reluctance to dilute control is confirmed by the survey results, where the business owners and managers consider issuing equity as a last resort. Another possible reason why firms in Cambodia prefer internally generated sources compared to externally generated sources is because small businesses have difficulties in arranging for acceptable collateral. As high as 90 percent of the participants perceive that financial institutions insist on collateral as part of their short-term and long-term borrowings. For example, in Cambodia, small businesses will need to have Hard Titles¹ to be able to use the titles as collateral for loans, which are subject to heavy taxation and costs (tax on profit, VAT, and formal accounting). Furthermore, the findings indicated that smaller firms are having difficulties to negate the problem of information asymmetries. Therefore, it is apparent why small businesses will prefer to use more internally generated sources to finance the WC requirement.

¹ Hard title is the strongest form of property ownership in Cambodia and the best Cambodia Land Title. Banks in Cambodia usually require this type of title for loans.

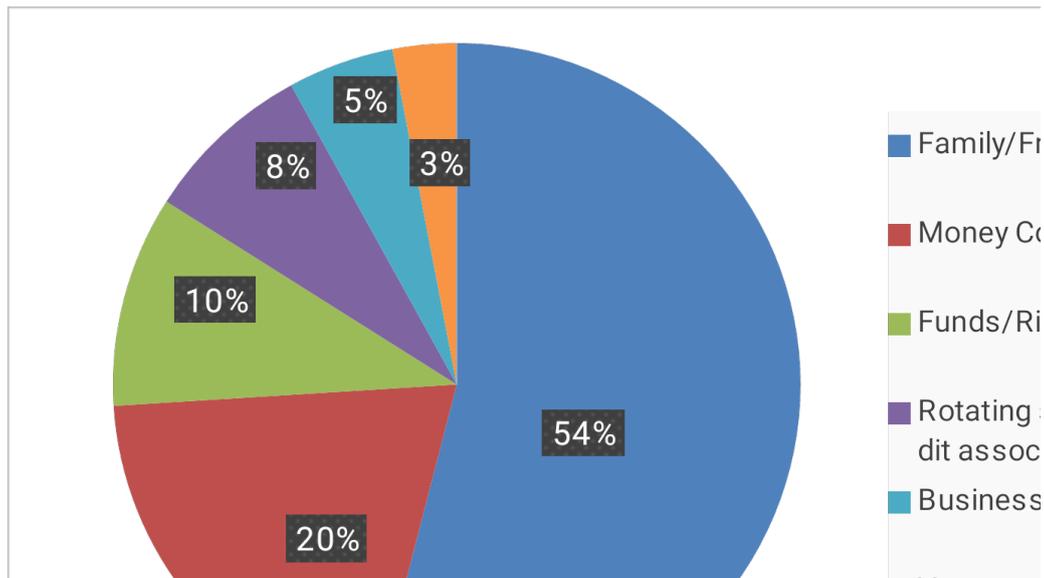


Figure 2. Informal sources of financing working capital

Informal Sources

The literature review highlighted the importance of informal investment as a major solution to the problem that the traditional sources of finance are often inaccessible by small firms. From the explorative interviews, conducted with eight business owners and managers, a number of informal sources of financing working capital were identified among Cambodian small businesses. The finding (Figure 2) indicated that the structure of informal financial sources for small entrepreneurs in Cambodia is predominated by “love capital” (mainly private, family, and friend savings), money counting/lenders, funds/rich families, rotating savings, and credit associations, while the percentage of business angels and venture capital financing is low. According to some of the participants:

It is difficult here for companies like ours to have access to finance from banks and other financial institutions easily as they require a lot of paperwork (business plan, collateral or guarantors, etc.) in order to obtain a loan from them. So, most of the time, if there is not enough money in the business, we used funds from family members or a friend through a simple agreement as we have a personal relationship and do not need any formal introduction. In comparison to banks and other formal sources, family/friends normally have fewer requirements (Participant 1, 2, 3, 4, 8).

Similarly, participant Company 1, 3, 5, 6, 7 said:

We found money counting/lending as an alternative way for us to finance our day-to-day operations as it is easy and very fast to secure loan money from a lender with a daily installment payback rate. Though money counting/lending bears a high-interest rate from 15 percent to 30 percent, it helps us as business owners to meet our business needs. Because borrowers and lenders are typically acquainted with one another, it makes it like a home-free run for us to borrow without black and white agreements (Company 1, 3, 5, 6, 7).

Ultimately, the key evidence of the mentioned analysis is that in Cambodia, informal financing is oriented to borrowers who have some kind of personal relations with lenders or know each other very well. The finding also showed that small businesses that attract informal financing in Cambodia prefer substantially internal sources (private, family, and

friends' money) in comparison with external money counting/lending, business angels, and venture capital investments.

Conclusion and Implications

This paper has shown, to some extent, that small businesses in the Cambodia manufacturing sector face difficulties in getting access to financing working capital. The findings indicated that these firms mostly rely on internal sources of finance as compared to external sources. In some cases, however, they have to rely on informal sources to finance the working capital requirement. Major forms of financing working capital requirements preferred are current liability, cash credit, retained earnings, and equity/long term loans. Besides, the study found that some companies do not have any specific method in determining working capital requirements. Therefore, a conclusion can be drawn that, in Cambodia, companies prefer internal sources of finance and current liability for financing their working capital. Currently, working capital management remains a fairly new concept as there are a number of small companies in Cambodia that do not have clear policies of how it is practiced.

The findings of this study could become a very important tool for business owners and managers to understand the best way to manage their working capital finance needs based on the type of their businesses and structure. The Royal Government of Cambodia (RGC) should consider passing a law on the use of movable assets (such as vehicles, machinery, livestock, account receivables, among others) to be used as collateral for small businesses to enhance access to credit. The Rural Development Bank (RDB), established as an autonomous public enterprise to support SMEs in loan services, could also use the findings to help formulate a program to support small businesses at different stages of the financial chain. This support should, therefore, include a process to help them transition from an informal to formal status and provide them with management and governance support to better understand and improve their businesses. The use or set up of dedicated agencies to provide that support would definitely be crucial to small businesses in Cambodia.

Acknowledgement

This research is fully supported by CamEd Business School, Phnom Pehn Cambodia. Therefore the authors wish to express gratitude to CamEd Business School for their financial support.

References

- Ayyagari, M., Demirgüç-Kunt, A., & Maksimovic, V. (2011). *Small vs. young firms across the world – Contribution to employment, job creation, and growth*, Policy Research Working Paper 5631 (The World Bank Development Research Group).
- Aidis, R. (2005). Why don't we see more small- and medium-sized enterprises (SMEs) in Lithuania? Institutional impediments to SME development. *Journal of Small Business Economics*, 25(4), 305–317.
- Arrow, K. (1962). The economic implications of learning by doing. *American Economic Review*, 29, 155-173.
- Beck, T. (2007). *Financing constraints of SMEs in developing countries: Evidence, determinants and solutions*, KDI 36th Anniversary International Conference, Retrieved, from https://pure.uvt.nl/portal/files/1107677/Financing_Constraints_of_SMEs.pdf
- Bhaidr, C. & Lucey, B. (2011). An empirical investigation of the financial growth lifecycle'. *Journal of Small Business and Enterprise Development*, 18(4), 715–731.
- Bhattacharya, H. (2001). *Working capital management: Strategies and techniques*. New Delhi: Prentice Hall.
- Bhunia, A. (2010). A trend analysis of liquidity management efficiency in selected private sector Indian steel industry. *International Journal of Research in Commerce and Management*, 1(5), 618–628.
- Burcu, D. (2018). *Financing of Working Capital Requirement and Profitability: Evidence from Borsa Istanbul Chemical, Petroleum, Rubber, and Plastic Sector*. Chapter 9, Financial Management from an Emerging Market Perspective. Pp. 175 – 187.
- Chittenden, F., Hall, G., & Hutchinson, P. (1996). Small firm growth, access to capital markets and financial structure: A review of issues and an empirical investigation. *Small Business Economics*, 8, 59–67.
- Donaldson, G. (1961). *Corporate debt capacity: A study of corporate debt policy and the determination of corporate debt capacity*, Boston: Division of Research, Harvard School of Business Administration.
- Ericson, R. & Pakes, A. (1995). Markov-perfect industry dynamics: A framework for empirical work. *Review of Economic Studies*, 62, 53-82.
- Eric, O.A., Godfred, A.B., & Daniel, K.T. (2012). "Microenterprise financing preference: Testing POH within the context of Ghana's rural financial market", *Journal of Economic Studies*, 39(1), 84-105.
- EU (2014). A recovery on the horizon? Annual report on European SMES 2012/2013.
- Fuentes, S. (2018). *SMEs and funding in Cambodia: An overview*. Geeks in Cambodia, available at <http://geeksincambodia.com/smes-and-funding-in-cambodia-an-overview/>
- Forsinetti, C. (2012). *Financing SMEs in ASEAN, the case of Cambodia*. The Phnom Penh Post <https://www.phnompenhpost.com/post-plus/financing-smes-asean-case-cambodia>.
- Gitman, L. J. (2000). *Principles of managerial finance*, (9th Ed.). Reading, MA: Addison Wesley & Longman.
- Holmes, S. & Kent, P. (1991). An empirical analysis of the financial structure of small and large Australian manufacturing enterprises. *The Journal of Small Business Finance*, 1, 141–154.
- Hughes, A. (1997). Finance for SMEs: A UK perspective. *Small Business Economics*, 9, 151–166.
- Hussain, J. & Matlay, H. (2007). Financing preferences of ethnic minority owner/managers in the UK, *Journal of Small Business and Enterprise Development*, 14(3), 487–500.
- Jovanovic, B. (1982). Selection and the evolution of Industry, *Econometrica*, 50, 649–670.
- Myer, S. (1984). The capital structure puzzle. *The Journal of Finance*, 39(3), 575–592.

- Olomi, D. R. (2008). *Demand assessment for micro finance services in Zanzibar with a gender perspective*. Report submitted to the International Labour Organisation (ILO), Dar es Salaam.
- Padachi, K., Howorth, C., & Narasimhan, M. (2012). Working capital financing preferences: the case of mauritian manufacturing small and medium-sized enterprises (SMEs). *Asian Academy of Management Journal of Accounting and Finance*, 8(1), 125–157.
- Pisei, H. (2019). *Ministry: SMEs vital to economy, but 95% not registered*. The Phnom Penh Post, available at <https://www.phnompenhpost.com/business/ministry-smes-vital-economy-95-not-registered>
- Watson, R. & Wilson, N. (2002). Small and medium size enterprise financing: A note on some of the implications of a pecking order. *Journal of Business Finance and Accounting*, 29(3/4), 557–578.
- Winborg, J. (2009). Use of financial bootstrapping in new businesses: a question of last resort? *Venture Capital: An International Journal of Entrepreneurial Finance*, 11(1), 71–83.
- World Bank (2016). *Enhancing export competitiveness: The key to Cambodia's future economic success*. World Bank Group, available at <http://gs.mef.gov.kh/contents/uploads/2016/10/October-2016-Cambodia-Economic-Update-Oct-10-2016-final.pdf>
- World Bank (2016). *Enterprise surveys: Cambodia 2016 country profile*. World Bank Group, available at <https://www.enterprisesurveys.org/content/dam/enterprisesurveys/documents/country-profiles/Cambodia-2016.pdf>
- Zoppa, A. & McMahon, R. (2002). *Pecking order theory and the financial structure of manufacturing SMEs from Australia's business longitudinal survey*. Research paper series: 02–1, The Flinders University of South Australia.