

Social Trust on the Use of Trade Credit: A Major Hinderance to the Growth of MSMEs

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Abstract

Micro, Small and Medium Enterprises (MSMEs) is one of the mechanisms that drive economic growth. Only little attention has been given to sociology-business relationship. The main purpose of this article.to bring to the public the awareness on the issue of social trust and why it affects the offering of trade credit to MSMEs, as numerous of these MSMEs lack capital or requirement to secure formal loans which is a major problem among other factors faced by businesses that offer trade credit to MSMEs within African region. Countries most especially developing ones that have low social trust tend to have low economic growth. It was found that even with all the factors that affect the use of trade credit by MSMEs most new MSMEs still struggle to raise capital for their businesses and many fall out of business in the first five years and quantitative research needs to be carried out to see the level of influence, social trust has caused to the development of MSMEs in Africa countries.

Keywords: Social trust, trade credit, hindrance, growth, MSME

1.0 INTRODUCTION

Micro, Small and Medium Enterprises (MSMEs) has been identified as one of the mechanisms that drive economic growth therefore should not be neglected under any circumstance and needs proper funding in order to meet up with its proposed mission. There are several factors that determines the success of MSMEs, in a quick remind, every business needs capital at different stage of business. The main reason why MSMEs drives the economy is that it creates jobs thereby improving Human Development Index (HDI) as well as Gross Domestic Produce (GDP). SME contribute less than 20% to GDP in Africa compared to 40% in Asian countries and 50% in the US or Europe which shows large gap in the development of MSMEs in Africa. Despite the increase in the number of MSMEs and Governments' effort in west Africa nations on the frequent micro loan schemes, it is of great surprise that it only makes very less significant impact to Africa countries' GDP. Could it be that the micro loans are not readily available? To what extent does trade credit contribute to MSMEs? Are those MSMEs wishing to receive trade credit having proper information about their businesses? Several factors might be contributing to the reasons why offering of trade credit to most MSMEs within the Africa region may be very crucial.

Many researchers have shown that size, age, growth rate, ownership etc. among all the factors that has been researched, very little attention has been given to the issue of trust in business dealings within the African coast.

2.0 LITERATURE REVIEW

A lot of researches have been done on social trust across various disciplines such as sociology. Looking at social trust from business perspective is quite interesting to know that trust on payment of trade credit by MSMEs that lack collaterals for formal loan application is of great importance. In developing countries such as South Africa, MSMEs has been a major driver of economic as it contributes towards unemployment eradication as well as improving the well-being of the people (Otto 2018). For these reasons, a lot has to be done in strengthening MSMEs through financing in ensuring growth in the sector SME sector in Ghana perceives difficulties in obtaining formal loan which has led to sourcing for alternate source (Quartey et al 2017) and as a result of that, the adopting of trade credit as a means of financing business has become usual.

2.1 TRADE CREDIT EFFECT ON MSME GROWTH IN AFRICA

Research shows that trade credit has relationship with profitability and has attracted researchers to embark on researches in view of how this affects the economics of developing countries. It is very advantageous for MSMEs when trade credit is granted to them because trade credit is cost saving as it offers possibility of paying later for goods received from its creditors after sales (Chludek, 2011) Trade credit has resemblance of loan, but exchange is made in form of goods and services, when firm A receives goods from firm B, firm A enters an agreement that specifies a date to which the total worth of the goods is due for payment to firm B The agreement here is usually entered based on trust between trader credit offer or and receiver (Usually MSMEs). For the fact that most MSMEs are owned and managed by owners and they do not have the required managerial skill to properly manage the business, knowing that most of these owners got themselves into running businesses due to Social, environmental and economic pressure.

Adebisi and Gbegi (2013) show that in the first five years of formation of SMEs, 80% of them fail in achieving success; they are likely to shut-down operations and create bad debt to their creditors or delay in settling their debt. Therefore, what happens when no collateral is tendered during contract and trade credit is issued to business owners or management that appears to have little or no credibility?

Trade credit as a source of financing MSMEs plays important role in financial management as it pave way for business growth if and only if suppliers or manufacturers who offer trade credit take much time to do proper research about the trustworthiness of the small business owners or management. But how and at what level does one have to trust before offering trade credit to these modern MSMEs? Most MSMEs tend to neglect how they should manage working capital effectively; this could be due to their small size (Sunday, 2011). When MSMEs face poor management in using trade credit as a source of capital, the risk in offering this credit needs to be considered as well. Most institutions that offers credit to firms often rejects application from such MSMEs (Tagoe, Nyarko & Smurfit 2005).

2.2 WHY SOCIAL TRUST AFFECTS TRADE CREDIT

Research has shown that trust matters a lot in business especially trade credit dealings. Wu et al (2013) argue for and show that supplier's offers more trade credit quickly to customers that are sited in places where social trust is high compared to low social trust places. Therefore, high social trust has been linked to positive economic growth. Therefore, we should not neglect the fact that Social trust plays a very important role besides other determinants in doing business transaction or trade credit.

Martin, et al (2014), elucidates trust within the context of business as a key factor to organizational success and views it as a requirement for customer satisfaction. It is very advantageous to organization that earns trust. Trust among business partners or associates is not as easy as other factors that determines business deals because of the way trust is been measured.

Martin, et al (2014) trust has been viewed in four streams - generalized, institutional, reputation-based, and stakeholder trust. They added that public trust creates in-depth understanding of trust in business. Focusing on the stakeholder trust because most MSMEs are one-man businesses especially the micro enterprises, we all understand that human attitudes are different and could change at any point in time.

Researchers have not been giving much attention to problem of trust in securing business loans. Externally regulated behaviour such as size, age, growth rate and ownership etc., are not really enough to conclude how credible MSME owners could be. Some MSME especially the micro enterprises which are surviving most youths among Africa countries do not have better tracking information to show the worth of the businesses.

Oyedokun (2018) showing that Nigeria has less number of domestic investment and this aspect should be given more attention where by Government should give financial support through soft loans because loans are not easily granted to MSMEs, majority of the formal loans are granted to large companies and government affiliated organizations; regarding Nigeria as the country that has weak overall support from Government. Meanwhile, different credit schemes for MSMEs are set from time to time without extending the benefits to most of the new or existing entrepreneurs.

Generally, a lot of problem has been traced to influence social trust in a negative direction which makes it critical for trade credit to be offered to MSMEs. Corruption that exist across various sectors where benefit is pledged for tempering a lay down system or procedure; where peoples' need are not fully met and tends to breakdown laws and orders for their comfort or interest by any means. Economic inequality is on the increase where people feel marginalized; where there is large margin between the rich and poor and many not listed here and in a society where all these circumstances become order of the day.

Martin.(2019) there is definitely a decline in social trust. Where trust is minimal should we consider size, age, growth rate and ownership as main determinants of trade credit offering? Even large firms that are tenderable still wind up. When trust is linked to trade credit, it gives us clear view of the willingness of firms that receives trade credit to settle their debt on time and this is regarded as trust by willing.

Social trust is seen as a culture as it varies among countries, ethnics, individuals and institutions. Majority of those who participated in a research done by Fritz et al (2018) declared that private institutions has less trustworthiness when compared with public institutions as this also refers to stakeholder's trust. There tends to be low social trust in places where violence is high as in the case of South Africa regarding xenophobia (Putnam 2007; Dinesen and Sønderskov 2018) in an argument that ethnic diversity destroys trust in many ways; It does not really mean that it does not impact social trust. The level of social trust could be affected by migrants of the opposite level of social trust and interacts with workplace organization which could also affect economies in the aggregate (Hoorn 2017).

3.0 METHODOLOGY

Researches that reveal factors that determine the use of trade credit and how it affects growth of SMEs in developed and undeveloped countries were extracted from search engines such as google search, google scholar, science direct; etc., keywords related to the topic of this paper was searched individually. “Trade credit contribution to MSME growth in Africa” was searched on google, the result displayed was about 7,590,000, while “Why Social trust affects trade credit” was searched on google scholar, Emerald insight, and SpringerLink result shows 17,600, 1,000 and 5,875 respectively; Only few articles that relates to social trust and trade credit on MSMEs were found. Most of the researches on social trust were done within the context of sociology. The incorporation of sociology and business in management of business relationship assist business entities to analyze business in a social dimension (Mandjak and Szanto 2010).

3.1 DISCUSSION

According to Lucey (2016), “75% of Irish SME’s use trade credit, as opposed to the European average of 50%” and have sustained Ireland during financial crises. The reverse of the benefit tend to be the case where the governments fails to invest in economic development particularly MSMEs, both skilled and unskilled people are taking stands to innovatively create jobs for their survival and has led to widespread of Micro businesses Adisa et al (2014) explore some of the challenges facing small businesses and finding out that small businesses in Africa are setup and managed by unemployed youths who see small businesses as their last hope which have given rise in the number of small businesses across the African continent, for example about 60% of all new businesses setup in Nigeria are on small scale (Femiwole, 2013 and Adisa et al, 2014) on the ontrary, most of those businesses are micro businesses. These micro businesses are in almost every street and have become major target to large companies in the

region, as helping them in distributing and promoting goods and services to the needy.

Often times, only few micro business owners benefit from these government micro loans schemes. Most business owners are left alone to fund their businesses. Discussing within the context of these selected factors: size, age, growth rate and ownership, although these factors varies from country to country, example in Ghana, size and gender of the management board are accessed. Quartey, et al (2017) explains that the higher the age of large business entity the easier it becomes for the firm to be able to secure more than 25% of its funds from external source due to the fact that they are able to tender collateral and adequate information to prove their credit worthiness; the fact in the research means if size is a determinant in securing business loan, would Micro and SMEs be able to raise sufficient capital for their businesses? Most large companies have higher chances of meeting their financial obligations even without external funding as they tend to have large number of customers or market network but the reverse is the case of MSMEs.

In a survey conducted by US International Trade Commission (USITC) among 46% of 850 large companies and 32% of 2,350 SMEs in some sector reported that they experienced problem while securing loan even when they have collateral. Specifically, 10% of large firms of US manufacturing sector while 17% per cent of large firm in the services sector reported similar problems and most SMEs in manufacturing sectors reported difficulties in securing loan and inflexibility in using alternative source of financing. (Azevêdo 2010,).

Many companies offers trade credit to MSMEs to help them in the distribution of their goods and services as they strive for growth because MSMEs have limited capacities to operate their businesses, being self-financed business and whatsoever that happens to the owner is likely to affect the business which is a major risk in offering trade credit to MSMEs. There is similar problem in trade financing, where banks find it difficult to issue letters of credit on behalf of

its customer (buyer) to the seller's bank. Social trust has very important role to play in most aspect of business ranging from fund raising to service delivery

SUMMARY AND CONCLUSION

Most researches based their evidences on several factors that determines the offering of trade credit due to the economic status of most developing countries, micro businesses becomes very rampant and there is sufficient information about businesses, therefore these MSMEs are finding it difficult to get formal loan from private and Government financial institutions.

Business institutions are taking advantage of trade credit to substitute for the formal loan in form of goods and services and even without collateral, trade credit are offered to these MSMEs base on trust that they would pay as when account payable is due. Researchers find trust to be a very important phenomenon in business transaction. Trust should be considered first in prioritizing the factors that influence trade credit offering.

While considering social trust as one key factor, a lot has to be done to ensure that high social trust is attained in African region suggesting those countries' leaders are able to exercise solid accountability and transparency to their citizens making it a better place, by fully engaging the people in handling or managing social and community challenges. There is a lot to be done by government and individuals in general in ensuring that they share common view towards fairness and justice as this would help to boost social trust; that is, when corrupt people and other criminals are brought to justice.

In view of the prevailing problem of social trust surrounding the using of trade credit as it affects MSMEs growth, quantitative research needs to be carried out to see the level of influence, social trust has caused to the development of MSMEs in Africa countries

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