

Effect of Corruption on Access to Finance for Market Pioneering in Nigeria: Evidence from Knowledge-Intensive Businesses

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Abstract

Finance is very crucial for the innovativeness of firms especially in pioneering new markets. Finance can be obtained from the formal and informal financial institutions. However, there is a growing concern about the prevalence of bribery and corruption as a menace in most developing economies especially in acquisition of debt finances for businesses. Hence, this study investigates the effect of bribery and corruption on access to finance for new market pioneering by Knowledge- Intensive Businesses (KIBs) SMEs in Nigeria. A quantitative approach was employed for this study using survey. A census-based method was employed for the sample size of 510 KIBs SMEs at Lagos. A self-administered questionnaire was employed for data collection and descriptive statistics, Pearson-moment correlation coefficient and multiple linear regressions was used for the analysis. The results indicate that bribery and corruption has a negative impact on KIBs owners/managers ability to acquire finance from the institutions. The study recommends that policy makers should back up the pioneering innovation with policies that can protect KIBs owners in obtaining debt-finances without being pressurised to give bribe. Also, the new government anti-corruption campaign should not only be limited to the politicians but to include everybody in every facet of the economy, whether private or public sectors. This study will contribute to the body of empirical study in entrepreneurial finance and innovation in developing economies.

Key words: *Corruption, finance, knowledge-intensive business services, New market pioneering, SMEs*

Introduction

As the political environment in Nigeria becomes stable there is a radical shift into the service sectors because technological and professional services are highly needed to complement the growth (Becker et al., 2008). By 2000, there was a policy shift to a knowledge-based economy which gave preference to Knowledge-Intensive Businesses (KIBs). The idea of KIBs originated from Miles et al. (1995) to describe private firms that generate, collect, analyse and distribute knowledge with the purpose of providing customised proficient service solutions to issues that client firms have not the capacity to perform. These firms offer highly intellectual value-added services mainly to other firms (Muller and Zenker, 2001). Thus, friendly policies fostering KIBs SMEs were promulgated in Nigeria to dive into *new market pioneering* (NMP) through venture creation or expansion into other markets (NPIT, 2000). This led to increase in the service sector importance and contribution to GDP and employment in Nigeria significantly from 29% and 42% respectively in 2000. In spite of the economic challenges, by 2015, it rose to 54.6% and became the largest contributor to the economy (National Bureau of Statistics (NBS), 2015). Many reports (e.g. Boz et al, 2010; Lawal, 2009) in recent times confirmed that Nigeria is a recognised major and leading market for ICT services in Adeyeye, M.M. & Wale Oshinowo. B. (2017) Effect of Corruption on Access to finance for market pioneering in Nigeria: Evidence from Knowledge- Intensive Business. Uniosun International Journal of Business Administration Vol. 1 (2) 12-24

Africa (CIA, 2015) and the present economic recession seems not to have impact on this sector. It transforms lives, work and creates new opportunities of demand (Yue, 2001) thus KIBs SMEs need to exploit these possibilities by NMP.

NMP is an indication that a positive change has happened in the composition of an organization or its strategy (Hanks et al., 1993) which brought about a need for expansion into other places. Finance is very integral to the effective functioning of KIBs firms to implement NMP in Nigeria and is obtainable from the formal and informal institutions (Aryeetey, 1998). Oswald (2003) expressed the importance of finance, whether equity or debt, in every operational stage of a firm. As business thrives, more financial resources are needed for expansion and implementation of innovation especially NMP. Nevertheless, the general consensus is that lack of finance can be a great constraint to the growth of SMEs (Levine, 2005; Papaloannou, 2007) but particularly for KIBs NMP because of the financial involvement especially in recruiting experts with creative skills. Hence the pecking order theory that firms, including KIBs SMEs, primary preference is for cheapest source of funding, when exhausted, move to the second, until it ends up with a preference for external debt but not equity. Therefore, external finances are required for NMP but KIBs owners are hesitant in using a particular source of finance because of the supply restrictions (Howorth, 2001). In addition, the problem of corruption with its negative cross-country effect on every facets of life, from the public to the private in Nigeria (Mambula, 2002; Oyefuga et al, 2008) deters access to debt financing by KIBs SMEs. Numerous empirical research (e.g. Oyefuga, et al 2008; Okpara, 2010, Umejei, 2011) have explored the matter of innovation in SMEs in Nigeria and also corruption in public places but existing gaps in knowledge is whether corruption affects access to finance for innovation into new market by KIBs SMEs.

Thus this study investigates the effect of bribery and corruption on access to finance for new market pioneering in Nigeria. It is expected that the study will contribute significantly to literature on innovation financing in developing economies. In order to achieve this objective the following hypothesis was developed for testing:

H0₁: There is no statistical relationship between NMP by KIBs SMEs and bribery and corruption in accessing external finance in Nigeria.

The remaining part of the paper is organized as follows: in section 2 and 3, the review of relevant literature and the research methodology. Section 4 presents the findings and discussion of the results and finally the conclusion and recommendations.

Literature Review

- *Knowledge Intensive Business Services*

KIBS are special service firms whose operations are particularly executed by experts that can integrate different form of knowledge into composite knowledge. That is, they integrate simple acquired knowledge or competencies that are identified with a particular (technical) discipline or (technical) functional area into complex form. They also provide knowledge-based intermediate products (Miles et al.,1995; den Hertog, 2000; Xin et al., 2009). The employees use knowledge as inputs and outputs in client-participation oriented services and interactive process of consultancy. KIBs currently represents over 60% of the Gross National Income (GNI) in most developed countries (Hazdra, 2010) with inadequate data in most developing economies as a new sector.

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However, there seems to be a shortfall in KIBs SMEs researches in both developed and developing economies and also in investigating access to finance needed for NMP, the gap this study attempts to fill.

KIBs are very important to the economy especially in creating and implementing new products, services and processes as carriers, shapers, facilitators and creators of both technological and managerial innovations (Den Hertog, 2000; Kuusisto and Viljamaa, 2004). They structure the infrastructure of the knowledge economy by fostering knowledge and ideas mobility around the economy, and encouraging firms to exploit the use of new technologies and ideas (Brinkley, 2012). They provide support systems like information technology (IT) networks and legal or accountancy function for business operations (Strambach, 2008). KIBs expansion by accessing new opportunities through NMP would be beneficial as it would affect the economy positively on a general note and as a catalyst for a knowledge economy.

- *New Market pioneering*

The concept of 'innovation' is very central to Schumpeter's theory of entrepreneurship. Schumpeter (1934) defined innovation as the 'exploitation of a profitable opportunity' and rephrased it in 1939 as the 'setting up of new production functions' or 'carrying out new combinations'. He identified five dimensions of innovation by an entrepreneur - *introduction of new products; introduction of new methods of production; identification of new sources of supply of raw materials; opening of new markets; and creation of new ways of organizing businesses*. Although, Schumpeter referred to opening of new market or market innovation and its importance, but more emphasis has often been placed on product and process innovation (Liebermann and Montgomery, 1988). His work also did not explore access to finance for new market opening despite innovative firms need for finance.

New market opening is the act of being one of the first (pioneer) to introduce your service into an existing market where the service has not been known or creating a market where none existed in order to better address customers' needs and increasing firms' credibility (Klepper and Thompson, 2006). It is linked with structural changes in an economy which can produce a positive effect on development (Acs and Virgill, 2009). Innovation is only complete when there is a market place to convert it to economic rent (OECD/Eurostat, 2005; Adeyeye, Abubakar & Mitra, 2015). This emphasised the essence of regular pioneering of new market as it provides opportunities for dynamic operations by entrepreneurs for economic growth.

When KIBs firms go into a market as pioneer, it is an exclusive innovation in its ability for expansion into unreached geographic area (e.g. Feeser and Willard, 1990; Klepper and Thompson, 2006). It assists SMEs to obtain firm growth by capturing a new market share and enlarging the firm's size (employees). Obviously, more finances will be required than they can generate internally, thus the need for external finances to meet the innovative challenge. However, KIBs SMEs need a lot of finance especially in this era of recession in Nigeria for a range of expenses which includes office rent and maintenance, specialised and general staff salaries and wages, purchase of assets including office equipment, expansion of operating systems, business site (or premises), publicity, advertisement and promotions, R&D, network and collaborations, and other things in embarking for the new market pioneering (Liebamann and Montgomery, 1998) and maintain a competitive advantage. According to the pecking order hierarchy, firms' exhaustion of internal finance would lead to the demand for external debt finance as an

option (Myers, 1984; Howorth, 2001). The question is: Will the corruption in Nigeria financial institutions interfere with the access to finance by KIBs SMEs for NMP or not?

Nevertheless, scholars seem not to have largely given attention to NMP (OECD/EUROSTAT, 2005) especially in KIBs SMEs and whether the menace of corruption can affect access to finance in Lagos. The reason might be because of the general neglect of literature on developing economies (Egbetokun, 2011) as well as on sources of finance by KIBs SMEs in both developing and developed economies (Scarso and Bolisana, 2012).

- *Problem of bribery and corruption*

There are problematic factors affecting KIBs SMEs' ability to access finance for expansion. Such factors include collateral requirements by banks, high interest rate, paperwork/bureaucracy, personal connections with bank /financial institutions, bribery and corruption and others. However, researchers' like Dike (2005), Beck and Demirguc-Kunt, (2006) and Fatoki and Smit (2011) identified bribery and corruption as major obstacles to SMEs development. Furthermore, the Business Environment and Enterprise Performance Survey (BEEPS) adjudged that more than 70% of SMEs owners' in developing economies perceive corruption as an obstacle to their businesses. The World Economic Forum's Global Competitiveness Index (2015) indicated lack of freedom from corruption as one of the malign factors that encumber an economy's competitiveness. Corruption increases the overall cost of conducting business in terms of accessing capital as well as paying higher interest rates while operating in corrupt environments. Corruption is detrimental to all businesses but seems acute for KIBs SMEs located in the developing economies.

External sources of finance normally attract transactional cost such that additional cost of corruption could rather lead to liquidation after NMP than expansion. All these support Mambula (2002), Oyefuga et al's,(2008) and Kempe (2017) assertion that corruption permeates every sector of many developing countries and a threat to SMEs realization of optimum growth capacities, profitability and effective job creation especially through NMP. Nigeria is ranked 140th of 176 countries in the Corruption Perception Index (2016) result.

The efforts directed towards SMEs are generally based on the assertion that they are engines of economic growth but flaws and market inefficiencies attached to formal institutions stand as barriers (Kempe, 2017). The inadequacies of the formal institutions pressurized some SMEs owners into corrupt practices because previous studies (Dike, 2005; Magaji, 2017) shows a positive relationship between the probability of becoming engaged in corruption, and a lack of confidence in the judicial system. For instance, in view of the KIBs SMEs owners' high level of educational background, they possess all the required documents and collateral needed for debt finance from the bank but still experienced denial or undue delays. The bank officials might request for more unrelated documents to frustrate the entrepreneur. Sometimes, the bank officials might demand for 'additional payment' or payment without a receipt. Others who paid the additional payments were sometimes able to obtain the loan (Adeyeye, 2013) while the ones for due process are left out.

However, the time factor is a strong determinant in this respect. Compliance with regulations and red tapes cause delays that, in turn, create financial costs that are

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disproportionately high comparatively for SMEs than large firms (Rune, 2012). Consequently, SMEs often resort to corrupt practices to expedite actions thereby reducing the cost of delays (Magaji, 2017). Research data revealed that the more time are needed to deal with bureaucracy and red tapes, the higher the likelihood that SMEs will engage in corruption. Empirical research also showed the availability of legal alternatives to bribes (Dike, 2005; Demirguc-Kunt, 2006) in a corrupt society sometimes would lead to more loss of time and money. If entrepreneurs supposed their environment as wholly corrupt, and there are no legal alternatives for certain transactions, the likelihood of joining the wagon and being involved in corruption is very high.

Generally, some SMEs owners are almost convinced that corruption forms part of daily businesses and it is almost impossible to survive without it (Safavian and Wimpey, 2007; Okpara, 2011). One possible explanation for this attitude could be the fact that in a region where corruption is endemic (Agbu, 2003), KIBs owners that refused to provide officials with additional payments, while other competitors do, will sooner or later face problems. Consequently, the competitive position in the market might be threatened, experiencing severe decline and inability to proceed on the dynamic NMP innovation. However, the apparent quick way of due process is by paying the bribe which ultimately can become an expensive scheme with uncertain outcomes.

The price and risks of corruption are economically inefficient and are great impediments to growth prospects (UNIDO, 2006). The bribes paid are uneconomical transaction costs: rent paid without values added to business (Rune, 2012). If such monies are invested in the business, more NMP might be possible, more jobs created with greater and better services for clients, higher incomes generated and a general contribution to better standard of living for the community. So many businesses face this problem and the negative effect on the local economy can be significant.

Safavian and Wimpey, (2007) in their study of 29 countries found that KIBS SMEs prefer the course of informal financing to formal financing to evade paying bribes to corrupt government and bank officials. They were willing to accept the extra costs of informal financing if there is the advantage of avoiding a bribe (Rune, 2012). Informal sources may not be completely free of corruption but direct demand for bribe is seldom done because the relationship is often based on network and trust hence it could damage the long established relationship and reputation in the community (Ayyagari et al. 2010). Whilst it is clear that some KIBs SMEs, in certain conditions intentionally choose either to participate or not to participate in corrupt practices. It is essential to recognize instances where KIBs SMEs have little or no choice (UNIDO, 2012). However, if these environmental factors are minimised in a developing economy, KIBs SMEs will be able to access external financial resources for NMP.

Methodology

The study seeks to establish the relationship between NMP and bribery and corruption by using the quantitative approach survey to generate a numerical data to provide direct information on firms' situation (Colluzzi, 2012). The study was conducted in Lagos, Nigeria. The unit of analysis was the firm level. The sampling frame was drawn from two major directories: Nigerian Yellow Pages and Nigeria Search Engines. 891 KIBs were found but only 510 cases (57%) fell into the criteria for data analysis as registered KIBs SMEs. Thus a census-based method was employed to embrace them all for a robust result. Data collection was done between December and March, 2016.

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Measures of variables

NMP simply refers to being “one of the first to introduce a product/service to a new or existing market”. To operationalise the constructs that identify newness for pioneering firms, includes being newly introduced to the country, firm, market, environment and so on (European Commission, 1995); seven variables were used to collect data for newness. The KMO was .83 and the Bartlett’s Test of sphericity was statistically significant at $P < .001$. The factor components were tested for reliability using Chronbac alpha, and the factors had an average score of .86 and can thereby considered reliable (Bryman and Bell, 2003). Thus the newness can justifiably measure NMP by KIBs SMEs.

There are five indices from the World Business Environment Survey that measure bribery and corruption. The study specifically investigated responses related to the level of corruption that firms must deal with. The questions are whether corruption of bank officials creates a problem (rated from 1 to 10) as described below: (1) if firms are required to make “additional payments” to get things done through bank officials; (2) if the demand is categorically stated and not documented (3) if services are delivered when the “additional payments” are made as requested; 4) if the services rendered justify the additional payment and (5) if it is possible to find honest officials to circumvent corrupt ones without being alluded to unofficial payments (Beck and Demirg-Kunt, 2006). To ensure the validity, some experts scrutinized the questionnaire for face and content validity and afterward, a pilot study was conducted with 20 KIBs SMEs firms from the sample. For the reliability of the instrument, test-re-test was applied and the mean score of the questionnaire was computed for the two scores using Pearson-Product Moment coefficient correlation. The reliability coefficient was .96. This indicated that the instrument is reliable as the score is high and positive. All the variables were tested for reliability, using Cronbach’s alpha. The questionnaires were administered to only owners/managers of the enterprises. Respondents were to rate how much obstacles these factors are in obtaining debt finance. Of the specific corruption obstacles reported, the need to make additional payments is the highest at 8.86. The second highest rated obstacle is firms’ inability to have recourse to honest officials at 8.02. Descriptive statistics, Pearson-moment correlation and multiple regressions were used for the analysis.

Results and discussion

Descriptive statistics

Descriptive statistics explains the general patterns in the data before undertaking other forms of analysis.

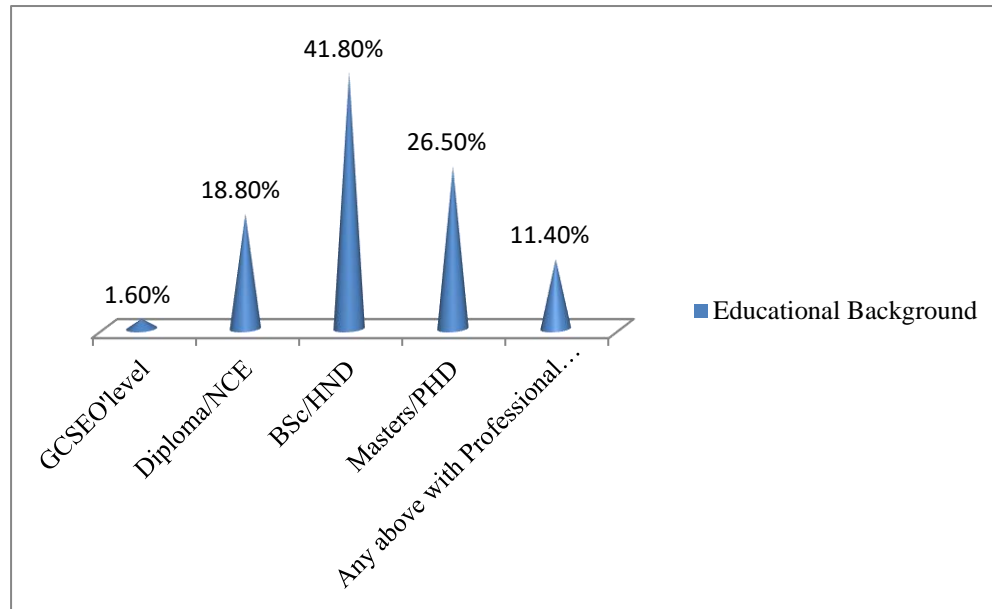


Figure 1: Percentage distribution of respondents by educational background

Figure 1 reveals the distribution of the educational background of the founders/manager of the KIBS SMEs in Lagos. 213(41.8%) are university degree holders, followed by postgraduate degrees 135(26.5%), and after that are diploma holders 106(18.8%). Those with added professional certificates are 48(11.8%) while only 8(1.6%) holds GCSE/O' levels are least. This supports den Hertog's (2000) assertion that KIBS firms rely heavily on specialised knowledge, that is, knowledge or professionals related to a specific (technical) discipline or functional domain that is generally acquired through higher education.

Table 1: Distribution by gender and educational background

Educational Background	GCSE O'Level	Diploma/NCE	B.Sc./HND	Masters/ PhD	Any other professional certificate	Total
Male	4	72	169	106	35	385
Female	4	34	45	29	13	125
Total Count	8	106	213	135	48	510

Table 1 indicates that 385(75%) of the sample are men while 125(25%) are women showing an uneven distribution of gender in this sector at Lagos. It implies that in the KIBS sector of the economy in Lagos, men are more predominantly involved in market pioneering. It seems the generic problem of women in education and empowerment affected women full involvement in KIBS sectors as entrepreneurs or managers. Gender inequality and education has persisted as a serious issue both in education and developmental discourse in Nigeria (Agu, 2007). This supports Ndukwe's

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(2005) claim that women entrepreneurs in Africa are more into starting trade, school or hospital related firms rather than technological sectors, probably because of the risk and stress involved with regards to acquisition of finance, maintenance and regular innovation like NMP for sustainability. However, majority of the females involved are university degree or higher diploma holders which is 36% of the female KIBS owner/manager. After that is the diploma/ NCE which is 27.2% and 23.2% holds masters/ PhD certificates. 10.4% of them have additional professional certificates and the least being 3.2% with GCSE O 'level certificate.

Pearson-Moment Correlation Result

Pearson-Moment correlation was run to confirm the strength of the relationship that exists between NMP and bribery and corruption in the quest of KIBS owners to access external finance.

Table 3: Pearson-Moment Correlation Analysis Result

	NMP
.New Market Pioneering	-
2. Bribery and corruption	-.285**
3.Corruption of bank officials	-.358**
4.collateral requirements of banks/financial institutions	-.270**
5.High interest bank rate	-.226**
6.Banks paperwork/bureaucracy	-.166**
7.Special connections with bank/financial institutions	-.285**

** Correlation is significant at the 0.01 level (2-tailed).* Correlation is significant at the 0.05 level (2-tailed).

The correlation between bribery and corruption and NMP ($r = -.285, P < .01$) is a negative and significant relationship. Bribery and corruption and NMP are inversely related. However, looking at the variables individually, corruption of bank officials ($r = -.358, P < .01$); Collateral requirements ($r = -.270, P < .01$); High interest rate ($r = -.226, P < .01$); Banks bureaucracy ($r = -.166, P < .01$); Special connections ($r = -.285, P < .01$). All these variables indicate a negative and significant ($P < .01$) association with NMP. This study is in consonance with previous studies (Howorth,2001; Fatoki and Smit, 2011) that found other problematic factors like collateral, high interest to rate and others as barriers to access finance by SMEs with a little divergence. The finding of the study is that these factors are inversely related hence the more these factors, the less the NMP. The more bribery and corruption, the less the KIBs owners are able to access finance for NMP.

Regression analysis result

The regression analysis result helps to establish if there is a statistical relationship between bribery and corruption and NMP by KIBs in accessing external finance.

Table 3: Regression analysis result

Regression Model 1		
	B-coefficients	t-value
Constant	19.679	13.307***
Bribery and corruption: Bank officials	-.616	-3.658***
Formal Finance1	.188	2.660***
Informal Finance1	-.027	-3.820*
R ²	.258	
Adjusted R ²	.254	
F	58.737***	

Note: ***, **, * denotes significance at 1, 5 and 10 respectively. Values of the t-statistics are indicated in parentheses. The sample size used for calculations is 510 KIBS SMEs.

Table 3 expresses the regression analysis result that explains 25.4% of the variance in the model. It analyses whether bribery and corruption of bank officials have effect on access to finance for NMP. The regression analysis indicates that the corruption of bank officials moderated the formal institutions at 2.660 with $P < .01$ and informal finance is -3.820 with $P < .10$. The challenges of corruption of bank officials affect access to debt finance in formal institutions. In other words, the more the problem of corruption the less KIBs SMEs will be able to access debt finance from bank for NMP.

Many previous studies (Levine, 1999; Kauffmann, 2005; OECD, 2006) found inability to access external finances by SMEs to be basically for lack of collateral, capacity of information and documentations. However, this study takes another perspective as KIBs SMEs owners are highly skilled personnel that have a level of business acumen as revealed by their level of absorptive capacity in this study, but the barrier to accessing funds from formal sources (Banks) is to avoid giving bribes to bank officials. Hence, funds are obtained from informal financial sources. This is in alignment with Beck et al (2003) findings for non-specific sector but for all innovative activities. The contribution of this study is extended to only KIBs SMEs NMP innovation in a developing economy. It is a very crucial finding which suggests that there might be a solution especially since commercial banks are privately owned and certain policy may be insinuated through this finding in view of the ongoing reform in banking sectors, anti-corruption campaign as well as the efforts in promoting KIBS and NMP in Nigeria. Aside it also disproves the general claims (Kauffman, 1996; Beck et al, 2006) that exempted

bribery and corruption of bank officials as a deterrent to sourcing finance from external sources for innovative activities which is empirically proven in this study.

Therefore, contrary to the expectation, the informal institution is also related to NMP by KIBS SMEs in Lagos. This indicates that KIBS SMEs in Lagos obtained debt finances for NMP from non-banks sources like gifts and remittances, cooperative societies, rotating savings, moneylenders, lease and hire purchase which are mainly informal sources. This study confirms previous studies by Aryeetey (1996) on Ghana, Ndukwe (2005) on Nigeria pioneering work on the existence of formal and the informal financial sectors in Africa. It is alarming to discover that bribery and corruption is associated with informal sources of finance. Bribery and corruption seems to have eaten up every facet of the system, whether formal or informal in a developing economy (Oyefuga, 2008). Bribery and corruption in the informal institution is different from the informal institutions because it is not directly demanded for like bank officials but in form of incentive for decision makers in the organisations. However, the problem of bribery and corruption is highly associated with KIBS SMEs incapability to source external funding for NMP. This might have made obtaining adequate finance difficult, consequently inhibiting many KIBS SMEs from effective NMP. The result therefore suggests that corruption is negatively associated with KIBS SMEs ability to use external resources for NMP. The more this problem, the less KIBS SMEs can use external financial resources from the formal institutions for NMP.

Conclusion and Recommendations

This research is very relevant at this particular time that Nigeria is encouraging SMEs especially in KIBs despite the economic recession, to expand into more areas as the country advances as a knowledge- based economy in this era of technological advancement. The overall result of this study showed a relationship between bribery and corruption and access external sources of financial resources for NMP. Hence to answer the research question, it can be said that bribery and corruption in a developing economy is negatively associated with KIBS SMEs ability to acquire finance from external sources for NMP to a large extent thereby resorting to informal sources.

The result of this survey is based on a fairly large sample hence can be extrapolated. The study will contribute to the body of empirical study on entrepreneurial finance and developing economies in its discovery that KIBS SMEs preference for debt finances for NMP from informal sources more than from formal sources because of bribery and corruption. Therefore, in view of the national policy to foster innovation and SMEs growth, a new policy might be necessary to provide direction for sourcing financial resources for NMP. The study recommends that policy makers should back up the pioneering innovation with policies that can protect KIBS SMEs from being compelled to give bribe in order to obtain finances. Also, the new government anti-corruption campaign should not only be limited to the politicians but include every facet of the economy with a focus on commercial banks. Women should be motivated along the line of KIBs from secondary school level till tertiary level to be involved in KIBs.

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