

Venture Capital and the Emergence and Development of Entrepreneurship: A Focus on Employment Generation and Poverty Alleviation in Lagos State

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Abstract

Entrepreneurship is a vital force in the economy of any nation because of the strategic role it plays in the achievement of macro-economic objectives and national development but is confronted with many Impediments such as the dearth of start up and working capital for expansion. Venture capital (VC) came into the financial market to bridge the gap created by the scarcity of long term and cheap finance which is considered appropriate for SMEs. VC is attractive due to low rate of interest coupled with investor's technical input. This research paper investigated the effect of VC on emergence and development of entrepreneurship as an aid to employment creation and poverty alleviation in Lagos State. Findings revealed that the venture capital in Lagos State exists but not effective. The study concluded that ineffective VC activity has resulted in the low number entrepreneurship emergence, underdevelopment of the sector, high level of unemployment and huge poverty in the state.

Key Words: Venture capital; Entrepreneurship; Employment generation; Poverty alleviation

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INTRODUCTION

Small and Medium-Sized Enterprises (SMEs) is an essential source and foundation for economic development

in any economy. Many developed countries attained their present level of development because they focused and supported new and innovative businesses and gave full fiscal and monetary incentives necessary for the success of such businesses ventures. Nigeria has long recognized the importance and valuable contributions of SMEs as a major source of new competition, poverty alleviation, wealth creation, employment generation, increased government revenue and private sector development (Oma-William, 2003). SMEs especially micro enterprises have offered a safety net for the survival of the poor, unemployed youths, and a nursery-bed of entrepreneurship development (Oma-William, 2003). Ayozie and Farayola (2005) observed that various governments are turning to SMEs as a means of economic development and a veritable means of solving economic and social problems but are constrained in many ways. One of the major hindrances of the entrepreneurship is start up capital for new entrants and working capital for existing ones because they can neither access the capital market nor meet the requirements of commercial banks for funding (Pandey, 2005). Venture capital flagged off to address the issue of lack of long term and cheap finance hindering entrepreneurial activities. The venture capitalist in addition to the acquisition of interest in the business by providing the requisite capital, participates fully in management of the enterprise which is not possible with conventional bank loans. Presently in Nigeria, there is mass turn out of graduates from higher institutions which cannot be absorbed by the existing jobs in both private and public organizations. This is the driving force leading all levels of government into paying policy attention to support entrepreneurship to resolve the problems of unemployment and poverty. Currently, all efforts seem not to be enough as they do not translate into the envisaged level of entrepreneurship emergence and development.

(1) Statement of Research Problem

SMEs are faced with many problems such as dearth set up capital, lack of funds for expansion, unreliable

and inadequate economic infrastructure and lack of management skills and techniques. Among all the pressing limiting factors, accessing finance for set up and working capital for expansion seems to be the most challenging (Oma-William, 2003). SMEs are essential and central to the achievement of Lagos State major macro-economic objectives and development but without capital, set up may be impossible and existing businesses can neither replace old equipments nor finance working capital as the company grows (Ovadje, 2003). Lack of access to credit is one of the major limitations of Nigerian entrepreneurs because they are restricted by lack of collateral, absence of past track records for business appraisal, sometimes lack of cognate experience and also the inability of pioneering entrepreneurs to persuade financial institutions to invest in risky projects with potentially low returns. Financing early stage business involves special problems and is fundamentally different from investments in matured and well established companies (Keuschnigg & Nielsen, 2000).

Employments available in both private and public organizations are not enough for the growing population of Lagos State and the inability of entrepreneurs to convert laudable innovative ideals into enterprise reality due to lack of cheap and long term finance has resulted in unemployment of those who should have been absorbed by personal efforts. This is the major source of huge poverty level in the state. Recent report of National Bureau of Statistics revealed that Lagos State harbours 70% of poor people due to unemployment level (CIA fact book, 2011). VC emerged as a solution to financing problem of the entrepreneur which will eliminate unemployment and poverty in the state (Gompers and Lerner, 2002). The core objective of this study is to investigate the effect of VC on the emergence and development of entrepreneurship in Lagos State between 2002 and 2011 and the implications on employment creation and poverty alleviation. To accomplish this, the study will also examine the operations of venture capitalist, unemployment and poverty level in the State. The research questions on which attempt is made to provide solution includes (i) how does lack of venture capital hinders entrepreneurship emergence and development? And (ii) To what extent has entrepreneurship emergence and development created jobs and reduced poverty in Lagos State?

(2) Statement of Research Hypotheses

H₀: Venture capital activities have not significantly resulted in emergence and development of SMEs in Lagos State.

H₁: There is no significant relationship between SMEs, and job creation and poverty alleviation in Lagos State.

1. REVIEW OF RELATED LITERATURE

Venture capital and entrepreneurship studies have attracted attention from scholar, finance managers professional

bodies and entrepreneurs. Although most of the studies are less advanced in developing countries but the importance cannot be overruled. Amit *et. al.*, (1999) noted that an important source of finance for entrepreneurial sector is the venture capital and their activity involves the provision of equity and debt financing to young privately held firms. Gomper and Lerner (2002) also stressed that VC, entrepreneurship and innovation are closely knotted together. Entrepreneurs who had laudable project ideas with positive net present value require substantial capital to implement but are limited by lack the fund to execute them. VC evolves in response to this need. US venture capital industry is one of the most admired institutions among industrialist because of the role it plays in the economy (Dossani & Kenney, 2002). Nigeria as an emerging nation can also develop a successful VC industry to harness the available resources in form of human capital and materials in order to reach her targeted economic destination.

1.1 Venture Capital Overview

During the 1990s, venture capital emerged as a new source to finance technology innovation in the private sector. Especially in the United States, where many small high tech start-up companies in Silicon Valley and outside Boston received financing from VC funds. Lately, venture capital has begun to play an increasingly important role in European and Asian countries (Pfeil, 2000). Start up investment is viewed as a key source of innovation, employment and economic growth, hence the need for policy makers to pay attention to entrepreneurship and venture capital (OECD, 2008).

Pandey (2005) defines venture capital as an innovation of significance in the twentieth century, a synonym of risk capital, and a source of finance for early stage enterprise for start up and young enterprise seeking to grow rapidly. OECD (2004) defines it as a capital provided by firms who invest alongside management in young companies that are not quoted on the stock exchange market. Keuschnigg and Nielsen (2000) noted that venture capital has come to specialize in financing early stage investment, supply equity finance and provides valuable business advice to enhance SMEs survival. Form the above definitions, venture capital differs from conventional form of financing due to the following: (i) provision of equity through purchase of share, options and convertible securities directly with the objective of disposing-off once the business is profitable (ii) Long-term investment spanning between 5-10 years not repayable on demand at the option of the venture capitalists (iii) involvement of providers of funds in management thereby rendering support services such as marketing, recruitment of key personnel and designing strategies. (Heard & Sibert, 2000; EVCA, 2004; Kumar, 2005). The growing emphasis on the role of entrepreneurship as a critical factor for national development has led to the search through a wide range of

schemes aimed at accelerating the tempo of new business activities in the organized private sector. Lagos State was not left out as successive governors have made efforts to promote SME sector through a complementary range of fiscal, financial extension, subsidies, advisory services, and provision of infrastructure designed to stimulate indigenous entrepreneurship (Nnanna, 2001). The venture capital activity involves deal origination, Screening of all projects on the basis of some broad criteria which may limit projects to areas of familiarity, due diligence to evaluate investment proposal, deal structuring for negotiation of post investment activities and ends with exit to enable the VC firm cash out its investments as stated in agreement (Kumar, 2005). The VC firm recoups its investments when the portfolio companies either go public or sell out to other corporations in the finance market (Liaw, 2003; Kotolnikov, 2001).

The emergence of entrepreneurship is a continuous and important phenomenon in modern economies (Arend 1999). Ogundele (2007) defines entrepreneurial emergence as the process of coming into existence of new entrepreneurial organisation. Development refers to the process of enhancing entrepreneurial skills and knowledge through structural training and institutional building programmes. It aims at enlarging the base of entrepreneurs to accelerate the pace of venture progress, job creation and economic development (UNDP, 1999). Entrepreneurial development programmes may include support for orientation and awareness, development of the competencies necessary to recognize market opportunities and organize resources to meet them.

1.2 Limitations to Entrepreneurship Emergence and Development in Lagos State and Government efforts

The limitations to the emergence and development of SMEs in Lagos state includes: finances, inadequate and unreliable infrastructural facilities, unfavourable fiscal policy and policy inconsistencies, entrepreneurs internal problems such as poor management practice, poor accounting records, shortage of manpower, financial indiscipline, corruption and economic and political instability (Sanusi, 2003; Omolola, 2008; Njoku, 2002; Obitayo, 2001). In recognition of financial setback facing SMEs, successive governments had shown interest in ensuring availability of adequate funds. This is being done by setting up various schemes and specialized financial institutions to provide appropriate funding to the subsector (Olaitan, 2006).

At the Federal level, efforts in this direction dated back to 1946, when the Nigerian Local Development Board was established through a ten-year development plan which was presented to the Legislative Council. This was the first time a policy framework on National economic development received appropriate focus (Emmanuel, 2002). This was dissolved in 1949 with its functions

transferred to three (3) Regional Development Board which was active for seven years. The dissolution of RDB gave way to the establishment of the Federal Loans Board and the Federal institute of Industrial Research Oshodi (FIIRO) in 1956 (Obademi, 2007). The Federal Loans Board was replaced with Revolving Loans Funds which was set up to provide technical assistance to the Small Scale Credit Scheme (Emmanuel, 2002). All efforts to achieve the objective of SMEs revival failed owing to inadequate funding, high ratio of nonperforming loans, poor management and corruptions, many of these institutions became moribund (Njoku, 2002). Loans were unjustly granted and based on political rather than commercial considerations. CBN (2012, July) noted that development financing is one of the requirements for sustainable economic growth in any economy.

The government can also aid entrepreneurial emergence and development by providing sound fiscal and monetary policies as a basis for a stable enabling environment to support smooth operations. (OCED, 2008). Lagos State in order to effectively assist the entrepreneurial activities to reduce unemployment and poverty in the State, established Lagos State Micro Finance Institution (LASMI) to partner with eight (8) Micro Finance Banks addressed as Agency Banks distributed across three Senatorial Districts to facilitate disbursement of financial assistance to prospective and eligible beneficiaries (LASMI, 2012). The 8 Agency Banks are shown in table 1 below:

Table 1
Agency Banks in Partnership with LASMI

S/N	Microfinance	Location
i	Integrated Micro-Finance Bank	Adeniyi Jones Avenue, Ikeja, Lagos
ii	Gap Bridge Micro-Finance Bank	Oko-Awo Street, V/I, Lagos
iii	LASU Micro-Finance Bank	LASU Campus, Lagos / Banditry Exp.
iv	Ojokoro Micro-Finance Bank	Lagos/Abeokuta Expressway, Ijaiye,
v	Infinity Micro-Finance Bank	Ikoroku Rd, Kosofe Mile 12, Lagos
vi	GS Micro-Finance Bank	1, Kudirat Abiola Way, Ikeja, Lagos
vii	Townserve Micro-Finance	Gbasemo Street, Aga, Ikorodu, Lagos
viii	MIC Micro-Finance Bank	10, Allen Avenue, Ikeja, Lagos

Source: Field survey, August 2012

The following are the functions of LASMI to enable Lagos state achieve optimum employment and poverty alleviation: (i) Providing basic financial assistance to entrepreneurs who are not able to benefit from the orthodox banking system due to their inability to provide collateral (ii) monitoring of the records of the Agency banks to ensure that disbursement are in line with their objectives (iii) collaborating with local and foreign development finance agencies to co-fund the Lagos State

Micro-Finance Fund to entrepreneurs (vi) developing value-added support services that impacts positively on the business of micro entrepreneurs through qualitative education and confidence building programmes (v) developing and implementing graduate entrepreneurship scheme to create employers of Labour rather than graduate job seekers in the state (LASMI, 2012).

1.3 Unemployment and Poverty Level in Lagos State

The recent report of National Bureau of Statistics revealed that the poverty level in Nigeria is alarming. The rate of poor people in 2004 was 68 million out of 150m and in 2010 increased to 112 million out of 158 million Nigerians. This represents 71% of our country's total population while economic wellbeing indicator showed otherwise (CIA Fact book, 2011). Awoyemi (2012) noted that the significant divergence between the Nigerian economic indicators, macro economics variables and the reality presents a source of concern. The rate of poverty incidence in Lagos increased nearly nine times from 6.27 per cent in 1996 to 53% in 2004. Nigeria Living Standard Survey produced by the Federal Office of Statistics in collaboration with the European Union (EU), and World Bank in 2003/2004 was principally designed to provide national and sub-national statistics on poverty and a range of sectoral topics. Poverty was defined to mean not only the lack of income, but also the lack of access to health, education, electricity and other essential services. The report aimed at providing deeper analysis of poverty that will serve as a basis for monitoring and evaluating the performance of policies and national development programmes in relation to the living conditions of households. Recently, a report of NBS showing states by poverty headcount using self-related lines revealed that Lagos State harbours 70.29 per cent of poor people. Today, the State government is turning to SMEs as solution to the two headed monster – Unemployment and poverty.

1.4 Role of Venture Capital Land Entrepreneurship in Employment Creation and Poverty Alleviation

Entrepreneurship involves creative ideas and mobilizing resources in pursuit of opportunities found in new businesses (Aldrich, 1990). During the process, capital resource is crucial for bringing the innovative ideas into project reality. The role of venture capital as a specialized intermediary is important to SMEs. In Lagos State, financing entrepreneurial companies is widely recognize as key to industrial revival and solution to economic problems but relative little evidence shows the real effects of venture capital investments (Gomper & Lerner, 2001). Heard and Sibert (2000) noted that VC is a key ingredient for SMEs growth and since it induces entrepreneurial activity both are playing strong roles in economy development. Sen and Dreze (1995) economic development is a broad term that refers to the sustained,

concerted effort of policymakers and the community to promote the standard of living and economic health in a specific area. Such effort involves supporting SMEs.

The role of SMEs as a catalyst for economic growth and development has been well documented in the economic literature and recognised by most countries (Sanusi, 2003). World Bank (1995, as cited in Nnanna, 2001) stated that evidence around the world indicates that SMEs provides effective means of stimulating indigenous entrepreneurship and employment opportunities per unit of capital invested. Rothenbush (2005) noted that some of the importance of venture capital and entrepreneurship includes: creating employment opportunities, promoting effective resource utilization considered critical for poverty reduction. It also facilitating industrialization, economic growth, increase per capita income and output and enhancing regional economic balance through industrial dispersal (Ogujiuba, *et. al*, 2004; Obitayo, 2001)

2. METHODOLOGY

The population of the study consists of 492 SMEs registered with Lagos Chamber of commerce, 27 VC firms in Lagos State and 9 Micro Finance Banks made up of Lagos State Micro Finance Institution (LASMI) and associated 8 Agency Banks. A sample size of 74 entrepreneurs representing 15% was selected at random and a census survey of all venture capitalists and LASMI and Agency banks were studied. This formed the basis 109 copies of questionnaire administered to the operating officer of each firm. 103 valid questionnaires were filled and returned as follows: Entrepreneurs (70), VC firms (25) and LASMI (8). The questionnaire distribution was independent of sex and Age. The instrument consists of an 8 - term survey questionnaire with a - 5 Likert scale response options: Strongly Agree (5), Agree (4), Undecided (3) Disagree (2), and Strongly Disagree (1). The structured questionnaire was divided into two sections: "A" for VC firms and "B" for entrepreneurs and was validated by experts in the field. A reliability pre- test carried out yielded stability co-efficient of 0.87 which was considered well enough. Pearson Product Moment Correlation Coefficient method was used to confirm hypotheses of the study.

$$r = \frac{N\sum xy - (\sum x)(\sum y)}{\sqrt{N[\sum x^2 - (\sum x)^2][N\sum y^2 - (\sum y)^2]}}$$

3. DISCUSSION OF RESULT

The article investigated relationship between VC and emergence and development of entrepreneurship on one hand and SMEs and employment generation and poverty reduction on the other. The work attempted to fill a gap in

research in entrepreneurship with a survey of VC firms in Lagos metropolis. Hypothesis tested in table 5 revealed that there is weak relationship between VC activities and entrepreneurship in Lagos state. Although all VC Firms unanimous agreed in question 2: Availability of VC leads to the existence of new indigenous entrepreneurship in Lagos State with 68/63% to rank first. They also unanimously agreed that the efforts of Lagos state government are not adequate to ensure fund availability in the state with 40%/25% as lowest in the ranking. The “r” calculated of 0.41 shows that VCs have not adequately stimulated the SMEs in the State. In table 5, entrepreneurs agreed on question 5: That establishment and development of SMEs leads to employment creation and poverty alleviation in the State with 71% to rank first in section B. This is confirmed by question 6 – Lack of start up capital and high SMEs mortality rate due to inadequate working funds has resulted in unemployment and high level of poverty in Lagos State. The “r” calculated of 0.67, shows that there a weak positive correlation (insignificant) relationship between SMEs and job creation and poverty alleviation in Lagos State

3.1 Summary of Findings

Based on the analysis carried out, the following findings were revealed:

VC is highly needed for emergence and development SMEs in Lagos State. This will eliminate the issues of scarcity of cheap and long term finance limiting entrepreneurial activities. It will also reduce the SMEs mortality rate.

Existing VC Firms have not adequately stimulated the growth of SMEs in the State.

The LASMI responsible for funding SMEs has not embarked on intensive education of entrepreneurs on VC activates to reduce ignorance.

There are no adequate government policies in form of tax pass for venture capital firms, exit and investments flexibility to encourage the entrance of independent firms to further enhance the flow of fund to the sector.

CONCLUSION REMARKS

Entrepreneurship plays a unique roles in economic growth and development of any nation by multiplying employers of labours, promoting utilization of local resources, redistributing income and reducing inequality gap, eliminating poverty, reducing rural-urban migration and accompanying social vices, maintaining social stability and generating revenue for the state government. Despite the importance of SMEs in the economy at large, they are still faced with several obstacles which include limited access to finance. From the study, VC exists but effective in Lagos State and the state government has not paid enough policy attention to the issue in her economic reform process. The long term financial scarcity has not only hindered the emergence and development of the

subsector but also has resulted in high unemployment rate, increase poverty level and high social vices among youths in the State.

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APPENDIX 1

(1) Test of Statistical the Hypothesis

Hypothesis 1

H_0 : Venture capital activities have not significantly resulted in emergence and development of SMEs in Lagos State

H_1 : Venture capital activities have significantly resulted in emergence and development of SMEs in Lagos State

Table 2
(Section A) Response on Key Issues Linking the Relationship Between Venture Capital Activities and Emergence and Development of Entrepreneurship in Lagos State

S/N	Variables Responses (in %)	Venture Capitalist (25)					LASMI & Agency Bank (8)					Rank
		SA %	A %	U %	D %	SD %	SA %	A %	U %	D %	SD %	
1	Insufficient cheap and long term capital is a major factor affecting the emergence and development of entrepreneurship in Lagos State.	12 48%	2 8%	1 4%	8 32%	2 8%	4 50%	1 13%	1 12%	2 0%	0 0%	3rd
2	Venture capital is not available to SMEs in Lagos State due ignorance.	16 64%	7 28%	1 4%	1 4%	0 0%	3 38%	2 25%	1 12%	1 12%	1 12%	2nd
3	Availability of VC leads to the existence of new indigenous entrepreneurship in Lagos State.	17 68%	3 12%	2 8%	2 8%	1 4%	5 63%	2 25%	1 12%	0 0%	0 0%	1st
4	Government has made enough effort to ensure that funds are available for entrepreneurial activities in Lagos State	10 40%	5 20%	3 12%	2 8%	5 20%	2 25%	1 12%	2 25%	2 25%	1 12%	4th

Source: Author's Computation. September, 2012

Table 3
Question 1 of Questionnaire Administered: Insufficient Cheap and Long Term Capital is a Major Factor Affecting the Emergence and Development of Entrepreneurship in Lagos State.

Options	Venture Capitalist (25)					LASMI & Agency Bank (8)				
	Point (x)	Response (y)	xy	x ²	y ²	Point (x)	Response (y)	xy	x ²	y ²
SA	5	12	60	25	144	5	4	20	25	16
A	4	2	8	16	4	4	1	4	16	1
U	3	1	3	9	1	3	1	3	9	1
D	2	8	16	4	64	2	2	4	4	4
SD	1	2	2	1	4	1	0	0	1	0
Σ	15	25	89	55	217	15	8	31	55	22

Source: Author's Computation. September, 2012

Table 4
Calculation of Correlation (Using Average Aggregate (SD) Response)

Options	AA Point (x)	AA Response (y)	AA (xy)	AA (x ²)	AA (y ²)
SA	5	8	40	25	80
A	4	1.5	6	16	2.5
U	3	1	3	9	1
D	2	5	10	4	34
SD	1	1	1	1	2
Σ	15	16.5	60	55	119.5

Source: Author's Computation. September, 2012.

Note: AA = Average aggregate

$$r = \frac{N\sum xy - (\sum x)(\sum y)}{\sqrt{N\sum x^2 - (\sum x)^2} \sqrt{N\sum y^2 - (\sum y)^2}} = \frac{5(60) - (15)(16.5)}{\sqrt{[5(55) - (15)^2]} \sqrt{[5(119.5) - (16.5)^2]}}$$

$$= \frac{300 - 247.5}{\sqrt{(275 - 225)(597.5 - 272.25)}} = \frac{52.5}{\sqrt{(50)(325.25)}} = \frac{52.5}{127.52}$$

$$r = \underline{0.41(41\%)}$$

Decision: The "r" calculated of $0.41 \leq 0.5$ level of significance. The null hypothesis is accepted. Venture Capital activities have not meaningfully resulted in emergence and development of SMEs in Lagos State.

Hypothesis 2

H_0 : There is no significant relationship between SMEs and job creation and poverty alleviation in Lagos State

H_1 : There is significant relationship between SMEs and job creation and poverty alleviation in Lagos State

Table 5
(Section B) Response on Key Issues Involving the Relationship Between SMEs and Job Creation and Poverty Alleviation in Lagos State

S/N	Variables Responses (in %)	SA %	A %	U %	D %	SD%	Rank
5	Establishment and development of SMEs leads to employment creation and poverty alleviation in the State.	50	8	2	7	3	1st
		71%	11%	3%	10%	4%	
6	Unemployment and poverty in Lagos state is due to inadequate entrepreneurship emergence and development.	47	12	2	6	4	2nd
		68%	18%	4%	2%	9%	
7	Lack of start up capital and high SMEs mortality rate due to inadequate working funds has resulted in unemployment and high level of poverty in Lagos State.	46	15	1	3	5	3rd
		66%	21%	1%	4%	7%	
8	Innovative ideas without set up capital to convert them into project reality die without implementation.	45	14	3	4	4	4th
		64%	20%	4%	6%	6%	

Source: Author's Computation. September, 2012

Table 6
Question 5 of Questionnaire Administered: Establishment and Development of SMEs Leads to Employment Creation and Poverty Alleviation in the State

Calculation of Correlation (using "SD" response)

Options	Point (x)	Response (y)	xy	x ²	y ²
SD	5	42	210	25	1,764
A	4	8	32	16	64
U	3	4	12	9	16
D	2	7	14	4	49
SD	1	9	9	1	81
Σ	15	70	277	55	1,974

Source: Author's Computation. September, 2012

$$r = \frac{N \sum xy - (\sum x)(\sum y)}{\sqrt{N \sum x^2 - (\sum x)^2} \sqrt{N \sum y^2 - (\sum y)^2}} = \frac{5(277) - (15)(70)}{\sqrt{[5(55) - (15)^2][5(1,970) - (70)^2]}}$$

$$= \frac{1,385 - 1,050}{\sqrt{(275 - 225)(9,870 - 4,900)}} = \frac{335}{\sqrt{(50)(4,970)}} = \frac{335}{498.5}$$

$$r = \underline{\underline{0.67 (67\%)}}$$

Decision: The r calculated of $0.67 \geq 0.5$ level of significance. The alternate hypothesis is accepted. There is significant relationship between entrepreneurship and job creation and poverty alleviation in Lagos State. However 67% shows a weak positive correlation.