A Qualitative Study to Discover the Determinants of Capital Structure of Micro and Small-sized Enterprises in Malaysia

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ABSTRACT
The study aims to discover the factors affecting capital structure decisions of micro and small enterprises (MSEs) and develop a model of capital structure determinants. The study employed in-depth and face-to-face interviews and focus-groups discussions to validate the existing concepts that have been identified in the literature within the Asian context, specifically the Malaysian MSEs. The inter-rater reliability technique was used to analyse the data. The results indicate that the large proportion of respondents relied extensively on the internal finance during start-up stage and in subsequent years. The results identified 13 factors of capital structure choice which are consistent with major studies on the capital structure determinants. This study reveals two new determinants of capital structure, namely 'awareness' and 'business culture' and some new items which can be included in the existing constructs. The research findings should help managers to make optimal capital structure decisions as well as assist the policy maker in formulating the financing policy.

Keywords- Micro and *Small Enterprises (MSEs), capital structure, finance, interview, focus group, ethnicity, Malaysia*

1. INTRODUCTION

Finance is very important for the development of micro and small enterprises (MSEs). Without finance, it is impossible to start a business or to cover the initial loss-making period which was experienced by most small firms (Mat Nawi, 2015; McMahon et al., 1993). The capital structure choice is one of the most crucial decisions faced by MSEs' entrepreneurs. A significant theoretical and empirical works had focused on the capital structure decision. Most of the studies focused on large firms (see Beattie et al., 2006; Bevan and Danbolt, 2002; Allen, 1991) or MSEs in western countries (see López-Gracia and Sánchez-Andújar, 2007; Hernández-Cánovas and Koëter-Kant, 2006; Sogorb-Mira, 2005). Nevertheless, more recent studies have put the empirical focus on MSEs in non-western contexts such as China (Chen, 2006), Thailand (Wiwattanakantang, 1999) and Vietnam (Nguyen and

Ramachandran, 2006). However, the studies on capital structure in non-western countries are still relatively few if compared with the western countries. Therefore, it is essential to understand how capital structure theories work in non-western countries, especially those with different traditions and cultures like Malaysia. Apart from that, it is motivated by the traditional, cultural and institutional differences of the business environment as Malaysia is a multiracial[1] country.

This study proposed a qualitative study mainly to obtain evidence of capital structure determinants deemed to be important within the context of MSEs in Malaysia. This objective may test the limits of current models by identifying emerging capital structure determinants that are context-specific. The study among others intends (i) to establish a fundamental understanding of small-business capital structures; (ii) to obtain relevant information regarding the new construct of capital structure decisions; (iii) to collect data for comparison and validation of the capital structure determinants models; and (iv) to illustrate the literature findings and explore underlying objectives in order to develop more reliable model of capital structure determinants for Malaysian MSEs. Specifically, this study aims to answer the following research question: "How and in relation to what factors do Malaysian MSEs choose their financial structure?"

2. LITERATURE REVIEW

The capital structure comprises of debt and equity. The theories of capital structure give explanations for questions among others like how companies choose their capital structure, what sources of financing companies should choose for different stages of life-cycle, how much money should companies borrow or issue, and so on.

This study considers two main theories; i). Pecking Order Theory (Myers and Majluf, 1984) suggests that companies follow a hierarchical order of financing sources, which begin with internal sources of finance, followed by debt if further finance is required, and the last resort is an external equity; and ii). Trade-Off Theory (Modigliani and Miller, 1963) involves a trade-off between the cost and benefit of debt financing. It predicts the existence of an optimal target financial debt ratio, which will directly maximise the value of the firm. Both theories have been adopted by previous researches as a theoretical foundation to investigate the determinants of capital structure. Some additional theories are also considered in this study; Agency Theory (Jensen and Meckling, 1976), Information Asymmetry (Myers and Majluf, 1984), and Free Cash Flow Problem (Jensen, 1986).

Although there is no exact formula available in achieving optimal target debt and capital ratio, previous empirical studies showed that owner-related factors, firm-related factors, and business environment should be considered when formulating capital structure strategy.

Moreover, the usual methodology of capital structure studies has been used to investigate the relationships between the capital structure and factors affecting it. However, this methodology has been criticised by Hempel (1983) among others; because the explanatory variables are restricted to those, which can be quantified (Barton and Gordon, 1987). This restriction leads to oversimplification of how the firm works. In order to include the qualitative factors, which have an impact on the firm's

[1] Multi-racial – The country comprises of three major ethnic groups; namely Malay, Chinese, and Indian. They have equal rights in politics, economics and social activities.

capital structure decisions, Matthews et al. (1994) stated that a new paradigm was needed for studying the determinants of capital structure. Thus, this study uses qualitative study technique in order to obtain information concerning the financial (quantitative) and non-financial (qualitative) factors of capital structure decisions.

Additionally, there are still relatively few empirical studies exploring the perceptions of owners-managers in the finance even though they play a vital role in MSEs' financing decisions. Alternatively, most of the studies in capital structure determinants obtained information from secondary sources of panel data. This study, therefore, investigates empirically the financing patterns of Malaysian MSEs' owners and examines determinants of capital structure by using data which were gathered from focus group discussions and interviews.

3. RESEARCH METHODOLOGY AND ANALYSIS

The study involved face-to-face interviews and focus group discussions with 25 respondents. This study adopts convenience and snowball sampling. The respondents are the MSEs' owners of the firm in the East Coast Region of Malaysia. A coding scheme was used to categorise the items reflecting determinants of capital structure regardless whether it is consistent or different from those identified in existing models.

In testing the reliability, the study uses inter-rater reliability test. The study applied a card sorting exercise (see King, 1994) to check the consistency with which different raters could assign factors identified from the interviews or discussions to the proposed capital structure determinants constructs. The researcher invited six lecturers from two public universities in Malaysia to participate in this exercise and asked them to classify the factors into the constructs based on the definitions given, individually. The researcher then listed the responses, compared with the item sorted earlier (i.e. by the researcher), and calculated the percentage agreement between each pair of raters by using Goodwin and Goodwin's (1985: p.14) formula, where inter-rater reliability equal to number of coding agreements divided by number of coding agreement plus a number of coding. The inter-rater reliability estimates for the capital structure determinants areas are depicted in Table 1.

Table 1: Inter-Rater Reliability for Capital Structure Determinants (CSD)

CSD	Minimum inter-rater reliability estimate	Maximum inter-rater reliability estimate	Mean inter-rater reliability estimate
Relationship & Networking	.82	.86	.84
Information Asymmetry	.83	.92	.89
Perceptions & Beliefs	.75	1.00	.86
Objectives & Goals	.68	.94	.80
Business Planning	.82	.92	.88
Awareness	.67	.82	.74
Business Environment	.56	.72	.69
Business Cultural Orientation	.69	.72	.70

Alternatively, evidence of validity was established through the process of comparing the items related to capital structure preference with non-preference. This comparison method is acceptable as suggested by Maxwell (1996) that a suitable method to check the validity of an outcome is to verify its replicability by comparing the results obtained in the present study with other studies. It was found that part of capital structure constructs and items identified in the present research significantly related with results reported by Mac an Bhaird and Lucey (2010), Romano et al. (2001) and Michaelas et al. (1998), providing some evidence of the validity of the qualitative data. Finally, a new capital structure model has been developed based on the factors derived from this study.

4. RESEARCH FINDINGS

4.1 Factors Affecting Capital Structure

The identification of characteristics that reflected models of 13 areas of CSD, as proposed by the existing literature, confirmed the applicability of Romano's et al. (2001) model of capital structure determinants and some others; such as Mac an Bhaird and Lucey (2010), Nguyen and Ramachandran (2006), Smallbone et al. (2003) and Michaelas (1998) The 13 constructs of CSD that shared commonalities with existing models of CSD were firm age, firm size, profitability, asset structure, business planning, objectives and goals, asymmetric information, owner's age, owner's education, ethnicity, perceptions and beliefs, relationship and networking, and business environment. The study also identified two new constructs which are 'awareness' and 'business cultural orientation'.

4.1.1 Owner-related factors

Respondents were asked to explain how they financed their businesses and to specify what demographic factors that determined their choice of finance. The respondents consist of 10 Malay, 8 Chinese, and 7 Indians. The owners' ages ranged from 22 to 62 years, where the mean age being 39 years (SD= 8.78). On the other hand, in terms of owner's age at business start-up, it varied from the mid-20s to early 40s, with the average age of 28 years old (SD=6.92). All participants had some working experience prior to venturing into their current business. The working experience includes both related and unrelated experience with the current business activities.

Table 2: Financing preferences of the respondents

	Malay	Chinese	Indian	Total
Initial funding				
Personal savings	50%	25%	14.29%	32%
Funds from friends and family (F&F)	30%	75%	42.86%	48%
Government	10%	-	14.29%	8%
Bank	10%	-	28.57%	12%
Total	100%	100%	100%	100%
Funds at growth stage				
Retained earnings	20%	37.5%	28.57%	28%
F&F/ Trade credits/ Leasing/ Hire purchase	-	12.5%	14.29%	8%
Government	40%	12.5%	-	20%
Bank	40%	37.5%	42.86%	40%
Private investor	-	-	14.29%	4%
Total	100%	100%	100%	100%
Funds at maturity stage				
Retained earnings	40%	75%	42.86%	52%
F&F/ Trade credits/ Leasing/ Hire purchase	20%	25%	42.86%	28%
Government	30%	-	-	12%
Bank	10%	-	-	4%
Private investor	-	-	14.29%	4%
Total	100%	100%	100%	100%

Table 2 shows that personal savings and funds from friends and families are the most significant sources of funds at start-up for all ethnic groups. They started to opt for different types of finance as the business grows. For example, Malays opt to utilise the government grants and loans. The higher concentration on Bumiputra[2] finance by the Malaysian government may be the result of this supply-side effect. It could be argued that ethnic minority small business owners find it difficult to obtain government grants or loans since they are not Bumiputra. Some comments given by the non-bumiputra[3] owners are as follows.

> *'My financing option is quite limited, especially the sources from the government. It is because most of the financial sources are only limited for Bumiputra. I mean Malays only.'* (The owner of a Hardware and Painting, Chinese)
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> *'…It is just because of I'm an Indian; I could not get the grant from the government.' (*The owner of a Bakery and Cakes, Indian)

[2] Bumiputra is the indigenous group in Malaysia which mostly consists of Malays.
[3] Non-Bumiputra is non-indigenous group in Malaysia, which mostly comprises of Chinese and Indian.

> *'It is hard for me to get external funding due to the fact that most of the external funding is only available for Bumiputra.'* (The owner of a Wholesale and Retail, Chinese)

Some of the respondents expressed that their beliefs in religion hinder or encourage them to borrow or not to borrow money from others.

> *'As Muslims, we are not encouraged to borrow especially from conventional banks. Therefore, I prefer to use my own money as a capital. If it is not enough, I will borrow from family and friends*.' (The Ice Cube Producer, Malay)

> '*I think, in all religion, all debts must be paid, including me as a Hindus. That is why, before making any decision on financing, I will think seriously*.' (The owner of a computer-related service, Indian)

Besides, owners' financing attitude, as well as their way of life, may influence the decisions to borrow, issue equity, or maintain with the internal sources of finance. The risk-taker entrepreneur would prefer to acquire an external finance; while the risk-averse entrepreneur would prefer to use only safer financing sources such as personal savings, retained earnings, or funds from friends and families.

> *'I do not like risk, and I will not let my business involve in any risky activities.'* (Ice Cube Producer, Malay)

> *'I like a challenge, which is why I prefer to use funds from external sources. When the credit side of your balance sheet is bigger than the debit side, you will automatically work harder and try not to miss any valuable opportunity for your business. This may be one kind of motivations.'* (The owner of Public Relation consulting, Malay)

> *'I have no problem to share this firm as long as the firm survives and makes profit.'*(The owner of Catering service and Restaurant, Indian)

> *'I have no problem to use internal or external funds as long as the control power of my company is 100% in my hand. I'm not willing to share my company's control with others.'* (The owner of Hardware and Painting, Chinese)

> *'100% of my financing sources came from internal sources. It is because I do not like to be burdened by debt and I certainly do not like this type of commitment.'* (The owner of an Air Conditioner services, Chinese)

> *'I would rather grow slower than borrow. If I want to make a new investment, I'll use retained earnings. If it did not enough I prefer to wait until the capital is enough.'* (Ice Cube Producer, Malay)

The age of the owner may also affect the financial structure of small firms. The owners' age and their experience are interrelated to each other. The older the person, the more experience he or she will possess. The experience with the use of borrowed money will affect future capital structure decisions. Firms that have been through bad experiences caused by high gearing ratios are less likely to use external finances if compared with the one with more pleasant experience. They may not be so careful in raising external finance.

> *'Previously, I had involved in more than three businesses. I was only 15 years old when I first involved in the business. At that time, I just used my own money and some amount of my parent's money. Same financing choices I had taken when I first started this business up. I think this may be because of the age factor. When I was young, I felt afraid to use a loan or any funds from others. However, my perception towards financing had changed. I've started using bank overdraft during growing stage of this business.'* (The owner of a Wholesale and Retail, Chinese)

> *'I chose to use internal funds for a start-up because I'm not confident to apply for a loan. That was may be because I'm still young at that time. I just completed my secondary school. However, now I'm quite open-minded and confident. That is why I've used bank loan for my current business operation. This may be because of my age and my exposure to the business.'* (The owner of Steel Trading and Retail, Malay)

> *'About 20 years ago, at that age, when I wanted to do something, I would do it no matter what. I ended up with overdraft facilities from more than one bank. I had almost all my personal assets secured against bank loans....but now, I do not think I'm going to borrow or use any debt anymore...may be because I'm getting older. What I'm concerning about now is just to make sure the business runs well. I would be satisfied as long as the cash is positive.'* (The owner of Tailoring and Dry Cleaning, Malay)

However, owner's age, experience, knowledge, and their perception and beliefs may not be the only factors influencing the capital structure choice of the small firms. The awareness of the owners regarding the financial facilities may influence the financing structure of the small firms.

> *'In my opinion, the awareness can influence the choice of each owner. If you know something, it will be easy for you to make a decision. In the case of choosing a capital to finance the operation of my company, I will choose the one that I know in detail. Let me give you an example, I used to finance this company with soft-loan offered by the SME Bank. I knew about the loan from the advertisement on television and radio. I then obtained a detailed explanation from the bank itself.'* (The owner of a Transportation and Logistics services, Chinese)

> *'An attractive package offered by the bank regarding the financial sources had attracted me to choose the bank financing which is a loan. The bank was my business banking bank. I also used bank overdraft for the same reason, which is an attractive package.'* (The owner of a Bakery and Cakes, Indian)

> *'As an old company, I can confidently say that the awareness concerning various types of funds is extremely important for financing decisions of the business. I used personal funds only at start-up age. It was not because I did not want to borrow, but in that situation, I was very naive and did not aware of the availability of financial facilities that are suitable for my firm.'* (Textile and Clothes Producer, Chinese)

Based on the responses discussed above, it can be concluded that the choice of capital structure of small firms may be the consequences of a mixture of factors which are related to the owner's age, education and experience, ethnicity, perceptions and beliefs, as well as awareness.

4.1.2 Firm-related factors

Only one-third of the respondents involve in manufacturing sectors and the remaining two-third operates in the service sectors. All firms are sole proprietorship except two of them are partnership. The size of the firms varies from 2 to 32 employees with an average size of 6 employees (SD=6.56). In terms of firm's age, it varies from 2 to 38 years, with the median age of 8 and average firm's age of 10.6 years (SD= 18.72). Respondents were asked to indicate which factors (firm-related) in their opinion influence their capital structure decisions and how these factors work in determining the capital structure of their firms.

The decision to choose the financial capital among small firms found to be influenced by several factors that are related to the firm. Many of determinants of capital structure identified by theoretical as well as empirical studies were revealed from the responses of this study. The respondents generally perceived business age to be important concerning the utilisation of external finance of their firms. Majority of them used their own money for financing their business at start-up stage (refer Table 1). When the business grows, they then look for an external fund such as debt or external equity, as the amount of capital needed become higher. In other words, the preference of sources of capital is different for each stage of business (see Dollinger, 1995).

> '*I have been in this business since 1980. Based on my experience in accessing the financing for this firm, the age of the firm can be one of the most influential factors. In the first stage, when I first started up this business, the financing choice was very limited for me. However, when the company reached its maturity, I found that many types of financing are available for this business. For example, my suppliers became more confident to give me credit terms now, whereby at the early stage of business, everything must be paid in cash. Bank financing had also become more accessible than before because they felt confident with the stability of our business.'* (The owner of Bakery and Cakes, Malay)
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> '*It is quite difficult for me to obtain the sources of finance. It may be because my business is still new and unknown to others. Up to now, I just used internal sources of financing like personal savings and funds from family members during start-up, while for monthly capital, I used retained earnings and maintained by using the same amount of capital for the first year. For the following year, I added some amount of capital. That was also by using internal funds.'* (The owner of air conditioner service, Chinese)
>
> *'For me, the longer you are in the business, the more financing choices will be available to you. I have been in this business for already 10 years. At the first stage of my business, I just used internal funds because it was very difficult for me to apply for external financing. However, when I was in the 3rd year of my business, there were various financing choices available for me, such as bank loan, trade credit, venture capital and et cetera. I would say that, the age of the business affects my financing preference.'* (The owner of a Car Trading and Insurance services, Malay)

Respondents also relate their choice of finance with the asset composition of firms, size, and profitability. The respondents argued that, the more assets the firm possessed, the more employees that the company employed, and the more profitability of the firm, the easier for the firms to obtain external sources of capital such as debt or external equity.

> *'I think my financing choices are really affected by the size of my firm. If I compare the availability of sources of finance previously (first start-up) and today, the financing sources are much more available for my firm. As the size of the firm becomes bigger than in the previous one, suppliers become more confident to give me credit terms. There is also a government grant available to me. During my sixth year of operation, I have decided to share the firm. As the size becomes bigger, the investor felt confident enough to invest their money into this business. That is why I said earlier on that, the size of my firm has really influenced my way of financing.*' (The owner of the catering service and restaurant, Malay)
>
> *'I will request for debt or external equity only when the profitability of the firm is poor. If not so, I will try to finance using internal sources of finance.'* (The owner of a Hardware and Painting, Chinese)
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> *'During early 1990's, this business had a problem and incurred losses. The business was unable to be financed by using internal funds; and because of that, I applied for a government loan and also bank loan. Luckily, my application for government loan had been approved. I used it to cover the losses and used it as a capital. When the business is stable, I just maintained using retained earnings and other internal funds.'* (The owner of a Tailoring and Dry Cleaning, Malay)
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> *'It was difficult for me to borrow from a bank due to insufficient collateral value of assets and unstable cash flows of my firm.'* (Handbag Designer, Malay)
>
> *'When the first time I applied for a bank loan, it was rejected. The reason given by the bank was because my firm provided insufficient security. I only had the business plan and my skills as a baker, but that was not strong enough to secure me any loans.'* (The owner of a Bakery and Cakes, Indian)
>
> *'When I started this business, I borrowed money from the bank. I gave bank 10% out of the total loan that I applied as a security. During my third year of business operation, again, I financed by using bank loan. This time, I provided my home plus business equipment as a security.'* (The owner of a Car Trading and Insurance Services, Indian)
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> *'To deal with the banks for loan applications, you need a lot of things. They will ask for a proper documentation, collateral and a lot more. The process is also tedious and sometimes it is better to use my own savings.'* (The *owner of an Optometry Services, Chinese)*

The last four comments provide some evidence that the firm's assets composition (tangible assets) will affect the capital structure of small firms. Enterprise with lesser collateral prefer to use internal funds instead of debt finance (see Onaolapo, 2015; Thippayana, 2014; Sogorb-Mira, 2005; Hall et al. 2004; Michaelas et al., 1999; Van der Wijst and Thurik, 1993) and vice versa.

Another important issue concerning asset structure of the firm is that, since small firms are not as informationally transparent as large firms, collateral is important for them to borrow. This can indirectly reduce the asymmetric information related costs in financing (Myres, 1984). Small firms often do not have to provide (audited) financial statements or do not issue traded securities. However, the information asymmetry problem can be abolished by preparing and providing sufficient information of the firms continuously.

> *'I prepare formal financial reports and record for my company's financial track for at least every week... Keeping financial record is essential for each firm in order to avoid the firm from losing its focus. I mean, the firm will be more focused as it knows the financial situations of the firm.'* (The owner of a Hardware and Painting, Chinese)
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> *'Poor documentation can hinder the firm from getting debt from outsiders.'* (The owner of a Bakery and Cakes, Malay)
>
> *'My firm prepares a formal report and proper documentation. Both can assist me when dealing with banks or suppliers. If your firm only used internal funds, it may not be necessary for you to prepare a proper report or documentation. If your firm used or plan to use external capital, it would be better for you to prepare it.'* (The owner of a Textile and Clothes, Chinese)
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> *'My previous personal credit records affected my financing choice. It is very difficult for me to get the loan whether from the bank or the government as my previous credit records were poor.'* (Ice Cube Producer, Malay)

Other than information adequacy, the respondents also commented on the management planning of the firm. Business plan, for example, found to be an important document for the small firms in obtaining external finance (Berger and Udell, 1998; Harvey and Evans, 1995) or in maintaining the flow of the firm's performance. Some of the respondents reported that other than a business plan, strategic plan, management structure, as well as business performance appraisal are also significant in affecting the financial structure of their firms.

> *'Business plan is essential for a business start-up especially when the firm wants to apply for an external fund. I had prepared a business plan when I applied for a bank loan during business start-up.'* (The Handbag Designer, Indian)
>
> *'My firm prepare the detail of task schedule for every month. This task schedule includes all work to be done and works that had been done by each of the employees, including myself. Thus, everyone knows what they should do and they will try their best to achieve company's target. When the bank manager saw this, I mean the schedule, he felt confident to provide the loan for us.'* (The owner of Hardware and Painting, Indian)

Some respondents indicate that the relationship or networking between their firms and the lenders as one of the factors influencing the capital structure choice of their firms. This is in line with the previous study of Nguyen and Ramachandran (2006), Pfeffer and Salancik (2003) and Berger and Udell (1998).

> *'For sure, when you know the lender, it would be very easy for you to borrow. Since I have already involved in this field for almost 10 years, of course, my network is quite wide. This*

> *may ease me to handle my business whether in term of customer service, daily business activities and financing. For example, I obtained credit terms from my suppliers as I've close relationship with them; I received a grant from the government as I knew one of the main person in that particular department; I got an offer from my business banking bank as I'm the client of that bank for more than 10 years.'* (The owner of Car Trading and Insurance Services, Indian)

> *'I'm of the opinion that, close relationship with anyone who is related to your business is particularly essential. If you have a poor relationship or low networking, then it would be difficult for you to get an external fund like a bank loan, government grant or loan, venture capital and so on.'* (The Cosmetic Producer, Indian)

Other than all the above factors, other significant factors as mentioned by the respondents are the objectives and goals of the owner-managers. They emphasised that, even though a number of owner-related factors and other firm characteristics may largely affect their capital structure decisions, the single most important influence is their objectives and goals, which largely determined the management of the firms. For example, if the firms aim to maintain control, they will try to avoid external equity financing; no matter how close their relationship with the lender, how old the company is, the level of experience of the owner, and so on.

> *'Before you plan for something, you should know your business aim. In my case, I am doing business in order to fit around family commitments and improve my family lifestyle. Therefore, for any decision that I want to make, I should consider those two things.'* (The owner of Tailoring and Dry Cleaning, Malay)

> *'My main concern was to improve my personal lifestyle…my financing choice was reflected by my business objectives. Until today, I used more debt compared with internal funds.'* (The owner of Car Trading and Insurance Services, Indian)

> *'I'm doing business to change my life, to make it better, and to make money. When I want to make a decision regarding financing, I will make sure that it is in line with my objectives and planning. For example, during the third year of business, when my firm introduced a new cosmetic product, there was one investor wanted to invest money into my firm. Since the offer was interesting, I then accepted the offer and used the finance from a private investor for that particular product.'* (The Cosmetic Producer, Indian)

> *'Previously, I taught entrepreneurship and I used to assist my students in doing small businesses. After pension, I started this business because I want to apply all my knowledge and skills that I have. I only used my personal savings for the first start-up.'* (The owner of a Business Consulting, Chinese)

> *'I would use whatever sources available to me, regardless of internal or external. As long as I can expand my business, I'll use it. If by raising funds from debt financing is the only way for the firm to raise profit, I'll use it*.' (The owner of Wholesale and Retail, Chinese)

'Want to maintain control was the main goal of my business. I want to be my own boss and a decision maker.' (Ice Cube Producer, Malay)

'I think most of the business owners want to be independent. However, in reality, not everyone was really independent. Why did I say that? This is because, when you financed by using external funds, then you would automatically not 100% independent. However, I am totally free from outsiders. All my funds were from internal. Anything I bought for this business also in cash.' (The owner of Optometry Service, Chinese)

'Business is something like a compulsory job for our family since my late grandfather. This business was started by my father. All my siblings are working together. We all have our share in this company. We will try our best to maintain the share of this company. Therefore, we will avoid using any fund which will make us lose our control of the business.' (Textile and Clothes Producer, Chinese)

4.2 Indirect factors affecting capital structure

More than fifty percent of the respondents in this study indicate that the 'business environments' as well as 'business cultural orientation' influence their preference for finance. For example, the government policy, which restricted some grants or loans to certain groups, may hinder some small firms to use such financing facilities. Another example is in terms of environmental pressure such as advanced technology. It may push small firms to employ more external finance in order for them to be able to compete and survive in their businesses. Below are some evidence related to these two factors (i.e. business cultural and business environment).

'Last two years, I've applied for the government grant. The main reason I applied for the grant was that the rules and regulations were less stringent at that time.' (The owner of a Construction firm, Malay)

'I think the social environment is also important in influencing my business decisions. I knew about the availability of capital sources from social gatherings and functions conducted by the state government; i.e. women society.' (The owner of a Bakery and Cakes, Indian)

'The performance of my firm was unstable for the last year, 2009. It may be due to the global economic crisis; hence the demand for my product was decreased dramatically. So, I could not totally depend on my own money or internal funds. I had applied for the government loan.' (The Cosmetic Producer, Indian).

'Sales for the last year were quite low due to widespread recession problem. I didn't apply for a bank loan because the interest rate was too high at that time.' (The owner of Hardware and Painting, Chinese)

'Harmonious working relationship is essential for the firm to be efficient and effective. This indirectly affects the needs of sources of capital.' (Textile and clothes producer, Chinese)

> *'An aggressive financing policy of the company is important for my company's survival as I'll be more careful in planning my business, setting goals for the firm, as well as in the utilisation of the source of capital.'* (The owner of Construction firm, Malay)

Thus, from the response presented so far, it can be argued that capital structure decisions in small firms are strongly influenced by various factors, either directly or indirectly. Different factors may have different influences on the capital structure of the firms depending on the circumstances happening in the firm at that time.

5. DISCUSSION

A number of significant results have been derived from this study. The results show the financing behaviours of the micro and small firms in Malaysia follow the pecking order theory (Myers and Majluf, 1984). Personal sources of finance proved significant for all ethnic groups during the initial stage of the business and the subsequent years, except for Malay and Indian who appeared to prefer external finances during the growing stage. Bank finance appeared to be the favourable external source of finance. The 'government grant and loan' is the least preferred financial source by ethnic minority groups especially Chinese. The use of internal sources instead of external sources is mostly driven by the desire of the owner-manager to maintain control, as most of them are family businesses, and due to their averse behaviour toward external sources of finance. This is in parallel with the argument of Michaelas et al. (1998) who argued that the preference of the small firms on internal over external funds is mainly because they want to maintain control and because of their beliefs and attitudes toward external finance.

Table 3: Factors influencing capital structure derived from interviews and focus groups

Owner-related factors	Firm-related factors	Other factors (indirectly related)
Age Ethnicity Education Perceptions and beliefs	Age Size Asset structure Profitability	Business environment (e.g. government policy, social pressure, economic condition, etc)
Awareness	Business planning Objectives and goals Information asymmetry Relationship & Networking	Business cultural orientations (e.g. preserve public image, group interest, group loyalty, harmony, etc)

Further, the identification of CSD was grouped into 15 constructs (see Table 3), which shared commonalities with existing models. It showed that these models suggest a sound degree of cross-cultural generalisation. CSD included asset structure, firm size, firm's age, profitability, asymmetry information, business planning, objectives and goals, relationship and networking, awareness, owner's education, owner's age, ethnicity, perceptions and beliefs, business culture, and business environment. All these constructs were reported to be important by participants, even though some behaviour associated with each determinant were reported more frequently by one group than the other.

For instance, the majority of entrepreneurs agreed that asset structure was crucial for them, specifically the ability to provide enough security for the lender. In addition, awareness is also important as it reflects the ability to identify the best financing package which is appropriate for them. Asymmetry information is also vital because by having enough information to be provided to outsiders, it may increase the chances of the firm to obtain external funds or additional funds needed. The business age was also seen by participants as being important. Participants believed that, as the business grows, there will be lots of financial packages available for business. Business-lender relationship, as reflected in the ability to establish and maintain strong relationships with lenders or suppliers, was described as crucial for participants in so far as establishing reliable networks, and striving to increase access to resources and opportunities. Other significant factors were the education and experience. The findings suggested that participants believed a continuous learning process, formally or informally, would influence their financing preferences. It would enable the organisations to survive through time.

The identification of additional categories of determinants of capital structure suggests that the existing models (see Romano et al., 2001; Michaelas et al., 1998) may need to be revised to enhance their applicability to the measurement of capital structure decision in Malaysia. Besides, the data generated by the present study provide a referencing item pool for modifying and updating the existing instrument. The additional items identified will be incorporated to enhance the measurement of CSD in Malaysia.

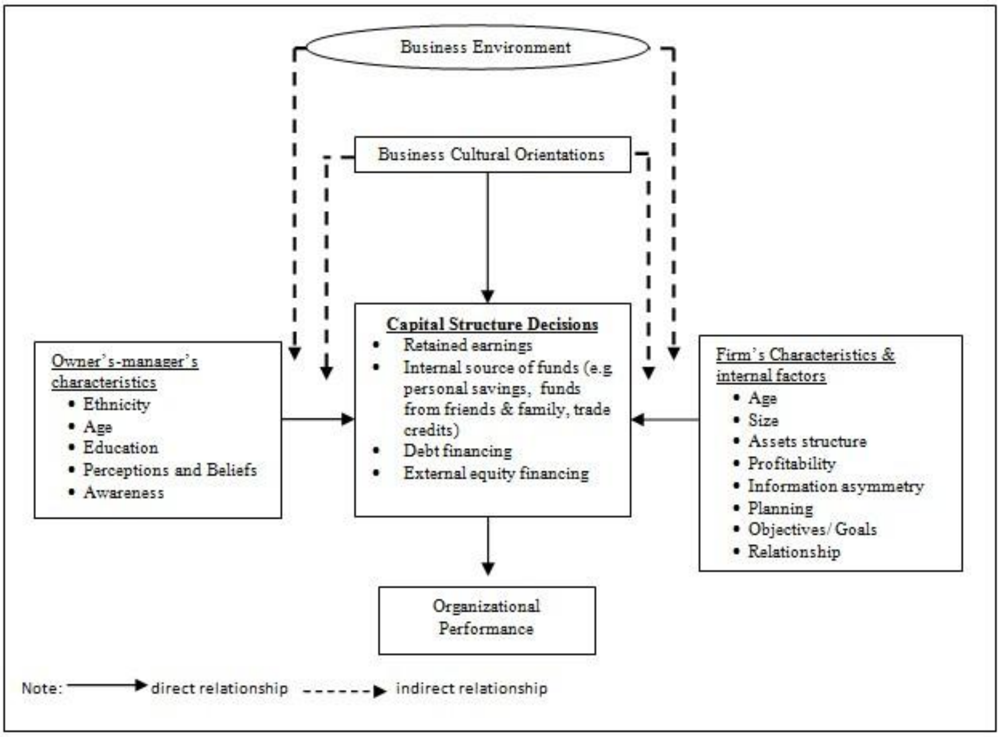

Figure 1: The Capital Structure Determinant's Model based on Previous Studies & Qualitative Study

Figure 1 presents a model based on this qualitative study. The figure indicates the capital structure decision-making process of small firms in Malaysia. The dotted arrows represent indirect relationships between the variables to the capital structure. The effect of external factors, the business environment, for example, may influence the capital structure decision-making of one firm through the influence on the owner-manager, and the firms themselves. On the other hand, the cultural factor may directly influence the capital structure decisions and indirectly influence through its influence on the owner-manager and the firm.

Moreover, this study will advance current knowledge by adding alternative insights to factors that contribute to the capital structure of the small firms. This research will demonstrate factors that perceived to be important to the small firms when choosing the capital structure. The capital structure of the firm is not just determined by the owner's characteristics and firm's characteristics. Rather, it is also influenced by the environment as well as business cultural factors, indirectly. The factors that affect the capital structure of small firms identified by the interviews and focus groups discussions are summarised in Table 3.

6. CONCLUSIONS

This study aims to discover a set of determinants that perceived to be important for capital structure choice by MSEs' owners in Malaysia. The outcomes of this study suggested that the existing frameworks constitute valid descriptions of capital structure determinants. However, there exist additional determinants and items, which suggest that the owners are required to be sensitive to issues of culture, awareness, and business environment.

Essentially, the qualitative research captured numerous important factors influence capital structure choice which was consistent with previous studies. A theoretical contribution of this study is the qualitative method used to uncover the determinants of capital structure decisions that aid the researcher to understand the topic. A qualitative study has not been widely used as a capital structure research technique. Relatively few researchers have adapted this method (Smallbone et al., 2003; Michaeles et al., 1998).

Empirically, this study is the first study that studied on MSEs finance through the interview and focus-group methods within Malaysian context. This paper thus contributes to the growing number of country-specific studies on determinants of capital structure in MSEs by providing original empirical evidence in Malaysia context, utilising a sample not restricted by sector.

The qualitative data reported here provides evidence of the universality of some aspects of CSD and at the same time generates more evidence about the possible cultural underpinnings of these determinants. In line with expectations, the cultural orientations of entrepreneurs play a part in determining the determinants they perceived as important. It should also be highlighted that the aim of this study was not to draw definitive conclusions about the link between determinants of capital structure and capital structure choice among MSEs. However, it is important to bear in mind that, in this study, the determinants identified by Malay, Chinese, and Indian entrepreneurs, both new and existing determinants were being combined in order to form a new model of capital structure decision-making that is more suitable for MSEs.

This study thus seeks to provide significant insights into the financing preferences of the entrepreneurs with relevant implementations to business practitioners, academics, and policy-makers. For the academicians and theorists, this information can help them formulate special procedures or rules which are relevant and focus directly on the needs of such financing facilities by MSEs. For those involved in the promotion and development of MSEs such as extension officers and small business consultants, findings from the present research can assist them in formulating better and more meaningful strategies in preparing the MSEs to cope with demands and challenges of the twenty-first century. For the MSEs' owners, this study can assist them in choosing the right financial capital.

Despite several limitations discussed above, this paper also presents some limitations of the study. First, the qualitative study, by its nature, was restricted to those respondents who can spend their time answering the questions verbally. The study did not include any written response. Therefore, care should be given in interpreting these findings. Besides, the sample consists only of MSEs from a specific region; a fact implies that we are not able to make generalisations in the region. The results are representative of micro, small, and medium-sized enterprises in Malaysia and are not necessarily able to generalise to other sectors or countries. As pointed out by Chen (2006) for China and Booth et al. (2001) for other countries, it is vital to be aware of the legal, cultural and institutional differences between developing economies and the Western economies.

Moreover, this paper also provides some directions for future research in this study. This study was the first study on the topic of MSEs' capital structure (i.e. major ethnic groups) in Malaysia and has only examined the financing behaviours of Malaysian MSEs' owners in the east coast region which is significantly different if compared to other contexts. It would be interesting to look at financing patterns of MSEs in different regions or different context. Besides, better results may be obtained by conducting more interviews or focus group studies.

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