FINANCING OF SMALL AND MEDIUM ENTERPRISES (SMEs) IN LIBYA: DETERMINANTS OF EXTERNAL FORMAL FINANCING
CONVENTIONAL AND ISLAMIC PERSPECTIVE

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July 2014
AUTHOR DECLARATION

بسم الله الرحمن الرحيم

I hereby declare that the work in this thesis is my own except for quotations and summaries which have been duly acknowledged.

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بسم الله الرحمن الرحيم

In the Name of Allah the Most Merciful and Compassionate

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ABSTRAK

Economic development and growth are significantly linked to the consistent and sustainable sector of small and medium enterprises (SMEs). As a country that is trying to realize its dream after the 2011 Revolution, Libya is seeking to diversify its industry-based sector in order to reduce its over-dependence on the volatile oil sector. To achieve this goal, the Libyan government launched the National Program for the Development of Small and Medium Enterprises in 2008 to frame policies and programs in cultivating Libyan SMEs. However, the access to funds for the development and sustainability of SMEs has become a major predicament in many developing countries, including Libya. Banks are the frontrunners in financing and advising SMEs. The main question of this research is, “Which of the SMEs can apply for and can access bank loans?” Four theories, namely; human capital, firm, business strategy, and information asymmetry, constitute the study’s theoretical framework. The three main objectives of the study are as follows: (i) to develop a bank loan model based on applicability, (ii) to develop a bank loan model based on accessibility, and (iii) to assess the tendency of SMEs to use the Islamic bank. Three models were developed using quantitative methods with a hypothetical-deductive testing approach. Model I (N = 364) used primary data on loan applications gathered from the questionnaires. Model II (N = 118) extracted the survey data from the same questionnaires. Model III (N = 364) used primary data on the tendency of SMEs to use Islamic banks gathered from the same questionnaires. The logistic regression and Mann-Whitney test indicate that the business experience of the firm’s owner does not have a significant relation with the firm’s application for a bank loan. The educational background of the firm’s owner, the firm’s size, collaterals, and loans with interest were found to be negatively related to application of the firm for a bank loan. However, the firm’s business plans and its start-up with bank loan were found to be positively related to the firm’s application for bank loans. Yet, business plans, experience, and educational background were insignificant to the firm’s access to bank loans. The firm’s age, size, and start-up with bank loan were negatively related to its difficulties in securing a loan. It is found the tendency to use Islamic bank varies between those firms which consider formal financing with the ones relying on informal financing with the latter tends more to use Islamic bank. This study can serve academic researchers, policy makers, and developing countries as a model of SMEs’ accessibility to external formal finance (i.e., conventional and Islamic finance).
ملخص البحث

ترتبط التنمية الاقتصادية في بلدان العالم بشكل ملحوظ مع التنمية المستدامة لقطاع المشروعات الصغيرة والمتوسطة. ولعبت ليبيا أدوارًا حاسمة في بلدان المنطقة فيما بعد توقيع اتفاقية الاحترام المشترك في النرويج، وتمتلك نفس القضايا مع المنتجات الصغيرة والمتوسطة، وتعتبر ليبيا أحد الدول التي تسعى لتحقيق هدف التنمية المستدامة. وللبحث في ذلك، تم اعتماد على قطاع النفط. وتم استخدام الهدف من الهدف أن تكون البيت في الحكومة الليبية برنامج)* wildlife* ووليد لدعم القطاع الصغير والمتوسط.

وتعد مشكلة تمويل المشروعات الصغيرة والمتوسطة من أهم المعوقات التي تواجه هذه المشروعات، خاصة في البلدان النامية بما فيها ليبيا، إذ تعتبر المصارف المصدر الوحيد لتمويل المشروعات الصغيرة والمتوسطة في تلك الدول.

من هنا كانت الأهداف الأساسية لهذا البحث (i) تطوير نموذج الطلب على الإقراض المصرفي (ii) تطوير نموذج احتمالية الحصول على القروض المصرفية (iii) تقييم ميل رغبة أصحاب المشروعات باستخدام المصارف الإسلامية.

تم اختيار أربع نظريات لتشكل الإطار النظري للدراسة: نظرية رأس المال البشري والنظرية الاستراتيجية ونظرية المشروع ونظرية عدم تناسق المعلومات. ولتحقيق أهداف الدراسة تم استخدام نهج التحليل الكمي، لتطوير ثلاثة نماذج وذلك بعد استخدام البيانات الأولية الناتجة من الاستجابة التي تم توزيعها على 364 مدير مشروع صغير وتموزع.

من خلال نتائج التحليل (الانحدار اللوجستي) واختبار (ام ويتني) أشارت النتائج إلى وجود علاقة سلبية بين مستوى تعلم المدير، والطلب على الإقراض المصرفي في حين أن خبرة المدير ليست لها أي تأثير على طلب الإقراض المصرفي، وحجم المشروع والضمانات على القروض، و كذلك القروض مع الفوائد جميعها لها تأثير سلبي على طلب الإقراض المصرفي، ومتى كلا المشروع والقروض مع الفوائد للمسؤولية للطلب على الإقراض المصرفي.

فيما يتعلق بصعوبات الحصول على القروض المصرفي، أظهرت النتائج أن حجم المشروع وعمر، وكذلك علاقة المشروع بالقروض، وكلاهما عامل له أهمية وتأثير سلبي علىлов要有 معادلات في القروض والفرنك، ثم أظهرت النتائج أن مستوى التعليم، والخبرة للمدير، وكذلك خطة العمل للمشروع يعتمد عليها أهمية إمكانية حصول المشروع على القروض المصرفي.

واخيراً، أظهرت الدراسة وجود فروقات بين نوع التمويل المستخدم في المشروع (قرض مصري، أو تمويل غير رسمي) ورغبة أصحاب المشروعات في استخدام المصارف الإسلامية.
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Appendix 1: The opinions of experts and arbitrators of questionnaire

The Honorable Professor/

The researcher attachment the copy of the test, and looks for your guidance and your comments in terms of:-

1- The clarity extent of the wording of paragraphs.

2- The suitability of paragraphs to objectives of the study.

3- Observations and modifications proposed by you.

4- The validity extent of paragraphs to measure financing SMEs in Libya by the access to external finance, using formal or informal finance, kind and level of obstacles that they faced also the desire of owner manager to use Islamic finance particularly musharaka and mudaraba.

Please accept my thanks and high appreciation.

The researcher: Khalid Hassan Abdesamed

Financing of Small and Medium Enterprises (SMEs) in Libya: Determinant of The external formal finance (Conventional and Islamic finance)

Abstract:

Small and medium-sized enterprises (SMEs) are inevitably paramount in a strategic economic build up of any country in the world. This is due to the role these enterprises play in lowering unemployment rate and strengthening economic growth. Taking into consideration the case of Libya where the government is striving to diversify its production base, developing small and medium-sized enterprises (SMEs) could provide better solutions to that matter. However, formal lending institutions such as commercial banks are more often reluctant in offering loans to those small firms. This study identifies variety which and why small and medium-sized enterprises find it difficult to secure loans form formal institutions? Some of the reasons could be to due to size and the age of the firm, the information provided by the firm or religious in nature. The earlier two are called excluded involuntarily and the later is called self-excluded group. “Financial gap” in the sectors of small and medium-sized enterprises
has been the focusing points among the scholars and practitioners in developed and developing countries. Despite attempts to close the “gap” the problem persists. Therefore, this thesis aims to contribute to a better understanding of the practices and problems of financing SMEs in Libya. It also investigates the desire of owner managers to use Islamic finance such as Musharaka and Mudaraba. The study will collect data from a sample of 530 SMEs through survey in agricultural, industrial, trade and service sectors in three regions of Libya. (Tripoli) in the north, (Sabha) in the south and (Banghazi) in west north. The study will use the methods of descriptive and regression analysis. The findings of the study will highlight all the problems and provide possible solutions to them for the SMEs owners and policy makers in Libya in their quest for finding concrete policy in tackling these problems.

**Research Questions**

The main question is, “Which SMEs have applied for and have accessed external formal finance, and which firms have not done so?” The researcher framed the research questions to solve the following issues:
1. What factors determine the bank loan application of SMEs?
2. For SMEs that applied for a bank loan, what factors determine the bank loan visibility for any SME?
3. What factors determine the preference of SMEs to use Islamic banks?

**Research Objectives**

The main objectives of this research are as follows:
1. To develop a model of bank loan application.
2. To develop a model of bank loan availability.
3. To develop a model of Islamic bank desirability