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TOWARDS INTERACTIVE MODERN FINANCE THEORY AND
BEHAVIOURAL FINANCE IN SHAPING ENTREPRENEURIAL
FINANCIAL MANAGEMENT STRATEGIES OF INDIGENOUS
MANUFACTURING SMALL AND MEDIUM ENTERPRISES IN
ZIMBABWE.

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A THESIS SUBMITTED TO THE GRADUATE SCHOOL OF BUSINESS IN
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ABSTRACT

The question of how to tailor the prescriptions of capital budgeting and capital structure theories to the entrepreneurial finance circumstances of small firms remains unanswered. In exploiting this gap in knowledge, this study examined how modern finance theory and behavioural finance interacted to shape entrepreneurial finance strategies of indigenous manufacturing small and medium enterprises in Zimbabwe. The main objective of the study was to develop capital budgeting and capital structure models that predict and/explain the financial strategy decision-making of indigenous manufacturing small and medium enterprises in Zimbabwe. The study adopted a mixed methods research design to investigate entrepreneurial finance strategies of the enterprises through the combined lenses of modern finance theory and behavioural finance. In the explanatory sequential design adopted, quantitative data collection and analysis were conducted first, followed by qualitative data collection and analysis. In the quantitative phase of the study, 75 usable questionnaires were obtained from a survey of 146 small and medium enterprises drawn from Harare, Chitungwiza, Mutare and Marondera. In the qualitative phase of the study, in-depth interviews were held with ten owner-managers drawn from a multiple-case study of ten enterprises selected from the 75 firms that returned usable questionnaires. Univariate analysis employing descriptive statistics, bivariate analysis employing Spearman's correlations and multivariate analysis employing ordinal capital budgeting and capital structure predictive models developed for the study were utilized to analyze quantitative data using IBM SPSS Statistics. Analytical generalization was used to analyze qualitative data. Informal capital budgeting analysis was preferred over formal capital budgeting analysis by the enterprises. Where formal capital budgeting analysis was applied, the enterprises preferred non-discounted cash flow techniques over discounted cash flow techniques. Most of the firm-level and managerial-level factors were not able to influence capital budgeting and capital structure decision-making of the enterprises. The firms did not apply the static trade-off theory in making capital structure decisions, while they followed a different version of financial pecking order from that prescribed by modern finance theory. The enterprises were not able to separate investment and financing decisions because of the opaque capital market they faced. These observations revealed inconsistencies between capital budgeting and capital structure theories and the practices of the enterprises. The owner-managers of the enterprises relied more on decision-making heuristics and cognitive biases in capital budgeting and capital structure decision-making. The application of decision-making heuristics and cognitive biases accounted for the inconsistencies between capital budgeting and capital structure theories and practices of the enterprises. The utilization of both capital budgeting and capital structure theories, and heuristics indicated that the modern finance theory lens and behavioural finance lens interacted to shape the entrepreneurial financial management strategies of the enterprises. However, behavioural finance had a greater influence on the ultimate capital budgeting and capital structure decision-making through the strong influence of decision-making heuristics. From the results and literature, a Modern Finance Theory and Behavioural Finance Interactive Theoretical Model was developed to predict and/explain the capital budgeting and capital structure decision-making of the enterprises. Business, government and academia, among other stakeholders, should use the models developed in this study as tools to understand the entrepreneurial financial management behaviour of the enterprises in order to generate optimal capital budgeting and capital structure decision-making.