Frontiers of Entrepreneurship Research

Volume 34 | Issue 3
CHAPTER III. FINANCING

Article 9

6-7-2014

RESOURCEFUL FINANCING BY NEW FIRMS (INTERACTIVE PAPER)

John M. Mueller
Western Michigan University, USA, john.mueller@wmich.edu

David Dubofsky
University of Louisville, USA

INTERACTIVE PAPER

RESOURCEFUL FINANCING BY NEW FIRMS

John M. Mueller, Western Michigan University, USA
David Dubofsky, University of Louisville, USA

Principal Topic

Financial capital is one of the fundamental resources needed to start and operate a firm (Cooper et al, 1994), and is a main factor in the performance of new firms (e.g. Cressy, 2006; Parker & Van Praag, 2006). Many new firms look for external funds to survive and grow their venture during their early years (Cressy, 2006), since many founders are personally constrained financially due to a lack of personal wealth (e.g. Evans & Jovanovic, 1989). Debt often becomes the first sizeable financing option available to new firms (e.g. Berger & Udell, 1998).

While banks can provide debt to assist new firms to overcome the financial constraints they face, they may ration credit to new firms due to information asymmetry prevalent in the relationship with their borrowers (e.g. Stiglitz & Weiss, 1981; Becchetti et al, 2011; Keeton, 1979). With the possibility that creditors ration credit and turn down requests for all or part of the requested funds by viable new firms that objectively should be able to service the debt, new firms will be less able to successfully operate and grow. This suggests that new firms require additional sources of external financing when their initial creditor imposes credit limits on them.

Entrepreneurship research suggests that new firms may continue to survive even when rationed credit since the founders who start new firms tend to be persistent, persevere longer than rational decision making models would predict, and are resourceful (Baker & Nelson, 2005; Bhide, 1992; Hmieleski & Corbett, 2008). The resourceful behavior of founders can lead to them tapping into additional credit sources after they have been rationed credit by their primary source (Stiglitz & Weiss, 1981; Myers & Majluf, 1984; Keeton, 1979). Using multiple credit sources could provide access to additional debt capital (capital constraint argument). This leads to the following research question: *Does resourceful financing, in the form of multiple credit source usage, affect the performance (survival and growth) of new firms?*

Method

Using the Kauffman Firm Survey, a 6-year longitudinal study is performed to test the hypotheses and to answer the research question. Survival and growth curve analyses are performed on the data set. Additional analyses are performed to test the robustness of the results.

Results and Implications

The results indicate that firms employing multiple credit sources are associated with a lower chance of survival. Overall, however, for those firms that survive, higher multiple credit source usage is associated with higher growth rates. These results suggest that being resourceful in financing in the form of multiple credit source usage is beneficial to new firms that are already growing faster than average, but not new firms that are growing slower than average. This could indicate the multiple credit source financing strategy should be used because the firm wants to use multiple credit sources, not because it has to use multiple credit sources.

CONTACT: John M. Mueller; john.mueller@wmich.edu; (T): +1-269-387-6056; Western Michigan University, Kalamazoo, Michigan 49008.