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Abstract
This study examines the initial, seasonal, and refinancing characteristics of 67 minority business owners. The results are compared to the financial characteristics of women-owned and mixed ownership small firms. Minority-owned firms are found to rely primarily on equity to finance initial operations. Minority business owners' initial debt was commonly obtained through Small Business Administration (SBA)guaranteed loans and government grants. A very large percent of the minority business owners who acquired debt were required to provide numerous supporting documents. The results indicate that minority firms that experienced difficulty in obtaining initial capital continue to experience financial problems relating to operations.

Disciplines
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FINANCING PATTERNS OF MINORITY-OWNED SMALL BUSINESS

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ABSTRACT

This study examines the initial, seasonal, and refinancing characteristics of 67 minority business owners. The results are compared to the financial characteristics of women-owned and mixed ownership small firms. Minority-owned firms are found to rely primarily on equity to finance initial operations. Minority business owners' initial debt was commonly obtained through Small Business Administration (SBA) guaranteed loans and government grants. A very large percent of the minority business owners who acquired debt were required to provide numerous supporting documents. The results indicate that minority firms that experienced difficulty in obtaining initial capital continue to experience financial problems relating to operations.

INRODUCTION

Small firms make an important contribution to the U.S. economy. The dynamic nature of small firms has been an important factor contributing to employment growth, product innovation, export growth, and regional economic development. While their contribution remains significant, the risk of starting a small firm is very large. Dodge and Robbins (1992) report that 55 percent of small firms fail within five years of starting and 81 percent fail within ten years. Reasons for the high failure rate among small firms include poor managerial skills, inadequate planning, and inappropriate financial resources.

The nature of a firm's capital structure has long been recognized as impacting the riskiness of the firm. Beginning with Modigliani and Miller (1958), the theory of a firm's capital structure has focused on the risk-return trade-off between the use of debt versus equity. In general, the higher the level of debt, the greater the risk of the firm. Brennan and Schwartz (1978) show that large levels of debt in the capital structure increase the likelihood of firm failure. The development of finance theory has, however, relied on assumptions of perfect capital markets (Brigham & Gapenski, 1993).

The economic environment in which small firms operate is not consistent with these perfect market assumptions. Carter and Van Auken (1991) express that small firms have limited access to both equity and debt capital markets. As a result, small firms are more reliant on debt financing—especially from financial institutions and accounts payable. Recent research on the financing of small firms is increasing our understanding of the specific sources of capital used to fund initial operations. Van Auken and Carter (1989) report a heavy reliance on personal equity and borrowing from financial institutions and friends or relatives to finance initial operations.

Van Auken, Gaskill, and Kao (forthcoming) examine the financing patterns among women-owned small firms. That research shows that women entrepreneurs use a much greater percentage of equity to finance their initial operations than was found by Van Auken and Carter (1989). In addition, the small women-owned firms generally relied more heavily on personal equity and friends or relatives and less on borrowing from lending institutions than small firms in general.

In an early study of the financial characteristics of minority-owned firms, Scott (1983) examined several financial characteristics of minority versus non-minority firms and found little difference in the relative levels of debt between the two categories of firms. Bates (1991) found that commercial banks extend small loans to black business owners than to white business owners. The great importance of lending institutions in financing small firms, coupled with the finding by Bates of commercial banks' reluctance to extend loans to black owners, results in black-owned firms being at a competitive disadvantage in the marketplace. They remain undercapitalized and are less able to gain on market opportunities. A recent study by Feldman, Koberg and Dean (1991) examined the background and path to ownership and sources of capital used to finance small minority-owned firms. They found that personal savings was ranked by the vast majority of firms as the most important source of capital. Lending institutions and friends or relatives were also commonly used and important sources of capital. Capital was infrequently obtained from other potential sources, such as third party investors, venture capital, government, and other sources.

The purpose of this paper is to present the results of a survey that examined the characteristics of initial financing and subsequently acquired capital of 67 minority-owned firms. While previous studies examined several aspects of the financing of minority-owned firms, this study identifies specific sources of capital, the relative percentage used of each source of capital, and financing mix. In addition, loan requirements from lending institutions and the use of seasonal financing are examined. Correlation analysis is used to determine the relationship between the difficulty of obtaining initial capital and the 1) financing mix, 2) lending requirements, and 3) lack of capital for operations. Such a study provides greater insight into how minority firms are financed. Comparisons of these results with other similar studies can reveal financial constraints experienced by minority-owned firms and how minority owners adapt to financial market constraints. Due to the differences in geographical scope and time-frames, statistical test of significance that compared the capitalization differences between minority-owned firms in this study with previous studies were not made. Such statistical tests would not be valid. Additionally, the purpose of the paper is to report on the capitalization experiences of minority-owned firms. In such a study, hypotheses were not appropriate and, thus, not developed.

SAMPLING METHODOLOGY

An attempt was made to identify as many minority-owned firms in Iowa as possible. As such, the sample was obtained from several sources. One source was a list of minority-owned firms from the Iowa Department of Economic Development, Office of Minority Affairs. In addition, the Chambers of Commerce in the ten cities in Iowa having the largest minority populations were asked to provide a list of minority-owned firms operating in their community. These sources were supplemented by membership lists from minority business associations. The final sample contained 194 firms located throughout the state of Iowa.

A questionnaire was developed and pretested in July and August, 1992. The construction of the questionnaire used previous studies of small firms' capitalization. By using similar questions, comparisons between minority-owned firm's acquisition of capital and other owner-

ship categories could be made. The questionnaire contained sections requesting information on the characteristics of minority-owned firms and sources of capital (both initial, refinancing, and seasonal capital). The questionnaire also asked several questions concerning the difficulty of obtaining capital and the degree to which lack of capital has affected operations. All mailings occurred during September and October, 1992. A total of 67 usable questionnaires were returned, providing a 35 percent response rate.

RESULTS

Business Characteristics

Approximately 29.9 percent of the responding firms were service businesses, 26.9 percent were construction, and 14.9 percent were retail businesses. The remaining 28.3 percent were in other business categories, such as professional, wholesale, and manufacturing. The *Survey of Minority-Owned Business Enterprises* (U.S. Bureau of Census, 1990) reported 55 percent of the minority-owned firms in Iowa were service firms and 20 percent were retail firms.

Approximately 52 percent of the minority-owned firms were operated as sole proprietorships, 40 percent as corporations, and 8 percent as partnerships. Approximately 50.7 percent identified their target market as being local, 31.3 percent identified a regional market, 11.9 percent served a national market, and 6.0 percent reported serving an international market. Almost one-half (49.3 percent) were located in cities larger than 100,000. The large percent located in larger cities is not surprising since most minorities in Iowa reside in larger communities.

Approximately 60 percent of the minority-owned firms had an initial capitalization of less than $20,000. About 28 percent had an initial capitalization between $20,001-$100,000, and the remaining 22 percent had an initial capitalization greater than $100,000. These results are consistent with the reported small initial capitalization of other small firms in Iowa (Van Auken & Carter, 1989). Bates (1991) also reported minority firms as being quite small.

Acquisition of Initial Capital

The average initial financing mix among the minority business owners was approximately 65 percent equity and 35 percent debt. This compares with an average initial financing mix among women business owners of 76 percent equity and 24 percent debt (Van Auken, Gaskill, & Kao, forthcoming). The average initial financing structure for a mixed ownership sample of small businesses was 45 percent equity and 55 percent debt (Van Auken & Carter, 1989). The heavy reliance on equity by minority small business owners to finance initial operations has been reported by Bates (1991). According to Bates, only low risk and financially secure minority firms are able to acquire debt financing. The difficulty of obtaining loans from lending institutions has resulted in the minority small business owners' use of greater levels of equity. Thus, the low level of debt in the initial capital structure is not surprising.

The distribution of equity versus debt in the capital structure indicated that 16.7 percent of the minority firms were financed using no equity (100 percent debt financed) and 55 percent were financed using no debt (100 percent equity financed). The financing mix of the remaining firms varied from equity levels of 2 to 67 percent of total capital. Approximately 71 percent of these remaining firms used less than 35 percent equity in their initial capital structure, and 29 percent used 36 to 67 percent equity in their capital structure. The distribution of equity versus debt

among the minority business owners is similar to that found among women business owners by Van Auken, Gaskill, and Kao (forthcoming). About 68 percent of the women business owners were 100 percent equity financed, while about 30 percent were 100 percent debt financed. Van Auken and Carter (1989) found a bipolar financing mix among small firms in that about 30 percent were 100 percent equity financed and 30 percent were 100 percent debt financed.

Table 1 shows the sources and composition of initial capital. The information in the table covering equity capital includes only those firms using equity capital in their initial financing structure. A similar criteria was used for initial debt capital. Table 1 demonstrates the importance of personal savings to finance the equity portion of initial operations. Approximately 73.4 percent of the respondents used personal savings as start-up capital and most relied on personal savings to fund the great majority of equity. Other sources of equity capital, in order of importance, include the use of home equity (14.3 percent), other sources (10.2 percent), third party investment (8.1 percent), sale of personal asset (8.0 percent), life insurance (4.0 percent), and limited partnership (4.0 percent).

Table 1

Sources of Initial Equity and Debt Capital

Percent of Responses by Category

Source of Equity ($n = 49$)	Percent of Equity Funds		
	1-50	51-100	TOTAL
Personal Savings	20.4	53.0	73.4
Life Insurance	0.0	4.0	4.0
Home Equity	8.2	6.1	14.3
Issuance of Stock	0.0	0.0	0.0
Limited Partnership	2.0	2.0	4.0
Sale of Personal Asset	4.0	4.0	8.0
Third Party Investment	4.1	4.1	8.1
Other	6.1	4.1	10.2
Source of Debt ($n = 27$)	**Percent of Debt Capital**		
	1-50	51-100	TOTAL
Friend/Relative	0.0	11.1	11.1
Lending Institution	4.8	29.6	34.4
SBA Guaranteed	18.5	29.6	48.1
Issuance of Bond	0.0	0.0	0.0
Finance Company	3.7	7.4	11.1
Government Grant	3.7	11.1	14.8
Other	0.0	7.4	7.4

The relative importance of personal savings to finance initial operations was reported by Feldman, Koberg, and Dean (1991). However, relative use of personal savings to finance initial operations among minority small business owners is much higher than for small firms as reported by Van Auken and Carter (1989), but is much lower than reported by Van Auken, Gaskill, and Kao (forthcoming) among women small business owners. An additional difference is that minority small business owners placed a much greater reliance on the use of home equity loans than either small firms in general or women-owned small firms.

The distribution of debt is also shown in Table 1. SBA guaranteed loans (48.1 percent), loans from lending institutions (34.4 percent), and government grants (14.8 percent) were the most important sources of initial debt capital. Other sources included friends or relatives (11.1 percent), finance companies (11.1 percent), and other debt sources (7.4 percent). The importance of loans from lending institutions (including SBA guaranteed loans) is evident in that 82.5 percent of the firms obtained funds from these sources. The table also shows that loans from friends or relatives and "other" sources were used only when debt comprised the majority of initial capital. Difficulties associated with raising a high percent of debt relative to total initial capital may necessitate packaging borrowed capital from a variety of sources. Similar situations were also found for both small businesses in general (Van Auken & Carter, 1989) and for women-owned small firms (Van Auken, Gaskill, & Kao, forthcoming) as debt became a relatively more important source of borrowing.

Table 2 compares the percent of minority-owned, women-owned, and mixed-ownership firms using each source of capital. A larger percent of the minority-owned firms placed a greater reliance on personal savings than did the mixed ownership sample of small firms. However, a greater percent of women-owned firms used personal savings than did minority-owned firms. In addition, more of the minority-owned firms used home equity loans to finance initial operations than either the women-owned firms or the more general sample of small firms.

Table 2

Percent of Firms Using Various Sources of Initial Capital

Source	Minority Owned (%)	Women Owned (%)[1]	Mixed Ownership (%)[2]
Equity			
Personal Savings	73.4	85.2	54.8
Life Insurance	4.0	3.0	8.4
Home Equity	14.3	7.0	4.8
Stock	0.0	2.0	8.4
Limited Partnership	4.0	2.0	1.2
Sale of Personal Asset	8.0	9.0	7.2
Third Party Investment	8.1	5.0	10.8
Other	10.2	7.0	4.8
Debt			
Friend/Relative	10.1	47.2	16.9
Lending Institution	34.4	55.6	63.9
SBA Guaranteed	48.1	5.6	7.8
Bond	0.0	0.0	2.6
Finance Company	11.1	0.0	2.6
Government Grant	14.8	0.0	0.0
Other Debt	7.4	11.2	6.5

[1] Van Auken, H., Gaskill, L., & Kao, S. (in press). Acquisition of capital by women entrepreneurs: Patterns of initial and refinancing capitalization. *Journal of Small Business and Entrepreneurship*.

[2] Van Auken, H., & Carter, R. (1989). Acquisition of capital by small business. *Journal of Small Business Management*, 29, 1-9.

A small percent of the minority-owned firms relied on loans from friends and lending institutions than did women-owned or the mixed ownership sample of small firms. In contrast, a much greater percent of the minority-owned small business owners used SBA guaranteed loans,

borrowing from finance companies and government grants than reported for the other categories of small firms in Table 2. Women-owned and mixed-ownership small firms reported very little use of these types of initial debt financing.

Bates (1991) suggested that the difficulty of obtaining loans from commercial banks has resulted in small use of debt in the capital structure of black small business owners. The results in Table 2 suggest that the commercial banks rely on the SBA guarantee to cover the "discriminatory risk" noted by Bates. This is especially evident in that no source of borrowing is a high percent of total initial debt funds. The minority small business owners apparently must rely on various sources of debt financing, perhaps even "piecing together" a debt financing package to complement personal savings. Such a composition of capital structure was not evident in previous studies of small firm financing.

Approximately 55.6 percent of the firms using debt to finance initial operations were "other" firms, 25.9 percent were service firms, and 18.5 percent were retail firms. Table 3 shows the lending requirements (collateral, business plan, financial projection, market study, professional advice, co-signer, other) associated with this debt relative to type of firm. Only the firms using debt to finance their initial operations are included in the table results. The chi-squared statistic, which tests for significant differences by type of firm, shows no differences in borrowing requirements by type of firm. Approximately 61 percent of the minority-owned firms had collateral requirements of 0-50 percent and about 39 percent had collateral requirements in excess of 50 percent of the loan value. Van Auken and Carter (1989) reported a larger percent of firms with less collateral requirements and a greater percent of firms with more collateral requirements. In contrast, women business owners had a much less collateral requirement in all categories (Van Auken, Gaskill, & Kao, forthcoming).

Table 3

Type of Business by Debt and Debt Requirements
Percent of Respondents by Category

Variable		N	Type of Business			
			Retail	Service	Other	Chi Squared[1]
Collateral (% of Debt)	0-50%	10	25.0	12.5	62.5	
	>50%	16	10.0	40.0	50.0	2.903
Business Plan	Yes	20	25.0	25.0	50.0	
	No	4	0.0	0.0	10.0	1.750
Financial Projections	Yes	20	23.5	23.5	53.0	
	No	8	16.7	16.7	66.7	1.400
Market Study	Yes	16	25.0	25.0	50.0	
	No	12	25.0	25.0	50.0	0.000
Professional Advice	Yes	14	35.0	8.3	66.7	
	No	14	18.2	36.4	45.5	4.857
Co-Signer	Yes	5	0.0	20.0	80.0	
	No	23	27.8	27.8	44.4	2.678
Other	Yes	4	0.0	0.0	0.0	
	No	24	25.0	25.0	50.0	1.750

[1] Adjusted for small sample size.

The majority of the minority business owners were required to provide business plans (85.7 percent) and financial projections (71.4 percent). A market study was required by 57.1 percent, and one-half of the firms were required to obtain professional advice. Only a small percentage of the firms were required to have a co-signer (17.9 percent) or meet other (14.3 percent) requirements.

Table 4 compares the lending requirements of the minority-owned firms with those reported for women-owned and mixed-ownership firms. The table shows that a greater percentage of minority-owned firms (except the co-signer and "other" category) reported collateral and other lending requirements than for either of the other categories of firms. The differences in the percentage of minority-owned firms versus women-owned and mixed-ownership who were required to provide financial projections, market study and professional advice are dramatic. These differences are supportive of the findings by Bates (1991) that minority-owned firms experience discrimination when borrowing capital. However, these results may also be a result of stringent SBA lending requirements.

Table 4

Borrowing Requirements: Percent of Firms by Ownership Category

Borrowing Requirement	Minority Owned	Women Owned[1]	Mixed Ownership[2]
Collateral	65.4	44.4	60.0
Business Plan	87.0	38.9	49.2
Financial Projections	73.9	36.1	45.2
Market Study	60.9	5.6	12.7
Professional Advice	52.1	13.9	20.6
Co-Signer	21.7	25.0	3/4
Other	13.0	30.6	25.4

[1] Van Auken, H., Gaskill, L., & Kao, S. (in press). Acquisition of capital by women entrepreneurs: Patterns of initial and refinancing capitalization. *Journal of Small Business and Entrepreneurship.*

[2] Van Auken, H., & Carter, R. (1989). Acquisition of capital by small business. *Journal of Small Business Management,* 29, 1-9.

Table 5 shows the lending requirements as compared to the percent of debt in the firms' initial capital structure and the relative chi-square statistic. The chi-squared statistic indicated that there was no statistical difference in the percentage of firms that were required to provide the lending requirements relative to the percentage of debt in the initial capital structure.

The results indicated that the majority of the firms were required to have collateral levels of more than 50 percent of their borrowed capital. In addition, a large majority of the firms were required to submit business plans, financial projections, and market studies. A lower percentage of the firms were required to obtain professional advice, while a minority of the firms were required to obtain a co-signer or other requirement.

Traditional finance theory emphasizes that the firm's financial risk increases as the percent of their debt relative to total capital increases (Brigham & Gapenski, 1993). As a consequence of this increasing financial risk, firms would be expected to meet more requirements prior to receiving a loan. The results in Table 5 confirm this expectation. As the level of debt relative to initial capital increases, a larger percentage of firms were required to meet all of the specific lending requirements. Similar results were found for women small business owners and mixed ownership small firms.

Table 5

Debt Requirements by Percent Initial Debt

Percent of Respondents by Category and Chi-squared Statistic

Requirements		N	Percent Initial Debt		Chi Squared[1]
			1-50	51-100	
Collateral	0-50	6	50.0	50.0	
	51-100	20	65.0	35.0	0.439
Business Plan	Yes	20	30.0	70.0	
	No	3	0.0	100.0	1.218
Financial Projections	Yes	17	23.5	76.5	
	No	6	33.3	66.7	0.221
Market Study	Yes	14	28.6	71.4	
	No	9	22.2	77.8	0.115
Professional Advice	Yes	12	33.3	66.7	
	No	11	18.2	81.8	0.683
Co-Signer	Yes	5	0.0	100.0	
	No	18	33.3	66.7	2.255
Other	Yes	3	0.0	100.0	
	No	20	30.0	70.0	1.218

[1] Adjusted for small sample size.

A comparison of these lending requirements relative to initial debt levels (as a percentage of total initial capital) for minority-owned and mixed-ownership categories of small firms is shown in Table 6. A greater percentage of minority firms is shown to have larger collateral requirements than for women and mixed ownership groups; however the differences in collateral requirements become small at higher debt levels.

Table 6 also shows that the percentage of minority-owned firms having business plan, financial projection, and market study requirements is much higher than for women-owned and mixed ownership firms regardless of the amount of debt in the initial capital structure. However, a lower percentage of the minority-owned firms had co-signer and other requirements than either the women-owned or mixed-ownership groups.

Table 6

Debt Requirements by Percent Initial Debt

Comparison by Type of Ownership

Requirements		Minority Owned (%)		Women Owned (%)[1]		Mixed Ownership (%)[2]	
		1-50	51-100	1-50	51-100	1-50	51-100
Collateral	0	3.8	30.8	13.9	41.7	11.3	29.0
	1-100	7.7	34.6	13.9	11.1	11.3	48.4
	>100	16.5	11.5	2.7	16.7	.8	.8
Business Plan		26.1	61.9	16.7	22.2	9.5	40.0
Financial Projections		17.4	78.3	13.9	19.4	8.1	37.1
Market Study		17.4	43.4	0.0	5.6	1.6	6.3
Professional Advice		17.4	34.8	5.6	8.3	6.3	14.3
Co-Signer		0.0	21.7	2.7	22.2	3/4	3/4
Other		0.0	13.0	8.3	22.2	6.3	19.0

[1] Van Auken, H., Gaskill, L., & Kao, S. (in press). Acquisition of capital by women entrepreneurs: Patterns of initial and refinancing capitalization. *Journal of Small Business and Entrepreneurship.*

[2] Van Auken, H., & Carter, R. (1989). Acquisition of capital by small business. *Journal of Small Business Management,* 29, 1-9.

Firms using debt as part of their start-up capital were divided into those launched before 1987 (n = 14) and 1987 to present (n = 12). This date was chosen since approximately one-half of the firms were in each age category. Table 7 shows the percentage of firms in each age category that were required to meet each lending requirement prior to receiving a loan and the respective chi-square statistic. The results showed that a significantly greater percentage of firms 1987 to present were required to provide business plans, financial projections, and market studies relative to firms launched before 1987. No significant difference was found between the percentages of firms that were required to have a co-signer, professional opinion, or other requirements. The results in Table 7 may be supportive of the increasing reluctance of lending institutions to extend loans to minorities that has been cited by Bates (1991). However, these results may also be reflective of greater caution and/or sophistication of lending institutions in the screening of loan applications to all applicants.

Table 7

Comparison of Lending Requirements between Firms Launched before 1987 and Firms Launched 1987 to Present

Percent of Firms and Chi-Square Test of Significance

Borrowing Requirement		N	Launched before 1987	Launched 1987-Present	Chi Squared[1]
Business Plan	Yes	20	40.0	60.0	3.760**
	No	3	100.0	0.0	
Financial Projections	Yes	17	29.4	70.6	8.856*
	No	6	100.0	0.0	
Market Study	Yes	14	21.4	78.6	9.991*
	No	9	88.9	11.6	
Co-Signer	Yes	5	20.0	80.0	1.982
	No	18	55.6	44.4	
Professional Opinion	Yes	12	50.0	50.0	0.048
	No	11	45.5	54.5	
Other	Yes	3	33.3	66.7	0.2980
	No	20	50.0	50.0	

[1] Adjusted for small sample size.
*Significant at 1%.
**Significant at 5%.

Sources of Additional Financing

New financing may be acquired to meet either short-term, seasonal, or expansionary needs. Growing firms who are unable to fund capital requirements using internal sources must rely on external financing. Firms that have been relatively low risk may become high risk due to greater financial obligations and a higher breakeven point as a result of obtaining the external capital.

Approximately 32.8 percent of the minority business owners acquired additional long-term capital after their first year in operation. The average financing mix of this newly acquired long-term capital was 54.3 percent equity and 46.7 percent debt. The majority of the equity capital (61.6 percent) was obtained from personal savings. Lending institutions provided 72.8 percent and friends or relatives provided 27.2 percent of the new debt capital. These results are similar to both women-owned and mixed ownership small firms.

The survey also collected information concerning the use of seasonal financing by the minority business owner. Seasonal financing is an important source of capital for firms whose sales are cyclical during the year. Approximately 35.8 percent of the respondents acquired seasonal financing. Of those using seasonal financing, 76.4 percent repaid the seasonal loan at maturity. Of those who refinanced their seasonal loans, only 10.4 percent refinanced the original note plus additional operating capital. These results are similar to the seasonal financing patterns for women-owned and mixed ownership small firms.

Difficulty of Obtaining Initial Capital

The questionnaire asked the minority business owners to rank how difficult it was to acquire the capital needed to begin operations. Respondents were given a Likert-type scale to rank the difficulty of obtaining start-up capital, with 1 = very difficult and 5 = not difficult. The average ranking of 2.7 indicated that the respondents believed it was somewhat difficult to raise their start-up capital.

The degree of difficulty in raising start-up capital is likely related to characteristics of the firm and its financing characteristics. The minority small business owners' rankings for the difficulty of raising capital were correlated with the type of firm, market served, and type of ownership. No significant relationships were found. The rankings were also correlated with the amount of total capital required to start the business, the level of debt relative to total capital, and composition of start-up capital. No significant relationships were found.

The lack of significant relationships between the difficulty of obtaining initial capital and both firm and financial characteristics indicates that these factors may not be important constraints to the minority business owners obtaining the required start-up capital. These results may be misleading, however. Those minority business owners who experienced great difficulty in obtaining their start-up capital may not have initiated operations. In addition, the sample is necessarily limited to firms still in operation. Firms experiencing difficulty in obtaining initial capital may have started operations undercapitalized and, resultingly, experienced financial distress leading to discontinuance. These types of firms would not have been included in the sample.

The respondents were also asked to rank (1 = to a large extent, and 5 = not a factor) the extent that the lack of capital has affected the operation of their business. The average ranking was 2.0. These rankings were correlated with the rankings on the difficulty of obtaining initial capital. The correlation coefficient of 0.466 between the two rankings was significant at the one percent level. This significant and positive correlation coefficient suggests that those firms experiencing difficulty in obtaining initial capital have experienced continuing financial difficulties in their operations.

SUMMARY AND IMPLICATIONS

This study examined the start-up financing characteristics of minority-owned small firms. As with other categories of small firms, minority small businesses were found to depend on a variety of sources to finance initial operations. The results showed that the minority small business owners placed a relatively high reliance on equity to finance initial operations. The primary source of start-up equity was personal savings, although other equity sources also played an important role. SBA guaranteed loans and loans from lending institutions were the primary source of initial debt financing. Government grants and loans from friends or relatives were also important.

Previous studies have found that the financial characteristics are important factors affecting the success of small firms (Gilbert, Krishnagopal, & Schwartz, 1990; Laitinen, 1991; Thomas & Evanson, 1987). Lack and inappropriate composition of initial capital often leads to financial distress and failure or discontinuance. The limited access of small firms to the financial markets

contributes to their difficulty of obtaining start-up capital. The problem associated with small firms being undercapitalized and using an inappropriate composition of start-up capital is a consequence of the difficulty of raising their initial capital. A better understanding of the alternative sources and associated difficulties can enable small firms to develop better strategies to raise sufficient levels and appropriate combinations of their initial capital.

The results have important implications for minority small business owners seeking initial capital. Minority business owners must assemble a package of alternative sources of capital to fund initial operations. Equity capital, especially personal savings, is the most important component of initial capital. Lending institutions, through direct and SBA guaranteed loans, and loans from friends or relatives are an important source of debt capital. In addition, minority small business owners have shown success in obtaining government grants.

The results also demonstrate that minority business owners should be prepared to provide more documentation than other types of business owners to obtain initial debt. Supporting documentation requirements have increased for the firms launched more recently. Planning and organizing the financial arrangements is a critical step in the successful acquisition of initial capital. The discrimination experienced by minority small business borrowers as discussed by Bates (1991), coupled with the necessity of assembling a package of initial capital and more numerous borrowing requirements, underscores the importance of prior planning and organizing.

Interpretation of the results may be limited by the geographical scope of the study. The results can likely be generalized to experiences of other minorities in the Midwest. Minority small business owners in other geographical areas within the United States may have different experiences. While the specific results may differ by geographical area, the general results, such as heavy reliance of personal savings, lending institutions, SBA guaranteed loans, numerous borrowing requirements, etc., is most likely experienced by minority business owners in numerous locations throughout the United States.

These limitations provide the opportunity for greater research into the financing of minority-owned firms. A national study that identified the financial composition, sources and constraints of minority business owners in raising initial capital would provide a much better understanding of the capitalization of minority-owned firms. A better understanding of these issues would enable potential minority small business owners to develop strategies in raising start-up capital and consultants to be better prepared in assisting prospective and current minority small business owners. A better understanding of the limitations and constraints in raising initial capital would enable government policy makers to develop better programs to assist minority small business.

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