African Journal of Business Management Vol.5 (10), pp. 3781-3793, 18 May 2011
Available online at http://www.academicjournals.org/AJBM
DOI: 10.5897/AJBM09.285
ISSN 1993-8233 ©2011 Academic Journals

Full Length Research Paper

Financial management practices of small firms in Ghana: An empirical study

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Accepted 29 December, 2010

The contribution of small firms to the employment of the youth in Ghana is highly recognised, but their contribution towards revenue to the national budget seems to be negligible. The reason for this situation is that these small firms do not have sound financial management systems in place which will help them to prepare financial reports. The end result is that it becomes very difficult for tax authorities to compute their taxable incomes. The three most influential factors that did motivate the sample firms in pursuing sound financial management practices were: (1) Pressure from bankers (90%); (2) Pressure from external accountants (80%) (3); Pressure from providers of capital (70%). The three most influential factors that prevent them from practicing sound financial management practices were: (1) Qualified accountants too expensive to maintain (93%); (2) Accounting records too difficult to understand (87%); (3) Lack of internal accounting staff (73%). In the light of the findings of the study, it has been recommended among other things that, they should avoid mixing business transactions with non-business transactions. It was also recommended that small firms should disclose fully the financial position by keeping full set of information on business transactions.

Key words: Financial management practices, small firms, Ghana.

INTRODUCTION

The study is about how financial decisions are taken in the small firms, to identify the factors that promote or inhibit the application of sound financial management practices, the problems they face with regards to taking financial decisions and how to help them improve on their businesses.

There appears to be little doubt that small businesses do make a large net contribution to the creation of new jobs compared with large businesses (Birch, 1979). Small firms have played great roles in the development of various economies of the world. They are recognized and acknowledged worldwide as vital and significant contributors to economic development, job creation, and the general health and welfare of economies, both nationally and internationally.

Financial management involves a wide spectrum of a company's financial decisions (Parkinson and Ogilvie, 1999). It covers areas such as:

a) Determining the source of finance and dividend policy.
b) Investment decisions including capital budgeting. assessing capital risk and cost of capital.
c) Working capital management.
d) Managing interest rate and exchange rate risks.

Small firms who will form part of the study do not pay dividends and do not have the capacity to manage interest rate and exchange risks. In view of this the literature reviewed were those that concentrate on capital budgeting and working capital management practices in small firms.

Small businesses defy specific definition hence; there is no generally accepted definition. Over the years there have been many attempts at defining what constitutes a small business. Researchers and policy makers, looking for an objective definition of small business, have used a variety of criteria including: total worth; relative size within industry; number of employees; value of products; annual sales or receipts; and net worth Cochran (1981). However, the benchmarks vary considerably. Distinguishing variables include, total assets, total employees, volume and value of turnover. The 1985 U.K. Companies Act defined "small company" in respect of financial disclosure as companies employing 50 or less employees, turnover not greater than £2.8 million and balance sheet total not greater than £1.4 million. Based on an agency

perspective, Ang (1991) suggested that it may be appropriate to define a business as small if it possesses most of the following characteristics: it has no publicly-traded securities; the owners have undiversified personal portfolios; limited liability is absent or ineffective; first-generation owners are entrepreneurial and prone to risk-taking; the management team is not complete; the business experiences the high cost of market and institutional imperfections; relationships with stakeholders are less formal; and it has a high degree of flexibility in designing compensation schemes.

A similar view was taken by Osteryoung and Newman (1993), who suggested that a small business be defined as a business in which there is no public negotiability of common stock and the owners must personally guarantee any existing or any planned financing.

The ultimate success of a firm's operations depends upon sound capital budgeting decision. Entrepreneurs invest money in their businesses for a reason. The reason, generally, is to receive a return on their precious resources. To test the link between earnings performance and capital budgeting practices, Christy (1967) used growth of earnings per share as an indicator of performance, but could not establish a consistent relationship between earnings performance and capital budgeting practices.

There is little doubt that financial management systems continue to be of significance to business success. Prior research by Raymond and Magnenat-Thalman (1982), Holmes and Nicholls (1989), Nayak and Greenfield (1994) and Lybaert (1998) has asserted that the quality of management accounting information utilised within the small business sector has a positive relationship with an entity's performance. Despite the importance of financial Inadequate working capital decisions and accounting information have been referenced consistently as causes of small business failure. According to Barrow (2001), there is enough evidence which point to small firms being inefficient users of working capital. As he puts it, "the smaller they are, the less efficient they tend to be". Dodge et al. (1994) also reported that the most important internal problems identified by small US firms relate to inadequate capital, cash flow management and inventory control. In his often quoted research on small business failure and bankruptcy, Berryman (1983), has also indicated that 'poor' or 'careless' financial management is a major cause of small business failure.

Small business financial management practice is, as evidenced by the number of recent studies cited earlier on, is a growing area of research. However, the research conducted to date has been largely exploratory and descriptive in nature, tending to focus on small samples of businesses in a variety of industries and locations in advanced economies. Financial management systems have been analyzed for micro businesses of less than 10 employees (Nayak and Greenfield, 1994), of less than 20 employees (Holmes and Nicholls, 1989; Mitchell et al., 1999), focused their attentions on new small businesses. Though new businesses, with their inherent risk and vulnerability, justify separate study, there is a need also not to ignore established businesses. Peel and Wilson (1996) considered small firms within the classification to be used in this study, but were restricted to only 82 respondents to their questionnaire.

There is currently less theoretical literature pertaining to the capital budgeting decisions of small firms than there is empirical research. Keasey and Watson (1993), however, have hypothesized that the factors which influence capital budgeting decisions differ significantly in relation to small and large firms.

In view of their greater economic significance in relative terms, the capital budgeting practices of small businesses in North America received considerable early attention from researchers like (Soldofsky, 1964; Luoma, 1967; Scott et al., 1982, Grablowsky and Burns, 1980). These results underscore the importance of the payback period, and informal criteria in the evaluation of capital expenditures by small businesses. It is also noteworthy that Soldofsky (1964) found there was considerable variation in the method of calculation and use of formal criteria among his survey respondents.

There is little doubt that financial management systems continue to be of significance to business success. Research has pointed to the relative volatility of the small business when compared with larger entities, due to volatile cash and profit positions, a reliance on short term debt funding and poorer liquidity (Walker and Petty, 1978). Financial management is critical, especially in relation to working capital and over-trading, due to the lack of medium and long-term finance available to small businesses and the reliance on short term debt funding (McMahon and Holmes, 1991; Dodge et al., 1994).

The danger of business failure due to lack of sound financial management practices is real. Gaskill, and Van Auken (1993) has reported that the most internal problems identified by small US firms relate to inadequate capital, cash flow management and inventory control. Berryman, (1983) indicated that 'poor' or 'careless' financial management is a major cause of small business failure. In addition, a major survey by the Insolvency Practitioner Society, (CIMA, 1994) indicated that 20% of UK corporate failures (the vast majority of which are small firms) were due to bad debts or poor credit management.

Despite the importance of working capital management to the small firms, it is perhaps surprising that no previous research has been conducted on the working capital management practices of small firms in the Ashanti Region of Ghana.

Furthermore, although, research has been conducted on the capital budgeting techniques used by large, medium, and small sized companies as cited by Sangster (1993), Louma (1967), Grablowsky and Burns (1980), Peel and Wilson (1986), no previous research has focused on this aspect of financial management in respect of small firms in a developing country setting.

Table 1.Size Characteristics (Number of employees).

Number of employees	Number of firms	Percentage (%)
1 - 5	16	64
6- 10	4	16
11- 15	5	20
Total	25	100

The aim of this study is to understand how working capital and capital budgeting decisions are made in the small firms and to identify the problems they face with regards to taking such decisions and how to help them improve on their businesses. The specific matters that will be studied are:

1. Accounting Systems--types of systems in use, the extent of computer utilization and applications.
2. Financial Reports--utilization of financial statements and associated information to facilitate managerial decisions, types of financial statements in use, techniques of financial analysis used.
3. Working Capital Management--techniques in use for the management of cash, accounts receivable, inventory, and accounts payable, useful quantitative management models, computer-based working capital management systems.
4. Fixed Asset Management--techniques in use for the evaluation of capital expenditure projects, administrative procedures for capital budgeting, post-acquisition management of fixed assets.

METHODOLOGY

The mixed-method strategy was adopted for this study to reduce the possibility of personal bias by not depending on only one method of approach or response coming from one or few firms.

A mixed-method strategy is one in which more than one method of approach is used in data collection and analysis while conducting research. This approach is similar to what Denzin, (1978) described as triangulation.

Semi-structured interview based on open-ended, flexible questionnaires and some structured interviews will be conducted with several groups of people interested or involved with the small business sector in Ashanti Region. The idea behind this is to obtain cross-referencing data and some independent confirmation of data, as well as a range of opinions. Inputs from the following groups were solicited: (1) Managers of small scale businesses; (2) Representatives of banks who give loans to small-scale businesses; and (3) Accountancy firms who have been auditing the accounts of small scale businesses.

There are about 3,000 retail firms, employing 20 or less employees in the Ashanti Region of Ghana. Considering the topic for the study, all the 3,000 firms constitute the population for the study.

Much as the researcher would have liked to work with the entire population, he was prevented from doing so as that would have been too difficult to handle effectively considering the fact that this is an exploratory study. As a result 80 firms selling general goods like, clothing, electrical and plumbing materials were selected to serve as the sample population. The sample was selected from small retailers in the following towns in Ashanti Region: 30 from Kumasi, 10 from Bekwai, 10 from Mampong, 10 from Konongo, and 20 from Obuasi.

Ghana is divided into ten administrative regions. The Ashanti region, with Kumasi as its capital lies approximately at the centre of the country. It covers an area of 24,390 km^2 representing 10.2% of the land area of Ghana. Even though majority of the people working in the informal sector are farmers, a large proportion of them are engage in small scale trading. These traders form the nucleus of the local entrepreneurs.

These traders were selected as they form the majority of small firms operating in the Region. Most of the small shop owners started from humble beginnings with capital less than ¢100,000 as 'shoe shine' boys and 'table top' traders. As their capital levels improved they acquired bigger shops to operate their businesses.

The validity and reliability of any research data depend to a large extent on the source and technique used in collecting the data. A questionnaire eliciting details on, inter alia, capital budgeting and working capital practices were mailed to the owner/managers of 80 firms selected randomly. The accompanying letter asked for comments on the questionnaire and requested an interview or telephone conversation.

Since most of the respondents did not have finance background the researcher had to explain most of the technical terms to help in obtaining the appropriate responses. To prevent a situation whereby some of the respondents will try to hide information the researcher visited each to examine some of the documents requested for. Documents like profit and loss accounts, balance sheets, cash flow statements and business plans were examined. During the visits to the respondents, opportunity was taken to observe how things were done in the various shops. Telephone conversations and interviews were held with Chartered Accountants and officials from the National Board for Small Scale Industries and bank officials to collaborate the responses. These interviews ensured the establishment of rapport and permitted greater depth and probing of some personal views. This helped in obtaining more complete data. The data were gathered during the period 13th March to 29th May 2006. On the average each interview lasted 2 h.

The information obtained was initially coded into definite categories, sorted and tallied manually. All subsequent computations were also done manually. In scoring responses which form the next chapter, the researcher made tables and indicated in the various results offered by the respondents. Each table is followed by some interpretations and comments. Out of the 80 sample firms, 28 responded to the questionnaire, giving a response rate of 35%. However, given the nature of small firms and the low response usually associated with most mail surveys, this response rate may be considered reasonably adequate for an exploratory study. Three of the responses received were not usable due to incomplete data. The rest of the responses from 25 firms were used in this study. The main findings of this study are presented in the form of two-way tables. Each of these tables is followed by some comments.

Table 1 Reports the size distribution of the sample responding firms in terms of the number of employees. Five firms had between11 and 15 employees. None of them had more than 15

Table 2. Firms' objectives.

Objectives	Frequency	Percentage (%)
Increasing profitability	25	100
Increasing sales growth	17	68
Providing service	11	44
Providing employment	20	80

Table 3. Incorporation of companies.

Number of years	Number of firms	Percentage (%)
Less than one year	3	12
1 - 5	10	40
6 - 10	8	32
11 - 15	4	16
Total	25	100

Table 4. Number of employees at the finance department.

Number of employees	Number of firms	Percentage (%)
1	18	72
2	7	28
Total	25	100

employees. Thus, the study's definition of small firm being those that employ less than 20 employees was achieved.

It is interesting to note that none of the employees of the respondent firms were given appointment letters before they started working in their various firms. As most of the employees are family members, in majority of cases, husband and wife, they did not pay themselves salaries. They do not enjoy any predetermined leave periods as they go on leave as and when they so desires.

The table reports responses to a question which sought to establish the key objectives which the small firms were pursuing. Respondents were requested to indicate how important they considered a range of objectives were to their firms. The responses revealed that all the firms (100%) were pursing the objective of "increasing profitability".

The study found that 48% of the firms have been in existence between six and fifteen years.

Most small firms collapse within the first five years of incorporation. Thus it is significant to note that 48% of respondent firms have existed over more than five years. Potts, (1977) noted that, "in 1973 of all failing concerns in the United States had been in operation five years or less". Table 4 show that majority of respondents, 72% have only one employee in charge of the finance department and none of them had more than 2 employees. All the employees were family members.

In an attempt to learn about respondents' level of knowledge in finance and accounting, they were asked to state the educational level of employees in charge of their finances. Table 5 shows that majority 84% had completed either secondary school form five or commercial school. Thus they have some knowledge of accounting and finance.

Table 6 show that 40% of the owner/managers of the respondents have no forma l education. The same percentage (40%) of respondents is university graduates.

The importance of analyzing past corporate financial statement in the investment decision-making process cannot be over-emphasized. A financial statement highlights the previous financial performance of a business and gives a broader picture of the financial capability of the borrower and the manner the business' finances have been managed.

Even though all the respondents stated that they have employed internal accounting staff 60% do not prepare management accounts at the end of the month.

All the ten firms, excluding the model firm DOY Enterprise Limited, who stated that they prepare monthly management accounts, which comprise of Trading/Manufacturing accounts, profit and loss accounts, fifty per cent, do not prepare balance sheets. Balance sheets help spot potential problems before becoming severed and the non preparation of balance sheets at the end of the month is not a good practice.

None of the respondents have ever used computers to prepare their accounts. To be able to know why the respondents prepare management accounts, they were asked to state the factors that influence they decisions. Out of the ten firms who prepare management accounts the evidence in Table 11 shows that the principal influences were:

1. Pressure from bankers (90%)
2. Pressure from external accountants/auditors (80%)
3. Pressure from providers of capital (70%):

Evidence from the study shows that the principal reasons why those firms (60%), who do not prepare any management accounts were:

Table 5. Educational backgrounds of head of finance

Level of education	Number of firms	Percentage (%)
Commercial school	12	48
Secondary form 5	9	36
Sixth form	1	4
Teachers' certificate	3	12
Total	25	100

Table 6. Educational background of owner/manager.

Level of education	Number of firms	Percentage (%)
No formal education	10	40
Middle school form 4	7	28
Commercial school	3	12
Secondary school form 5	2	8
Teacher training	1	4
University/professional	2	8
Total	25	100

Table 7. Do you prepare monthly management accounts?

Response	Number of firms	Percentage (%)
YES	10	40
NO	15	60

Table 8. Monthly management accounts.

Type of accounts	Number of firms	Percentage (%)
Trading / manufacturing accounts	10	100
Profit and loss account	10	100
Balance sheet	5	50

1. Qualified accountants too expensive to maintain (93%). To these respondents they are scared by the consultancy fees qualified accountants charge their clients. The qualified accountants also complain that these small firms have poor payment culture despite the fact that they spend a lot of time when it comes to the auditing of small companies.
2. Accounting records too difficult to understand (87%). The lack of accounting knowledge on the part of owner/managers account for this situation.
3. Lack of internal accounting staff (73%). The inability of these small firms to pay good salaries to their employees makes it very difficult to attract qualified accounting staff.

The lack of internal accounting staff as an inhibiting factor for the practice of sound financial management system collaborates with the findings of Stuart McChlery et al. (2004).

From Table 12, 47% of the respondents stated that they do not prepare monthly management accounts because they want to avoid paying taxes.

A section of the questionnaire was devoted to ascertain the working capital practices of surveyed firms. Respondents were requested to indicate (on a scale 1=never used/review; to 5= use/review very often) the frequency with which they used / reviewed various methods pertaining to the management of working capital.

Turning to the capital budgeting techniques used by the firms in the study, the study found that the proportion of firms using the various techniques. Only 9 firms (36%) of respondents indicated that they have ever used the pay back method. The other capital budgeting techniques; Accounting rate of return (ARR), Discounted cash flow [including Net present value(NPV), and Internal rate of return (IRR)], none of the respondents have ever used them.

As a result of the above revelation the question, 'state the interest rate used in the discounted cash flow became irrelevant.

Firms using the pay back technique were requested in the questionnaire to answer the following question; 'on the average over how many years are project returns evaluated?' Sixty six per cent of the respondent firms evaluated their project returns between one and two years.

The results of the capital budgeting practices in this study differ significantly from similar studies conducted on US small firms. Whereas small firms studied in the US by Luoma (1967) and

Table 9. Factors influencing the preparation of monthly management accounts.

Influential factors	Frequency	Percentage (%)
Qualified internal accounting staff	3	30
Pressure from bankers	9	90
Pressure from external auditor/accountant	8	80
Pressure from providers of finance	7	70
The importance of accounting records for a firm	5	50

Table 10. Factors inhibiting the preparation of monthly management accounts.

Inhibiting factors	Frequency	Percentage (%)
Lack of internal accounting staff	11	73
Accounting reports too difficult to understand	13	87
Qualified accountants too expensive to maintain	14	93
The business is too small	11	73
Accounting reports do not add any value to the business	7	47
To avoid paying taxes	7	47

Table 11. Working capital management techniques; frequency of usage.

Score	Never (%)	Sometimes (%)	Quite often (%)	Often (%)	Very often (%)	Number of firms
Cash budgeting (use)	10	13	14	30	33	25
Debtors' credit period (review)	36	24	22	10	8	20
Debtors' discount policy (review)	40	22.5	13.8	23.8	10	24
Bad debts (review)	78	4.9	8.5	4.9	3.7	25
Doubtful Debts (review)	78	4.9	8.5	4.9	3.7	25
Customer credit/risk standing (review)	35	10	18	23	14	25
Factoring (use)	98	2	0	0	0	25
Stock turnover (review)	30	23.8	22.5	13.8	10	25
Stock levels (review)	70	5.6	11.4	9.5	3.5	25
Stock reorder levels (review)	60	30	10	0	0	25
Economic order quantity model (use)	80	12	4	2	2	25

Table 12. Use of capital budgeting techniques

Technique	Number of firms	Percentage (%)
Pay back	9	36
Accounting rate of return (arr)	0	0
Discounted cash flow (npv / irr)	0	0

Table 13. Number of year's project returns evaluated.

Number of years	Number of firms	Percentage (%)
Less than 1	0	0
One	4	44
Two	2	22
Three	3	33
Four	1	11
Total	9	100

Table 14. Comparison of the use of capital budgeting techniques (Using percentage).

Researcher/ Technique	Luoma (1967)	Grablowsky and burns (1980)	Current study (2006)
Pay back	63%	Not ascertained	36%
Accounting rate of return	30%	12.3%	Not in use
Discounted cash flow	22.2%	13.8%	Not in use

Table 15. Sources of finance for most recent capital investment projects and working capital needs.

Sources of finance	Number of firms	Percentage (%)
Retained earnings	7	28
Bank loans	9	36
Loans from friends	8	32
New equity from family members	1	4
Total	25	100

Grablowsky and Burns (1980) have been using accounting rate of return and the discounted cash flow techniques in evaluating capital projects, their counterpart in Ghana, do not use any of these techniques.

The study found that 68% of respondents financed recent capital investment projects using loans from banks and friends.

With the recent high interest rates being charged by the banks it will be in the small firm's own interest if they can finance capital projects from retained earnings. Table 17 shows that 36% of the respondents raised funds from friends and family members.

Given the heavy reliance of small firms on bank finance, as shown above, and the recent criticism of the Ghanaian banking sector for not passing on reductions in the inter-bank prime rates by the Bank of Ghana, to the small firms, a section of the questionnaire was devoted to examining aspects of the relationship between the small firms and their bankers.

The study found that majority of the respondent firms, 72% answered that their bankers have acted fairly by passing on interest rate reductions to their businesses. Table 17 also shows that only 24% of the respondents stated that they were considering changing their bankers. Hence, overall, the responses reported in Table 16, indicate that a majority of respondents appeared to have a satisfactory relationship with their bankers.

RESULTS

The majority of employees of the firms studied are family members. They were not recruited through the normal process hence they were not offered any written contract of employment. The owner/managers did not receive salaries at the end of the month as they do not classify themselves as employees.

With the recent high interest rates being charged by the banks it will be in the small firm's own interest if they can finance capital projects from retained earnings. Despite these difficulties with bank credit 36% of the firms studied still go in for the loans as they have no other alternatives. The fact that 36% of the respondents raised funds from friends and family members confirms what Osei et al. (1993) found in their study under the title, "The impact of structural adjustment on SMEs in Ghana". Some complained bitterly that they expected their children who were supported to travel abroad for their education on completion will remit them to finance their capital projects but have refused to do so. Thus, only 4% of the respondents received support from the relations abroad.

Working capital management practices

Working capital is the capital available for conducting the day-to-day operations of an organisation. It is often defined simply as "current assets less current liabilities". Working capital is essential to a firm's long-term success and development, and the greater the degree to which the current assets cover the current liabilities, the more solvent the company.

Berryman, (1983) indicated that 'poor' or 'careless' financial management is a major cause of small business failure. In addition, a major survey by the Insolvency Practitioner Society, (CIMA 1994) indicated that 20% of UK corporate failures (the vast majority of which are small firms) were due to bad debts or poor credit management. According to Peel and Wilson (1994), "if the financial/working capital management practices in the small firm sector could be improved significantly, then fewer firms would fail and economic welfare would be increased substantially".

The control of working capital can be subdivided into areas dealing with stocks, debtors, creditors and cash. Considering the importance of efficient management of cash by small firms, it is not surprising that only 10% of respondents claimed that they never used cash budgeting, whereas 33% used cash budgeting 'very often'. Examination of the bank statements of the respondent firms revealed large credit balances at the end of the month.

This is a sign of inefficient cash management which

Table 16. Relationship with bankers.

	Yes, [number of firms(%)]	No, [number o firms (%)]
Has your bank been passing on interest rate reductions to your business?	18(72%)	7 (28%)
Are you considering changing bankers?	6(24%)	19(76%)

should be discouraged. Surplus cash which could have been invested in short term instruments like 'call accounts' which yield good returns are left in non interest yielding bank accounts. In Anvari and Gopal (1983)'s study, only 26% of the respondent to the survey said they used formal techniques to determine the level of their cash

In order to reduce the debtor days to a more respectable figure companies will offer customers inducements, in the form of cash discounts. These discounts may well speed up collection but reduce the amount from each sale when collected. Credit management thus, involves balancing the benefits to be gained from extending credit to customers against the costs of doing so, and finding the optimum level of credit and discounts which will maximize the firm's profits.

To have a good credit management a firm should assess the credit risk of its customers. This involves giving consideration to having a credit control policy and following the procedures. The study found that 64% of the firms reviewed their debtors' credit period with 8% reviewing it very often. However, a smaller proportion (60%) reviewed their debtors' discount policy, and only 10% reviewed it very often. Seventy-eight per cent (78%) claimed that they never reviewed bad and doubtful debts and only 35% of respondents claimed their firms never reviewed their customers' credit/risk standing. Bad debts can be major problem to small businesses, especially in the current economic climate where margins may already be squeezed and the high inflation rates may add salt to injury. Firms that provide most or all goods or services on credit to more or all of their customers are likely to experience bad debts situation on a large scale. Thus it is not unusual for a major customer's downfall to cause the insolvency of its suppliers by not paying outstanding debts.

The study found that a high proportion (98%) of firms stated that they had never used factoring services. This confirms the fact that, factoring is not popular in small firms. This is similar to what Grablowsky and Rowell (1980) found in their study conducted in Virginia. In that study only 30% of respondents used credit reporting services such as Dun and Bradstreet (1993). With reference to stock control, the study found that only 20% and 40% used the economic order quantity model and reviewed their reorder levels. In Grablowsky and Rowell (1980)'s study; only 6% used the economic order quantity for optimizing inventory. The study found that 68% of respondents financed recent capital investment projects using loans from banks and friends. Even though taking loans and overdrafts are accepted forms of corporate finance, too much reliance will greatly affect the survival of the small firms. The responses revealed that all the firms (100%) were pursing the objective of "increasing profitability". On the basis of these findings, smaller firms appear to be pursuing similar objectives to their larger counterparts. The theory of company finance is based on the assumption that the objective of a firm is to maximize the wealth of its owners.

Capital budgeting practices

Banks normally will finance projects with following characteristics:

i. Shorter pay back periods,
ii. Higher returns on capital employed
iii. A positive net present value (NPV), implying that future cash flows from the project under review, expressed in their present value terms using an appropriate interest rate was positive, implying profitability of the project under review.
iv. A positive internal rate of return (IRR) of the project, implying that the rate at which the project generates funds, relative to the cost of capital is positive.

Turning to the capital budgeting techniques used by the firms in the study, only 9 firms (36%) of respondents indicated that they have ever used the pay back method. The other capital budgeting techniques; Accounting rate of return (ARR), Discounted cash flow [including Net present value(NPV), and Internal rate of return (IRR)], none of the respondents have ever used them.

Factors promoting and inhibiting financial management practices

The importance of analyzing past corporate financial statement in the investment decision-making process cannot be over-emphasized. A financial statement highlights the previous financial performance of a business and gives a broader picture of the financial capability of the borrower and the manner the business' finances have been managed.

None of the respondents have ever used computers to

prepare their accounts. The availability of affordable computers and suitable software has played an important part in promoting the practice of sound financial management.

In a survey of 129 small manufacturing businesses in the province of Quebec, Raymond and Magnenat-Thalmann (1982) discovered a preponderance of accounting-related applications among computer software in use, particularly in the areas of accounts receivable, payroll, accounts payable, general ledger, sales analysis, and inventory.

Stuart McChlery et al. (2004)'s study also identified the use of computerized accounting system as a major factor in promoting sound financial management system. The firms that prepared monthly management accounts were motivated to do so due to the following factors:

1. Pressure from bankers (90%) It is interesting to note that the study revealed that most firms prepare financial statements when they have to support their loan applications with these statements.
2. Pressure from external accountants/auditors (80%): The external accountants are normally approached by these small firms to help prepare financial statements like, cash flow and income statements to help in the filing of their tax returns.
3. Pressure from providers of capital (70%): About 70% of the firms studied received financial support from their relations living outside the country and one of the conditions which they have to fulfill to be able to attract such support is to furnish these people their annual financial statements.

Even though all the respondents stated that they have employed internal accounting staff 60% do not prepare management accounts at the end of the month. The factors that inhibit the preparation of monthly management accounts were:

1. Qualified accountants too expensive to maintain (93%). To these respondents they are scared by the consultancy fees qualified accountants charge their clients. The qualified accountants also complain that these small firms have poor payment culture despite the fact that they spend a lot of time when it comes to the auditing of small companies.
2. Accounting records too difficult to understand (87%). The lack of accounting knowledge on the part of owner/managers account for this situation.
3. Lack of internal accounting staff (73%). The inability of these small firms to pay good salaries to their employees makes it very difficult to attract qualified accounting staff. The lack of internal accounting staff as an inhibiting factor for the practice of sound financial management system collaborates with the findings of Stuart McChlery et al. (2004).

From the discussions that the researcher had with stakeholders like, bank managers and chartered accountants based on the responses from the study, it came to light that accounting is generally not viewed as a core part of many businesses hence, these small firms tend not to employ qualified finance personnel. Most of these small firms assume they are saving money by employing cheap labour to carry out accounting functions.

The practicing accountants the researcher talked to also confirmed that most small firms come to them when they have to present financial statements and cash flow to their bankers to support their loan applications.

The hypothesis that; 'owner/managers of small firms who have good educational background tend to practice sound financial management as they appreciate its importance', has not been supported by evidence from the study. This is because all the owner/managers who were university graduates did not prepare any form of management accounts. Thus, there is no relationship between the educational background of owner/managers and the use of financial management practices.

Considering the importance of efficient management of cash by small firms, it is not surprising that only 10% of the respondents claimed they never used cash budgeting, where as 33% used cash budgeting 'very often'. However, most of them still keep large cash balances in their bank accounts which do not earn any interest.

Sixty four per cent of the firms reviewed their debtors' credit period with 8% reviewing it very often. However, a smaller proportion (60%) reviewed their debtor's discount policy and only 10% reviewed it very often.

The study revealed that the three most influential factors which compel the sample firms to pursue sound financial management practices were:

1. Pressure from bankers (90%) It is interesting to note that the study revealed that most firms prepare financial statements when they have to support their loan applications with these statements.
2. Pressure from external accountants/auditors (80%): The external accountants are normally approached by these small firms to help prepare financial statements like, cash flow and income statements to help in the filing of their tax returns.
3 Pressure from providers of capital (70%): About 70% of the firms studied received financial support from their relations living outside the country and one of the conditions which they have to fulfill to be able to attract such support is to furnish these people their annual financial statements.

The most influential factors that account for the inability of the sample firms to pursue sound financial management practices were:

a) Qualified accountants too expensive to maintain (93%). To these respondents they are scared by the

consultancy fees qualified accountants charge their clients. The qualified accountants also complain that these small firms have poor payment culture despite the fact that they spend a lot of time when it comes to the auditing of small companies.

b) Accounting records too difficult to understand (87%). The lack of accounting knowledge on the part of owner/managers account for this situation.

c) Lack of internal accounting staff (73%). The inability of these small firms to pay good salaries to their employees makes it very difficult to attract qualified accounting staff.

d) The business is too small (73%). Some owner/ managers feel it is only big firms that have to keep proper books of account and prepare financial statements regularly. This is an erroneous impression which should be discarded as the survival of their businesses depends on practicing sound financial management.

The study shows that 68% of the respondents financed recent capital projects from loans from banks and friends. This implies that these firms are not able to generate enough funds internally to finance capital projects. Some of them who were expecting support from their children working abroad were highly disappointed as these kids did not assist them.

The fact that 36% of the respondents raised funds from friends and family members confirms what Osei et al. (1993) found in their study under the title, “The impact of structural adjustment on SMEs in Ghana”.

Seventy-two per cent (72%) of the firms studied stated that their bankers have been fair in the last two years by passing on reductions in interest rates to their businesses. Seventy six percent (76%) also stated that they are satisfied with the services being provided by their bankers hence they do not have the intention of replacing them.

The popularity of payback as an investment evaluation method continues to grow, as is evidenced in this study, despite its known drawbacks. While academicians unanimously condemned the use of the pay back as misleading and worthless in reaching investment decisions, it continues to flourish as the most widely applied formal technique. The problem with the use of the pay back method as an investment evaluation method is that all cash flows with the payback period are given equal weight. Also cash flows outside the pay back period are ignored and it is very difficult to determine how long the pay back period should be. Only 9 firms (36%) of the respondents indicated that they have ever used the pay back method. These firms used the pay back method because the information presented to them is easy to understand.

The other capital budgeting techniques like Accounting rate of return, Discounting cash flow and internal rate of return have never been used by the firms studied. Thus, the findings of the study run contrary to earlier studies done in US by Luoma (1967) and Grablowsky and Burns (1980). In Luoma’s study 63% used the pay back method, 30% used the accounting rate of return and 22.2% used the discounted cash flow method.

The differences in the results may be due to cultural factors. This is because most owner/mangers of small businesses in the US are literate and thus understand the use of these capital budgeting techniques. The availability and use of qualified finance personnel in the developed economies contribute significantly to the use of these advanced capital budgeting techniques.

Unlike his counterpart in the advanced economies, the owner/managers of the small firms studied do not have access to qualified finance personnel as they cannot afford to pay them well. From the findings of the study enumerated above the following conclusions can be made.

Conclusion

In theory, the same general principles of financial management apply to small firms as they do to large firms. Small firms do not follow the right procedure when engaging their staff. All the firms studied even though have employed people they did not give them any appointment letters when they were first engaged. This practice runs contrary to the labour law and should be discouraged.

From the above findings it can be concluded that left on their own the owner/managers of the sample firms will not prepare any management accounts. For a profit making entity the main strategic objective is to maximize share holder wealth. This means achieving the maximum profit possible consistent with balancing the needs of the owners. The profits made by an entity can only be measured by preparing financial statements. Thus it will be very difficult for the owner/managers of the small firms studied to be able to compute their profits when they do not prepare financial statements.

Sound financial management is essential to the success of a business. Successfully managing financial resources is important in new as well as expanding businesses, so time should be taken to develop and implement financial plans that will ensure the success of small firms.

The action and inactions of owners of small firms could also act as significant barriers to the development of sound financial management systems. The lack of understanding of accounting information presented in the form difficult to understand could act as barriers in implementing sound financial systems. The findings of this study collaborates to a greater extent with the findings of previous research done in U.K. by the Chartered Institute of Management Accountants (CIMA), by revealing that there are factors which influence the small firms to either pursue sound financial management practices or do otherwise. The factors which apply in the

U.K. are different from those that apply to small firms in Ghana because small firms are much less likely to employ accountants it was not surprising to note that none of the respondents did ever us the more sophisticated capital budgeting techniques like discounted cash flow. It is not advisable to use the pay back on its own for investment appraisal and it should be combined with at least one other technique, preferably, based on discounted cash flow procedures, to ensure that all project returns are taken into account.

The inability of small firms to make use of Computerised accounting systems also act as a barrier to the successful implementation of sound financial management practices.

Recommendations

In the light of the above, the researcher would like to suggest to owner/managers that the careful management of working capital is vital for the survival of their firms. Poor management of working capital means that funds are unnecessarily tied up in idle assets hence reducing liquidity and also reducing the ability to invest in productive assets such as plant and machinery, so affecting profitability.

The owner/managers of small firms should do the following if they want to make better use of sound financial management practices:

1. Find out when your biggest customers have their monthly cheque run and make sure your bills reach them on time.
2. Send out statements promptly and chase up late payers and always follow up with phone calls.
3. Establish a credit control policy and follow the procedures established.

The following key elements should be taken into account in the formulation of the credit control policy:

i. The terms of trade, notably the period of credit to be granted, and any discounts to be allowed for early settlements.
ii. On a customer-by-customer basis, it is necessary to assess the creditworthiness and to establish limits in terms of amount and time. Consideration should be given to assessing a customer's creditworthiness, especially for new customers.
iii. In addition to the above consider reviewing existing customers from time to time, especially if they request that their credit limit should be raised.

Assessing customers' credit worthiness can be expensive in terms of both time and money, and as with all credit management the costs and the benefits have to be considered together. Thus the more detailed and expensive investigations should be reserved for potentially important or especially risky customers:

1. Always have accurate stock records and monitor slow-moving stock.
2. Be financially disciplined and controlled.
3. Cash and cheques should be banked promptly.
4. Avoid wasting money on shoddy deals and bribes.
5. Undertake proper multi-period capital budgeting using Net Present Value (NPV) and Internal Rate of Return (IRR) instead of relying only on Pay back.
6. Respect the separate corporate entity principle, by putting all employees and owner/managers on monthly salaries to avoid unnecessary withdrawals from the firm's resources.
7. Surplus/idle funds should be invested in overnight call accounts which yield high returns. This will help avoid keeping large cash balances in non-interest yielding current accounts.
8. Avoid mixing business transactions with non-business transactions. For example, financial dealings which do not add value to the business activities should not be allowed to take precedent over the core business activities.
9. Undertake credible internal and operational audits.
10. Disclose fully the financial position by keeping full set of information on business transactions. This makes it very easy to assess funds like venture capital which has been set up by the government.

The advent of the internet has brought a lot of innovations in the management of cash. For example, by using the internet the small firm can automatically route surplus cash to profitable investments. This is an area that small firms should consider investing in. A web-enabled treasury function brings a number of benefits. It allows increased control over cash positions and creates a portal for managing portfolios and trading in short term financial instruments like, over night call account, treasury bills, etc, available on the money market.

To help raise the standard of financial reporting in small firms, it is recommended that owner/managers should make good use of available computerised accounting packages. Computer spreadsheets are essential to modern organisations, as they allow managers to prepare a lot of financial reports. For example, cash budgets are vital to the management of cash. Management often makes use of cash budgets in determining cash surpluses or deficits. The availability of computer spreadsheets help in preparing several cash budgets based on possible future situations, such as:

i. An optimistic budget which assumes that the company achieves above-forecast growth.
ii. A pessimistic budget, which assumes below-forecast growth, and
iii. A target budget, which assumes forecast growth, is achieved.

One business process with which financial managers have an affinity, but which may nevertheless be contracted out, is the management of receivables. Specialist finance companies offer factoring arrangement under which they provide finance by advancing, say, 80% of invoice value immediately, the remainder being settled when the client's customers settle the debt. In Ghana factoring is not very popular even though some few companies have open offices in some of the major towns. Managers of small firms can make good use of such facilities to help improve upon the collection of their outstanding debts.

The government should also encourage the setting up of more factoring firms to help reduce the bad debt portfolios of not only the small firms but also those large companies who have difficulties in managing such risks. This can be done by granting tax holidays for such companies to encourage their establishment.

Owner/managers of small firms should avail themselves with the various training programmes organized by bodies like; Empretec Foundation, National board for small scale industries and the Ghana National Chamber of Commerce and Industry, to polish their knowledge in financial management and other management topics. This will help improve their trading activities. Poor managerial skills have commonly been associated with firm failure. Weitzel and Jonsson (1991) describe crises management and lack of planning as one of the last stages prior to failure. The employees working in these small firms should also be considered when it comes to training. This is important as in most cases when the owner/manager is not there then the whole business comes to a halt.

A study of Ghana's economic history shows that most small firms collapse on the death of the owner/managers. This results from the fact that whilst these owner/ managers were alive they did not have any succession plan in place for the continuance of their businesses. Some do not even allow their employees know their major suppliers as they think their employees may take their businesses from them if they are allowed to have contact with their major suppliers. Thus lack of faith in employees of these small firms has contributed significantly to the low survival rate of these small firms.

There is a slim line between tax avoidance and tax evasion. A significant number of small businesses are bent on paying little or no taxes and sometimes put pressure on auditors and accountants to comply with their wishes. Qualified accountants engaged by small firms should exercise great caution not to compromise their professional integrity to assist these firms to evade the payment of taxes. This is crucial as most of these accountants double as accountants and auditors to these small firms and the temptation to compromise on their professional integrity is so great.

Professional accountants engaged in providing services to small firms should charge reasonable fees to enable these companies use their services. The inability of these small firms to pay the high fees charged by qualified accountants is often cited as the main reason why these companies avoid using their services. The qualified accountants should not also use the small fees being recommended to cut corners in the services provided to the small firms.

As stated in earlier on, this is an exploratory study, the prime objective of which is to encourage further research. Future researchers could also consider an area such as; the relationship between firm size, finance and financial management practices and the relationship between these factors and firm performance.

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