

**THE IMPACT OF FINANCIAL MANAGEMENT PRACTICES ON GROWTH  
AND DEVELOPMENT OF MICRO AND SMALL ENTERPRISE. (THE CASE  
OF ADDIS KETEMA SUB-CITY, ADDIS ABABA, ETHIOPIA)**

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## FINAL APPROVAL FOR THESIS

This thesis titled “**The Impact of Financial Management Practices on Growth and Development of Micro and Small Enterprise. (The Case of Addis Ketema Sub-City, Addis Ababa, Ethiopia)**” has been prepared and submitted by **Seyfedin Mohammed SEYFEDIN** in partial fulfillment of the requirements in “**Anadolu University Directive on Graduate Education and Examination**” for the Master of Arts in **Department of Business Administration International Business** has been examined and approved on **27/12/2018**.

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## ABSTRACT

THE IMPACT OF FINANCIAL MANAGEMENT PRACTICES ON GROWTH AND DEVELOPMENT OF MICRO AND SMALL ENTERPRISE. (THE CASE OF ADDIS KETEMA SUB-CITY, ADDIS ABABA, ETHIOPIA).

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According to various studies, lack of finance is the most dominant constraint of Micro and Small Business in developing countries. Hence, management of financial resource is critical for small business development. Taking this, the study aimed in assessing the impact of financial management practice on growth and development of MSEs. The researcher chose *Addis Ketema sub-city, Addis Ababa, Ethiopia* as its geographical scope for the study due to its convenient nature to collect data.

The study used both primary and secondary sources of data. Survey data was obtained from 146 MSE owners/ managers through carefully designed questioner. These MSEs were proportionally selected from 3 main sectors which are textile and garment, food processing, and metal & wood work. Individual sample units were selected using a non-probability sampling technique called the convenience method. Further, due to definite nature of the population which was 896, a formula was implemented to determine the sample size needed to conduct the study.

Once data is collected, a *Descriptive* and *Explanatory* method of data analysis was implemented. Measures of central tendency was used to describe the general characteristics and variables while, inferential statistics tools specifically, *Regression* analysis and *Pearson* correlation coefficient was applied to measure the impact and relationships that exist between variables. Accordingly, despite strong relationship found between financial management and growth & development, poor financial management practice which strongly affect performance of MSEs was observed.

**Key words:** MSE, Financial Management, Growth & Development

## ÖZET

FİNANSAL YÖNETİM UYGULAMALARININ MİKRO VE KÜÇÜK İŞLETMELERİN BÜYÜME VE GELİŞMELERİ ÜZERİNE ETKİSİ. (ADDİS KETEMA BELEDİYESİ, ADDİS ABABA, ETİYOPYA).

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Danışman: Prof. Dr. Celal Hakan KAĞNICIOĞLU

Çeşitli çalışmalara göre, finans eksikliği, gelişmekte olan ülkelerde Mikro ve Küçük İşletmeler'in (MKİ) en baskın kısıtı olarak gözükmektedir. Bu nedenle, bu işletmelerin geliştirmek için finansal kaynağın yönetimi kritik öneme sahiptir. Bunu göz önünde bulundurarak bu çalışma finansal yönetim uygulamasının MKİ'lerin büyümesi ve gelişmesi üzerindeki etkisini değerlendirmeyi amaçlamıştır. Araştırmacı, veri toplamayı kolaylaştırmak amacıyla çalışmanın coğrafi kapsamı *Addis Ketema* belediyesi, *Addis Ababa*, *Etiyopya* olarak seçti.

Çalışma, birincil ve ikincil veri kaynaklarını kullanmıştır. Anket verileri, özenle tasarlanmış bir soru formülü aracılığıyla 146 MKİ sahiplerinden / yöneticisinden elde edilmiştir. Bu MKİ'ler, tekstil ve konfeksiyon, gıda işleme ve metal & ahşap işleri olmak üzere 3 ana sektörden orantılı olarak seçilmiştir. Bireysel numune birimleri kolayda örneklem yöntemi olarak adlandırılan olasılık dışı bir örnekleme tekniği kullanılarak seçilmiştir.. Ayrıca, hedef popülasyonu 896 olduğundan, çalışmayı yürütmek için gereken örnek büyüklüğünü belirlemek için bir formül uygulanmıştır.

Veri toplandıktan sonra, *Betimsel* ve *Açıklayıcı* bir veri analizi yöntemi uygulandı. Genel özellikleri ve değişkenleri tanımlamak için merkezi eğilim ölçüleri kullanılırken, değişken istatistik araçları özellikle Regresyon analizi ve Pearson korelasyon katsayısı değişkenler arasındaki etki ve ilişkileri ölçmek için uygulanmıştır. Buna göre, finansal yönetim ile büyüme ve gelişme arasında güçlü bir ilişki bulunmasına rağmen, MKİ'lerin performansını güçlü bir şekilde etkileyen zayıf finansal yönetim uygulaması gözlenmiştir.

**Anahtar Sözcükler:** MKİ, Finansal Yönetimi, Büyüme ve Gelişme

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## STATEMENT OF COMPLIANCE WITH ETHICAL PRINCIPLES AND RULES

27.12.2018

I hereby truthfully declare that this thesis is an original work prepared by me; that I have behaved in accordance with the scientific ethical principles and rules throughout the stages of preparation, data collection, analysis and presentation of my work; that I have cited the sources of all the data and information that could be obtained within the scope of this study, and included these sources in the references section; and that this study has been scanned for plagiarism with “scientific plagiarism detection program” used by Anadolu University, and that “it does not have any plagiarism” whatsoever. I also declare that, if a case contrary to my declaration is detected in my work at any time, I hereby express my consent to all the ethical and legal consequences that are involved.



(Signature)

Seyfedin Mohammed SEYFEDIN

## CONTENTS

	<u>Page</u>
<b>FINAL APPROVAL FOR THESIS .....</b>	<b>ii</b>
<b>ABSTRACT.....</b>	<b>iii</b>
<b>ÖZET .....</b>	<b>iv</b>
<b>ACKNOWLEDGEMENT.....</b>	<b>v</b>
<b>STATEMENT OF ETHICAL COMPLIANCE.....</b>	<b>vi</b>
<b>TABLE CONTENTS.....</b>	<b>vi</b>
<b>LIST OF TABLES .....</b>	<b>x</b>
<b>CHARTS &amp; FIGURES.....</b>	<b>xi</b>
<b>ACRONYMS &amp; ABBREVIATIONS .....</b>	<b>xii</b>
<b>CHAPTER 1: INTRODUCTION.....</b>	<b>1</b>
<b>1.1 Background of the Study .....</b>	<b>1</b>
<b>1.2 Background of the Country.....</b>	<b>4</b>
<b>1.3 Statement of The Problem.....</b>	<b>5</b>
<b>1.4 Significance of Study.....</b>	<b>7</b>
<b>1.5 Delimitation of The Study .....</b>	<b>7</b>
<b>1.6 Objectives of The Study.....</b>	<b>8</b>
<b>1.7 Conceptual Framework.....</b>	<b>8</b>
<b>1.8 Hypothesis of the Study .....</b>	<b>9</b>
<b>CHAPTER 2: LITERATURE REVIEW .....</b>	<b>10</b>
<b>2.1 Definition of Micro and Small Enterprises.....</b>	<b>10</b>
<b>2.2 The Role of Micro and Small Enterprises.....</b>	<b>12</b>
<b>2.3 The Need for Finance in Micro and Small Enterprises.....</b>	<b>14</b>
<b>2.4 Definition and Importance of Financial Management in MSE .....</b>	<b>15</b>
<b>2.4.1 Definition and goal of financial management .....</b>	<b>15</b>
<b>2.4.2 Importance of managing finance in MSE .....</b>	<b>17</b>
<b>2.5 Importance of Financial Records and Information to MSE.....</b>	<b>19</b>
<b>2.6 Financial Management and Small Business Owners.....</b>	<b>20</b>
<b>2.7 Financial Management Practice Differences in Large and Small Businesses.....</b>	<b>21</b>
<b>2.8 Cash and Working Capital Management in Small Businesses.....</b>	<b>23</b>
<b>2.8.1 Importance of cash flow in small business .....</b>	<b>23</b>
<b>2.8.2 Importance of working capital.....</b>	<b>25</b>

2.9 The Need for Financial Forecasting and Planning in Small Business.....	26
2.10 Financial Sources of MSE .....	28
2.10.1 Formal financial sources of MSE.....	30
2.10.2 Semi-formal financial sources of MSE .....	30
2.10.3 Informal financial sources of MSE .....	31
2.11 General Problems and Factors Affecting Financial Management of MSE .	33
2.12 Factors Affecting Financial Management Techniques .....	34
<b>CHAPTER 3: RESEARCH METHODOLOGY .....</b>	<b>36</b>
3.1 Research Design and Methodology.....	36
3.2 Sources of Data.....	37
3.3 Sampling Strategy and Procedures .....	38
3.3.1 Sampling technique and sample size determination .....	39
3.4 Reliability Test.....	40
3.5 Data Analysis and Presentation .....	41
3.6 Variable Measurement .....	42
3.6.1 Dependent variable.....	42
3.6.2 Independent variables .....	43
3.7 Model Specification.....	43
3.8 Research Ethics .....	44
<b>CHAPTER 4: DATA PRESENTATION, ANALYSIS AND INTERPRETATION</b> <b>.....</b>	<b>45</b>
4.1 General Profile of MSEs.....	45
4.1.1 Gender distribution of MSEs .....	45
4.1.2 Age distribution of MSE owners or managers.....	46
4.1.3 Marital status of MSE owners or managers .....	47
4.1.4 Educational status of MSE owners or managers.....	47
4.1.5 General business Experience of MSE owners or managers .....	48
4.2 Business Related Profile of the MSEs.....	49
4.2.1 Working sector of MSEs .....	49
4.2.2 Ownership form of MSEs .....	50
4.2.3 Number of employees in MSEs .....	51
4.2.4 General financial status of MSEs.....	52
4.2.5 Financial sources of MSEs.....	53

4.2.6 Profitability trend of MSEs .....	53
4.2.7 Market share trend of MSEs .....	54
4.2.8 Trend of employment opportunity creating of MSEs .....	55
4.3 Financial Management Practices of MSEs .....	56
4.3.1 General financial management approach of MSEs.....	56
4.3.2 Financial management skill and related factors of MSEs .....	60
4.3.3 Financial data usage and application of MSEs .....	62
4.3.4 Growth and development & financial management practices of MSEs .	66
4.4 Results of Inferential Statistics .....	67
4.4.1 Pearson’s product moment correlation coefficient .....	68
4.4.2 Regression analysis .....	69
4.5 Summary of The Results .....	72
<b>CHAPTER 5: CONCLUSION AND RECOMMENDATION .....</b>	<b>74</b>
5.1 Conclusions .....	74
5.2 Recommendations .....	76

**APPENDIX**

**CURRICULUM VITAE**

## LIST OF TABLES

	<b>Page</b>
<b>Table 1.1</b> Addis Ababa sub-cities .....	5
<b>Table 3.1</b> MSE sample size to be taken .....	40
<b>Table 3.2</b> Result of reliability test .....	40
<b>Table 3.3</b> Performance grading criteria.....	41
<b>Table 3.4</b> Interpretation of correlation coefficient r.....	42
<b>Table 4.1</b> Financial management attitude and application of MSEs.....	57
<b>Table 4.2</b> Financial management skill related factors of MSEs.....	61
<b>Table 4.3</b> Financial data usage and application of MSEs .....	63
<b>Table 4. 4</b> Financial management practice and growth and development of MSEs.....	66
<b>Table 4.5</b> The correlation of performance (growth & development) with financial management approach, skill & usage and application in MSEs.....	68
<b>Table 4.6</b> Regress financial management approach, skill & data usage and application of MSE as independent variable on performance (growth & development) as dependent variable.....	69

## CHARTS & FIGURES

	<u>Page</u>
<b>Figure 1.1</b> Conceptual Frame Work-----	9
<b>Figure 4.1</b> Gender Distribution of MSEs .....	46
<b>Figure 4.2</b> Age Distribution of MSE Owners or Managers .....	46
<b>Figure 4.3</b> Marital Status of MSE Owners or Managers .....	47
<b>Figure 4.4</b> Educational Status of MSE Owners or Managers .....	48
<b>Figure 4.5</b> General Work Experience of MSE Owners or Managers .....	49
<b>Figure 4.6</b> Working sectors of MSE .....	50
<b>Figure 4.7</b> Form of business ownership of MSEs.....	51
<b>Figure 4.8</b> Number of employees in MSEs.....	52
<b>Figure 4.9</b> The Number of MSEs Facing Financial Shortage.....	52
<b>Figure 4.10</b> Financial Sources of MSEs .....	53
<b>Figure 4.11</b> Profitability trend of MSEs .....	54
<b>Figure 4.12</b> Market share trend of MSEs.....	55
<b>Figure 4.13</b> Employment trend of MSEs .....	56

## ACRONYMS & ABBREVIATIONS

<b>AAMSEDA</b>	: Addis Ababa Micro and Small-Scale Enterprise Development Agency
<b>AD</b>	: Anno Domini
<b>AIS</b>	: Accounting Information System
<b>B2B</b>	: Business to Business
<b>CPA</b>	: Certified Public Accountant
<b>CSA</b>	: Central Statistics Authority
<b>FM</b>	: Financial Management
<b>FMSEDA</b>	: Federal Micro and Small-Scale Enterprise Development Agency
<b>GDP</b>	: Gross Domestic Product
<b>IMF</b>	: International Monetary Fund
<b>MFA</b>	: Ministry of Foreign Affairs
<b>MFI</b>	: Micro Finance Institution
<b>MTI</b>	: Ministry of Trade and Industry
<b>MSE</b>	: Micro and Small-Scale Enterprises
<b>NGO</b>	: Non-Governmental Organization
<b>SPSS</b>	: Statistical Package for Social Sciences
<b>UNIDO</b>	: United Nations Industrial Development Organizations

## CHAPTER 1: INTRODUCTION

This section deals with a brief over look of studies and concepts that serve as background to the study under consideration. It also provides us the road map as to what major problems the study wants to address, the research objective, the hypothesis behind, the significance to various stakeholders and scope of the study in general.

### 1.1 Background of the Study

Almost all business, be it small or big, start and run their operations to obtain and maximize profits. In doing so, businesses engage in various activities which result in generating income, incurring expenses, interest rates, payables and many other finance related activities. Business owners or entrepreneurs analyze and use the information generated from the above-mentioned transactions to help them in planning, formulating and implementing sound financial strategies and policies for their businesses. Therefore, management of financial activities is one of the most important areas that need focus, making financial management skill crucial to prevent the collapse of business and to successfully achieve business goals. (Scarborough & Zimmer, 2003, p 220).

According to Hatten (2006, p. 218), small business owners knowingly or unknowingly undermine the importance of financial management activities. This seemingly trivial but important function is usually neglected by business owners while they focus on other business activities like purchasing & sales. But it is this laxity towards financial management that usually tend to become deadly at the end of the day leading these small businesses out of the market.

Nowadays, many of the developing world, with their huge number of unemployed populations and poor economic conditions, development of micro and small enterprises (*MSEs*) is essential. These *MSEs* takes the lion share business format of developing economies and hence has been identified as major support and development assistances areas of donor nations (Carl and Donald, 1998, p, 134-136).

Although *MSEs* are major economic landscape in the developing countries, startup and development of such businesses has never been easy. In spite of the fact that relatively low capital is required to start up and develop *MSEs*, businesses path towards finding the capital needed, which is the epicenter problem of most developing countries, is full of obstacles. This factor usually plays the main role in discouraging entrepreneurs and thereby hampering the development of *MSEs*. (Sargent and Young, 1998: cited in Gashahun, 2004, p. 13). In fact, among other reasons, lack of financial support from

various financial institutions, which has attributed to the underdevelopment of *MSEs* can be better manifested in their minimal contributions to the overall economy. (Thorsten and Demircuc k., 2006, p 2935).

In recent years, in order to win the stiff competition created in addition to unfavorable economic conditions, business owners are expected to act in a more professional and smart way in operating their businesses. Operational efficiency in return leads to the ease of finding and or assuring the continuity of financial institutions support to their business activities (Longenecker, William and Leslie, 2006 p. 358). Before starting up of a business, entrepreneurs should clearly identify and analyze from where to get the money required to start and run their businesses. Businesses can raise the needed funds either from their own pockets or through reaching others (borrowing). Hence, they are ought to carefully consider available options and recognize their long and short-term consequences on the business while selecting sound financial strategy. The overall turmoil in financial market, which is the common characteristics of this markets, tends to pose a serious challenge for incumbent or existing businesses. This is in a sense, due to unstable nature of the finance sector, businesses face difficulty in planning, identifying and effectively using external finance institutions. External investors be it banks, angles or else, they naturally expect a return from their investments. Normally they are reluctant to invest their money on businesses which does not have market experiences or on businesses with low profile and prospects. This makes the scope of accessible potential businesses which lenders are willing to invest narrow (Longenecker et al, 2006, P 359).

For *MSEs*, the best way to convince lenders is to prepare and give them a comprehensive financial information showing them the status and performance of the business. This financial information presented to financing institutions according to (Longenecker et al, 2006, P 331) needs to be precise, clear and realistically promising regarding the success and profitability of the business. A small business consultant *Paul A. Broni* has put the importance of financial information as follows:” It doesn't matter whether you're applying for your first bank loan or your fifth, or whether you're seeking venture capital or debt financing. Sooner or later, you'll have to prepare a set of financial projections. Lenders will look for a strong likelihood of repayment; investors will calculate what they think is the value of your company”.

Financial management plays also a key role for the business itself by providing information on the status of businesses' working capital. It helps businesses to plan, follow, control and balance the flow of available finance to avoid a stuck in firms' day to day activities due to inadequacy of working capital. (McMahon and Holmes, 1991, p. 19). In other words, it is decisive for small businesses to vigilantly observe the overall finance flows of the business. This help business owners to better understand and interpret the consequences of these finance transactions thereby enabling them to take the necessary precautions and decisions.

In Ethiopia the contribution of small and medium enterprises is huge specially in consideration with the large population it engages thereby creating an employment opportunity. In Ethiopia, agriculture now accounts for less than fifty percent of GDP, though some 80% of the population still gains its livelihood, directly or indirectly (Ethiopian Government portal 2017). Next to agriculture, it is micro and small enterprises sector that accounts as major source of employment (Central statistics authority CSA, 2005:34-35). These enterprises play an important role in the overall poverty reduction strategy the government set to implement through its growth and transformation plan to achieve a steady and sustainable overall growth and development.

Despite of its significance, the *MSEs* sector in Ethiopia faces many similar problems like that of developing countries. This problems stretch-outs from financial problem or lack of capital to marketing, skilled human resource and to political problems (Werotew, 2010:226-37 cited from Admasu A. 2012, p3,). Considering that finance is chronic problem and that the current environment is characterized by a reduced availability of credit and tighter lending standards, the financing needs, practices and management of *MSEs* in Ethiopia deserves attention. Although every small business owner starts with the objective of being profitable and successful, it is becoming our part of day to day life to witness, hear or observe businesses go out of the market or bankrupt due to finance related problems. This is of course, being finance and related problems are not the only reason for enterprises to exit from the market. (Dennis and Fernald, 2001), therefore, assessing and understanding the financial practices and their impact on the starting up, growth and development of micro and small businesses is crucial.

## 1.2 Background of the Country

Ethiopia is among the world's oldest civilizations in history which dates back to the first millennium BC. A trade relationship is used to exist between ancient Egypt and the land of Punt which was located around present day the coast of Eritrea or possibly Somaliland. The Kingdom of Axum which was located present day northern Regional State of Tigray in Ethiopia was the famous one emerged at the beginning of the Christian Era and flourished until around 800 AD. (Ministry of foreign affairs, 2017)

Currently, Ethiopia is officially known as Federal Democratic Republic of Ethiopia and is located in what is known as the Horn of Africa. It shares borders with Eritrea to the north and northeast, Djibouti and Somalia to the east, Sudan and South Sudan to the west, and Kenya to the south. With over 102 million inhabitants, Ethiopia is the most populous landlocked country in the world and the second-most populous nation on the African continent. It occupies a total area of 1,100,000 square kilometres (420,000 sq mi), and its capital and largest city is *Addis Ababa*. Since 1996, Ethiopia has been divided into nine ethnically-based and politically autonomous regional states and two chartered cities, the latter being *Addis Ababa* and Dire Dawa.

According to the IMF, Ethiopia witnessed one among fastest growing economies in the world, registering over 10% economic growth from 2004 through 2009. It was Africa's fastest-growing economy in the years 2007 and 2008 among those whose economy does not depend on oil. In 2015, the World Bank highlighted that Ethiopia had witnessed rapid economic growth with real domestic product (GDP) growth averaging 10.9% between 2004 and 2014.

According to Ethiopian Government portal (2017) agriculture constitutes around 80% of the labor force. However, the service sector represents the largest portion of the GDP. Many other economic activities depend on agriculture, including marketing, processing, and export of agricultural products. Production is overwhelmingly by small-scale farmers and enterprises, and a large part of commodity exports are provided by the small agricultural cash-crop sector. Principal crops include coffee, legumes, oilseeds, cereals, potatoes, sugarcane, and vegetables.

The capital city *Addis Ababa* is often referred to as "the *political* capital of Africa" for its historical, diplomatic and *political* significance for the continent. The economic activities in *Addis Ababa* are diverse reaching from trade and commerce, manufacturing

and industry, homemakers of different variety, civil administration, transport and communication, education, health and social services, hotel and catering service and to agriculture (Ministry of foreign affairs, 2017). The city has recently been in a construction boom with tall buildings rising in many places. Various luxury services have also become available and the construction of shopping malls has recently increased. According to Tia Goldenberg of IOL, area spa professionals said that some people have labeled the city, "The spa capital of Africa". Table 1.1 here below shows the 10 administrative boroughs or sub-cities *Addis Ababa* city has as follows:

**Table 1.1 Addis Ababa sub-cities (Wikipedia, 2017)**

No.	Subcity	Area (km <sup>2</sup> )	Population
1	Addis Ketema*	7.41	271,644
2	Akaky Kaliti	118.08	195,273
3	Arada	9.91	225,999
4	Bole	122.08	328,900
5	Gullele	30.18	284,865
6	Kirkos	14.62	235,441
7	Kolfe Keranio	61.25	546,219
8	Lideta	9.18	214,769
9	Nifas Silk-Lafto	68.30	335,740
10	Yeka	85.46	337,575

\*This research is conducted on micro and small enterprises located in *Addis Ababa* city of *Addis Ketema* sub-city.

### **1.3 Statement of The Problem**

*MSEs* are one of fundamental sectors in Ethiopia accountable for the creation and absorption of employment opportunities (Federal Micro and Small-Scale Enterprise Development Agency FMSEDA, 2006:13). Regardless of this, the sector was not able to contribute for the development of the overall economy as expected. Poor performance of *MSEs* can be attributed to numerous factors reaching from turbulently changing market conditions to lack of capital access, weak managerial and practical business skills and others (Zinab and kalsoum 2017).

Finance and related issues are considered as a heartbeat with in most of business enterprises. Over the years, there has been a significant increase in government efforts to promote the financing of businesses by initiating policies which help small and medium

scale businesses to source funds for business operations. Business owners need to have good know how of financial management activities like working capital management, budgeting and financial planning to help them make the right decision when it comes to financial issues that affect the overall performance of their business. Inability of performing these functions properly has the capacity that leads to the failure of not only small businesses, but it can have a worldwide effect as witnessed in 2007s global financial crisis (Osisioma, 2010, p. 159). Similarly, careless or poor execution of financial management practice has been identified as one of the root causes for small business failures (McMahon and Holmes, 1991; p 19-29).

To address above problems, this study therefore aims to provide a holistic view of the financial management practices of *MSEs* through a comprehensive review of literature and empirical study available on the area. From the practical point of view, it serves not only as a status check to current situation of *MSEs* financial management practices, but also to increase success and profitability of businesses through a better understanding of these practices which helps in effective and efficient utilization of financial resources of *MSEs*.

In addition, the researcher's literature search shows that to date, very little research has been conducted on the financial management practices of small businesses in Ethiopia in general, and particularly none in *Addis Ababa/Addis Ketema* sub city. Thus, gaps exist with respect to understanding the importance and effects of financial management practice in *MSEs*. Given the significance of *MSEs* to a nation's development in different ways, this study generally evaluates the application and practice of financial management instruments and their effect in the initial and throughout the whole growth development stage of *MSEs*. Hence the study will address the following specific research questions.

- ✓ To what extent does financial management practice affect the growth and development of *MSEs*?
- ✓ To what extent does the approach, management and administration practices of financial management in micro and small enterprises affect the growth and development?
- ✓ To what extent does financial management knowhow and skills in micro and small enterprises affect the growth and development?
- ✓ To what extent does the usage and application of financial data in micro and small enterprises affect the growth and development?

## **1.4 Significance of Study**

The findings of this study will be useful to the stakeholders including:

### **I. Academicians or researchers**

Findings from this study will assist academicians in broadening of the prospectus with respect to this study hence providing a deeper understanding of financial management practices in *MSEs*.

### **II. Micro and small enterprises**

The findings of this study will help *MSEs* in *Addis ketema* sub-city and others, in clearly understanding the impact and importance of financial management practices thereby giving the attention it needs from business owners or entrepreneurs.

### **III. Governmental policy makers**

The government can use the findings of this study to assist in policy formulation and development for a framework for financial access problems *MSEs*.. Moreover, the findings of this study will help the policy makers and financial institutions how to encourage establishing or expanding *MSEs*. It also enables them to know what kind(s) of policies should be framed.

## **1.5 Delimitation of The Study**

The study assesses the impact of financial management practices on growth and development of *MSEs* in *Addis Ababa* city particularly in *Addis ketema* sub-city. *Addis Ketema* is one among the 10 administrative sub-divisions of *Addis Ababa* city. Although there are different sectors in which the *MSE* operators have engaged in *Addis Ketema* sub-city, the sectors to be selected for this research are textile and garment, food processing and metal and wood work sector because of the following rationales. First, the sectors are selected because of largest concentration in number Second, it will be difficult to reach the operators/or owners managers of some sectors like municipality service, parking and others. Lastly, According to Meheret and Tegegne (2010:36-37) textile and garment and metal and wood work engages the majority work force operating in micro and small business sector through cooperative form of organization. In addition, it is also in order to make the study manageable that the researcher delimit the study in *Addis ketema* sub-city and the above-mentioned sectors.

## **1.6 Objectives of The Study**

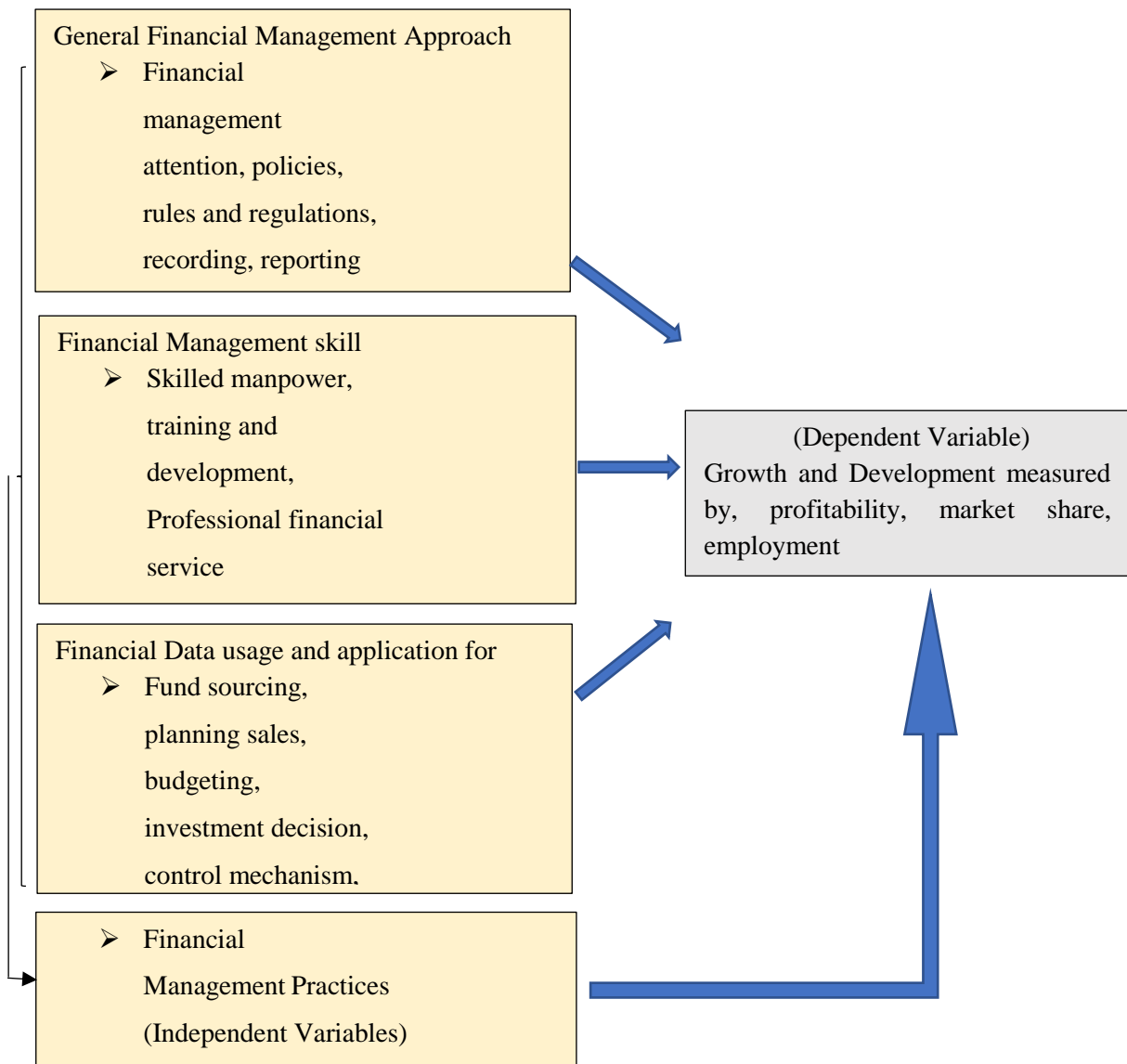
Virtually speaking, without finance in their hand, businesses are not able to perform any activities. It is a determinant factor for the success and survival of *MSEs*. In light of this, how *MSEs* successfully manage their financial resources is a crucial factor. Therefore, the main objective of the study is to assess the financial management practices used by business owners / managers of micro and small businesses and how this affects growth and development of *MSEs* in *Addis ketema* sub-city of *Addis Ababa*.

In relation to this, the following are specific objectives the study targets to address:

- 1) To assess the effect of financial management practice on *MSEs* growth and development.
- 2) To assess the extent to which *MSEs* approach, management and administration practices of financial management affects growth and development.
- 3) To assess the extent to which financial management knowhow and skills affects growth and development of *MSEs*.
- 4) To assess the extent to which usage and application of financial data affects growth and development of *MSEs*.
- 5) To suggest actions to be taken by concerned bodies to overcome problems regarding financial management practices and make *MSEs* sustainable and improve their performance.

## **1.7 Conceptual Framework**

Conceptual framework means that concepts that relate to one another were used to explain the research problem. Since the growth and development of micro and small business is influenced by various internal and external factors, this study focused on internal factors of a business with specific emphasis on how the financial management practices of *MSEs* affect growth and development. This is because, according to Hatten (2006), inefficient financial management practice in a business could fatally lead to the failure of businesses. In this context, this study has identified three crucial variables that were closely monitored to see their influence on *MSEs* growth and development. These are, overall financial management approach, financial management skill and financial data usage and application. The relationship of these variables is depicted in figure as follows:



**Figure 1.1** *Conceptual Frame Work*

## 1.8 Hypothesis of the Study

The study carefully tests the following hypothesis considering all independent variables and the dependent variable with the help of sufficient and appropriate empirical data on the impact of financial management practice on growth and development MSEs:

**H<sub>1</sub>:** Financial management practice has a significant impact and relationship with the growth and development of *MSEs*.

**H<sub>2</sub>:** The approach, management and administration practices of financial management has a significant impact and relationship with the growth and development of *MSEs*.

**H<sub>3</sub>:** Financial management skills have a significant impact and relationship with the growth and development of *MSEs*.

**H<sub>4</sub>:** Usage and application of financial data has a significant impact and relationship with the growth and development of *MSEs*.

## CHAPTER 2: LITERATURE REVIEW

This section is reserved for presenting the various concepts, theories and definitions the researcher reviewed in relation with the subject topic of micro and small enterprises and financial management. In doing so, various books, brochures, journals, articles, related previous studies and any relevant materials was used.

### 2.1 Definition of Micro and Small Enterprises

The *MSE* industry in almost all place around the world is known by its wide variety activities and potentials in creating job opportunities for a significant part of the population. This refers that this sector, if utilized properly, has a huge capability of alleviating unemployment problems in every society. In countries, especially those in developing ones, where young and productive work force comprises majority of the total population percentage, sustained overall development can only be achieved through creating and providing a conducive job opportunity (Mulugeta Y, 2011, p.13). Therefore, to direct all necessary support and facilities to this diversified sector, first there should be a consensus definition regarding how to categorize the sectors in *MSE*.

However, there is no generally accepted or clear-cut definition of a small enterprise (Kayanula and Quartey, 2000, P. 35). This is so because the basis used and ways of categorizing enterprises as micro and small differs from institution to institution and from country to country depending essentially on the country's level of development. In addition, changes in price levels, advances in technology or other considerations can also affect the definition of *MSE* (Emma I. and Akamoibi L, 2009, p. 1-9). Firms differ in their levels of capitalization, sales and employment. Hence, the use of measures of size (number of employees, turnover, profitability, net worth, etc.) can lead to two different definitions being applied in different conditions and circumstances. This has led to the difficulty of finding universal definition. In line with this, (Tegegne and Meheret, 2010 p. 11) argued that the absence of a single or globally applicable definition made the research and development work in this area demanding in different countries and though the rationale for most governments to make such definition and categorization is mainly for functional and promotional purposes to achieve the desired levels of development of the sector.

United Nations Industrial Development Organizations (UNIDO) defined *MSE* for developing countries by taking in to account the work force under employment i.e., if a firm runs its operation with 5 and less headcounts, then it is categorized under Micro enterprises, whereas firms with 5-10 headcounts are regarded as small enterprises. (UNIDO, 2002, p. 53).

In United States of America, the Small Business Act issued in 1953 defined small business as an independently owned and operated and not dominant in its field of operation. In the same country, the structure of this enterprise administration from top to bottom, the ownership style and the financial source are the unique characteristics attached to *MSE*.

In Kenya, by referring the 1999 *MSE* National Baseline Survey, including both the formal or informal sector employing 1-50 people and engaged basically in non-primary enterprises (excluding agricultural production, animal husbandry, fishing, hunting, gathering and forestry), are defined as *MSE* (Ronge et al., 2002 cited in Mulugeta, 2011:15). More specifically, based on the criteria of number of employees, degree of legal formality to distinguish between the formal and informal sectors and amounts of capital and skills per worker, those with less than 10 employees are stated as micro enterprises whereas those with 10-15 are referred as small businesses. If we tried to wrap the points made above, the two major outstanding considerations that are on board on today's condition to classify MSEs includes the extent of formality in their operation including both formal and informal enterprises, and how big they are.

When we came to the scenarios in Ethiopia regarding MSE, it is easy to notice above manifested problems of the international community in reaching to a uniform definition. Two prominent governmental institutions, Ministry of Trade and Industry (*MoTI*) and the Ethiopian Central Statistics Authority (*CSA*) have come up with their own terms of definition for *MSEs*. *MoTI*'s definition for micro and small-scale enterprise is based on capital investment which was used latter for formulating *MSE* development strategy. *CSA* on the other hand uses employment and favors capital intensive technologies as a yardstick (*MoTI*, 1997, P. 8-21).

According to (*MoTI*, 1998, Art. 2(1)), "Micro Enterprise means an enterprise having a total capital, excluding building, not exceeding Birr 50,000 in the case of service sector or not exceeding Birr 100,000 in the case of industrial sector and engages 5 workers including the owner, his family members and other employees. The same institution under (Art.2(2)) defines "small enterprise" as an enterprise having a total capital, excluding building, from Birr 50,001 to 500,000 in the case of service sector or Birr

100,001 to Birr 1,500,000 in the case of industrial sector and engages 6 to 30 workers including the owner his family members and other employees”.

Parameters like financial ability, technological advancement and application on business activities and work force engagement are the main benchmarks the central statistical authority (CSA) applied when defining MSE. Accordingly, micro enterprises are those employing less than 10 persons and are sub-divided into informal sector operations and cottage industries: cottage and handicraft industries refers to those traditional industries whose source of their production capacity depends only on hand works and personal skill. The informal sector is defined as household type establishments or activities, which are non-registered enterprises and cooperatives operating with less than 10 persons (CSA, 2003, p. 21).

We can clearly infer from the above the burdensome of getting a single acceptable definition for *MSE*. Different scholars, institutions and governments defined *MSEs* differently based on the level of development of the country under review and various economic indicators and using their own parameters.

## **2.2 The Role of Micro and Small Enterprises**

The *MSEs* have a huge contribution in elevating countries overall economic growth and development through considerably adding to value chain of productivity. According to Nichter and Goldmark (2005), value chain includes, such activities like product concept development, product design, manufacturing, product distribution and all other related activities up to final customer and final disposal after use.

The *MSEs* are considered as crucial part at local, national and even international level from various perspectives. For example, among important roles that *MSE* plays, employment and job opportunity creation is considered to be the major one. It is important to take note that employment is a vital aspect in the economic development because it helps to provide every individual or citizen the source of income. This improvement is followed by an increase in purchasing power of the individuals boosting their living standards. On the other side, an income generated serve as income tax source for the government enabling it to improve infrastructures and public services. This in turn develops and widens market opportunities leading to attract number of investments locally or even at international level.

The study made by Leegwater and Shaw (2008), shows that countries that witness higher growth in their economy are usually those with large *MSE* employment. This is,

as mentioned above, due to the direct impact employment has on purchasing or spending power of citizens thereby affecting financial or economic activities of the country on one way or another. This indicates that, it has the capacity to alter the overall operation of different commercial companies in the country and hence creating a great opportunity in adding financial sources for the local economy.

The key question now is the extent to which the development of the sector will assist in resolving major (economic and noneconomic) development issues. Over the past few years, *MSEs* started to play an important role providing solutions to major contemporary developmental problems. This was because of several factors but mainly due to a cumulative wealth of experiences and evaluations of a great variety of promotional efforts and projects. Researches done previously in this area exhibits that the effectiveness of micro-level efforts can be improved by addressing sectoral/regional and macro-economic factors. Thus, there is a greater disposition to consider the wider policy framework for *MSEs* development (Stewart *et al.*, 1990 cited in Helmsing and Kolstee, 1993).

In overall economic development, a critically important role is played by *MSEs* in Ethiopia. Expansion and development of this sector increases agricultural productivity through providing agricultural inputs and creating demand for agricultural outputs. Further, *MSEs* play key role in stimulating other sectors of the economy such as trade, construction and service sector contributing to unemployment reduction. Here are some of the important roles *MSEs* play in overall social and economic development.

- Serve as a ground base for expanding and growing of the business to medium level,
- Usually the start-up capital required is low,
- Less capital intensive (they are labor intensive),
- Provide Large employment opportunity to unskilled and semi-skilled labor force (particularly for women),
- Helps in balancing distribution of income in the society,
- Develop pool of skilled and semi-skilled workers necessary for future industrialization process to take place,
- Cross sectoral transaction and business activities are promoted,
- Apply simple and suitable technologies,
- Promotes local markets and production by utilizing local raw materials,
- Critically important for recycling for solid wastes,
- Serve as sources of raw material and distribution channel for the formal sector,

- Save scarce resources and have the capacity to generate foreign exchanges by producing import substitute/export products,
- Provide market opportunity especially for low income earners,
- Play significant role on the regulation of the market price,
- The sector has advantage to protect and transmit countries historical, religious and social values,
- Serve as a center of innovation, etc. (AAMSEDA, 2003 E.C: cited in Ermiyas W. 2011 p. 11-13).

### **2.3 The Need for Finance in Micro and Small Enterprises**

A decision to start a business or expand an already existing firm requires with it the availability of adequate money to help finance the decision. Consequently, financing is basically the major consideration and decision of *MSEs* in their course of starting-up, ruining and or expanding of operation. Keeping this, it is indicated that the inability to raise finance, which is the critical factor in the establishment and growth of such businesses, is one of the greatest challenges facing the *MSEs* (Sargent and Young cited in Gashahun, 2004, P. 13). Similarly, the need to finance for *MSEs* can be justified through the businesses need of finance to invest in new equipment and machinery, reach out to new markets and products and cope with temporary cash flow shortages as well as to innovate and expand (Fafchamps cited in Gebrehiwot and Wolday, 2003, p. 3). In spite of this, *MSEs* limited access to available finance compared to larger organizations have limited their growth and development. In addition, *MSEs* are forced to higher transaction costs than larger enterprises to obtain finance. Moreover, insufficient funding has been made available working capital scarce (Levy cited in Cook p., 2000:7).

The 1995/96 survey of urban informal activities in Ethiopia discloses that, among various problems *MSEs* face either in operating their day to day operations or planning for expansion activities, the most pressing one is identified to be financial problems or limitations. According to the survey of 1995/96, 50% of the informal sector operations indicated that their main problem in operation was lack of sufficient initial capital. Lack of sufficient capital, particularly at the start of their operations, was also identified as the major problem for about 35% of the small-scale manufacturing industries (Gebrehiwot and Wolday, 2004, p. 54).

## **2.4 Definition and Importance of Financial Management in MSE**

This section presents the product of the researchers review on various literatures regarding what financial management means and to what extent does small business need the application of financial management.

### **2.4.1 Definition and goal of financial management**

Finding a single universal definition for financial management is difficult. There are various definitions for financial management from various authors and researchers. According to (Meredith, 1986 & Amoako et al, 2013: cited in Solomon T. 2017 P. 19-20), financial management is part and parcel of management activities. It deals with the various responsibilities a finance manager in a business should address. This activity can be considered as success or failure factor of a business depending on how well it is carried on. It also focuses and highlights the use of information systems like financial management records and reports as a foundation for financial management (Barrow, 1988: cited in Regina G. 2012 p. 1905). While trying to define financial management, Barrow focused on making practical definitions by enlisting the tools necessary for financial analysis like measure of profitability, cost, volume, pricing, working capital and fixed assets control. McMahon (1995) examines specific areas of financial management including all areas that relate to items on the balance sheet of the business. Whereas (Massie, 1986: cited in Svetlana S & Svetlana S. 2016 p. 50-51) put financial management as a tool that help businesses to effectively and efficiently utilize business operations through modulating the acquisition of assets necessary. (Brealey, 2008: cited in Svetlana S & Svetlana S. 2016 p. 50-51) see financial management as a long-term process to best utilize funds available for best achievement of business objectives. As for (Howard & Upton, 1953) financial management is an application of general managerial principles to the area of financial decision-making.

In dealing with definitions in the areas of financial management, readers usually face with common terminologies of tools that scholars use in their definition. This includes: Financial planning, analysis, and control: This deals with the important tools one use in measuring financial performance of businesses. It includes examining financial objectives and targets, considering the available financial budgeting and designing control mechanism which provides the necessary data for analysis and interpretation. Financial reporting: deals with identifying the character, prevalence and objective of financial reporting. Working capital management: this is related with businesses investment in

short-term assets, accounts receivables, cash, and inventories. Accounting information systems: is done usually through the use of different software's and programs that collect, records, stores and processes data which serve as a source of input for decision makers in the business. This can be also done manually. Capital budgeting (Investing): concerned with the identifying analysing and making the best portfolio decision for the business among the opportunities available taking businesses limited resource in to consideration. Financing (Capital Structure): refers to finding out optional source of money for the long-term debt and equity (Solomon T., 2014, p. 19-20).

Basically, the main objective of businesses financial management has to be directed towards increasing the market value of the business and its stakeholders. In other words, all business activities and critical administrative methods and tools must be forwarded in a way that help the company significantly add to its value, making decisions taken in the business to have a solid logical and practical background. Financial management in businesses are not only an internal process. It involves considering various external forces and relationships which surround the business environment. This may include taking in to consideration of the market characteristics, potential investors competitors action and reaction. Most authors in this field argues that, mismanagement of financial resources or negligence of financial management activity obviously have an adverse impact on its value. This indicates that appropriate financial management indirectly means value adding to businesses. Practical formation of the financial management should be based upon certain theoretical platform. Businesses to achieve strategic goals need to adjust their financial management practices of planning, implementation, control and management decision-making. This makes the business in long-term achieve a sustainable development adding value to stakeholders through position the itself to effectively tap funding sources available, fixed and current assets at strategic and operational levels. (Savina & Saksonova 2016, P50-51). We have seen in the above definitions that more emphasis was given to the impact of financial management in the economic benefit aspect it has for businesses. Nevertheless, those definitions rarely incorporate the business goals and strategies.

In the contemporary world, the emerging role of the financial management is related with the emergence of a financial service industry (Lazonick, 2010, p. 84) and the understanding that how much financial management is critical to businesses (Stanciu, 2013, P. 56-64). The capacity of businesses, now a days, to create cash in the

future highly depends on the stock value they have in the market (Fama, 1970: cited in Svetlana S & Svetlana S. 2016 p. 50-51). Taking this in to consideration, businesses now focus mainly on adding their market value. Businesses require to carefully follow, analyse the characteristics and structure of their finance so that they will be able to put and apply a sound financial strategy in both the short term and long term. This clearly requires a sharp and deep understanding of the financial system. Firm management can also take specific decisions affecting firm value.

In addition, a business will never be successful in the long term if it does not have the right policy in regard with its working capital. Here, there are three important elements that needs attention in managing finance. The first one is liquidity management and cash flow management. This is due to the reason that cash is considered as a bloodline for businesses to operate. The element includes long term asset acquisition which directs the long-term course of business. Whereas the third element involves issues with funding, capital structure and cost of funding. Generally, the poor financial management of owner-managers is the main cause underlying the problems of MSEs. Therefore, to successfully manage small businesses, its financial management activity should find a smart way to systematically approach and comprehend the use of modern financial instruments and technologies (Irena Jindrichovska I. 2013, p79).

#### **2.4.2 Importance of managing finance in MSE**

Business owners or entrepreneurs in small business sector usually seems to neglect the financial management aspect of their business or as often noticed, divert this task to a third person like accountant to take care of. When small business owners display inefficiency in dealing with financial matter and fail to realize their potential by themselves, it is reasonable to reach out professionals like financial advisors considering that this act is an attempt to protect the business from falling apart and to benefit from techniques of best practice of the professionals in financial management area (Geoffrey Lightfoot 1998, p. 4-41).

This does not mean however, that small enterprise owner-managers doesn't need to take time and focus on financial management in running the business. In fact there are cases where the reason is attributed to lack of knowledge and skill in the area of financial management which includes activities like book keeping, knowhow of

financial data collection in a way that helps to develop a set of financial information for analysis. The other reason could be that business owners are immensely involved in other aspects of business like managing people, sales purchasing and production.

In running a business, financial management is an important element that owners need to focus because, business financial assets, which are at the epicenter of every business, are managed and controlled within this scope. In the long term, investments in assets defines the course that the business will take during the business lifetime, but it will be difficult to be successful in long term if there is no an appropriate financial plan and policy to effectively manage its working capital (Irena Jindrichovska I. 2013, p. 80).

Recent studies show that small businesses are not limited in classical principles of a business which depicts growth and profit maximization as sole and only purpose of businesses. Rather objectives of these small businesses may go beyond. (McMahon, 1995, p. 21-34) in doing so, perhaps the most important element of a business entails decisions related with financial matters. In order for businesses to successfully pursue their operation or survive, sound financial decisions are required which in minimum keeps their existing level of wealth. Businesses simply engage themselves in continuous investment activities like following and adjusting depreciated or outdated capital and in some situations the business cycle itself brings with it change requirements where businesses are expected to do more than just follow up and adjustment order to survive (Puxty and Dodds, 1991 cited in Yusnidah I 2000, p. 46).

Therefore, be it poor performance showed by business owners in financial management activities or lack of financial management skill itself, small businesses, if not able to alleviate this problem, are doomed to failure. This is even if the owner does a good job or provides superior service in other functional areas like human resource, marketing etcetera, the financial aspect of the firm, if not managed sharply, still endanger the existence and or sustainability of the business. Most small businesses only know one-half of what it takes to succeed. The part they are missing usually is the financial management skill on how to manage and grow their business. hence, entrepreneurs or small business owners in fact are supposed to develop themselves with necessary financial management skill and are expected to actively engage in applying them to their businesses (Yusnidah I. 2000, p. 46).

## **2.5 Importance of Financial Records and Information to MSE**

Giving the necessary importance and consideration for financial information in managing any business (big or small) is crucial factor for success in business world. Any wrong decision regarding financial issues in a business could fatally lead to the failure of businesses. Especially, the consequence for small businesses will be severe given their limited financial capability and resource. This deadly impact is usually resulted from, entrepreneurs or business owners, lack of access to appropriate financial information before making decision which is usually due to a lot of issues they are engaged with from making payroll to buying products to selling products (S. Hatten (2006), p. 218-19).

There are a lot of reasons for small businesses, especially for those who are located in developing world that justifies the need for financial information. The overall economic political and social progress witnessed in these developing countries has increasingly attracted attentions over the last 20 years. In order for developing countries to continue this astonishing development sustainably, the need for availability of sufficient finance is inarguable. One source of finance that can sustain this growth and development could be through foreign direct investment. Attracted by these developments, investment decision makers would normally need financial information regarding the prospect business overall performance. But, knowledge about financial management in any of these countries is not extensive with the most prominent exception being China (Hopper et al., 2009, p. 469-514).

In addition, Firms face increasing pressure from banks and other fund providers as well as economy regulators to provide all sorts of financial information about their operations. Financial institutions can easily get financial information access in case of lending to larger businesses as these businesses have a regularly audited and certified financial information. This make the lending process much easier for the banks and at the same time help large businesses get the credit in a shorter period of time. In contrast, since hardly any financial information is readily available in case of small businesses, credit access from financial institutions is very tough (Berger and Frame, 2007; Petersen and Rajan, 1994: cited in Geoffrey Lightfoot 1998, p. 4-41). Therefore, developing the culture of recording, preparing and generating financial information's in small businesses is essential in contributing for the success.

## **2.6 Financial Management and Small Business Owners**

Business owners or entrepreneurs are able to acquire formal skills needed in managing finances. At the same time, they can also manage businesses using informal skills through wider moral and social conventions in ways that makes it even difficult to draw a distinction line between personal authority and business legitimacy. Research studies regarding business owner's management inclination generally and financial management approach specifically reveals that, informal kind of business knowledge which is derived from ownership shapes and influence owners code of conduct in such a way that external formal and professional advice is made of limited use or irrelevant.

When we came to owner's financial management skill, considering that some of the business owners do have some 'basic' knowledge of financial tools, studies in small business showed that application of these tools, given the limited knowledge, is rare and also doesn't significantly affect small businesses. But, on the other hand, absence of deep and real financial management skills in small businesses hampers the growth and development of these businesses in the long run. This is because, lack of application of some essential financial management tools constrain the firm's in many ways. These can be through having a wrong concept and assumption of 'return', 'wealth' and 'profit' without considering techniques like the discounted cash flow technique and other similar critical problems may also raise up (Yusnidah I 2000, p. 284).

Often, small business owners are well familiar with their own day to day business operations. This is despite the absence of formal report communication tool with in the firm on the overall performance of the business. This implies that most of small business owners run the business intuitively and has no logical explanation as for why they are doing the business in the way they are doing it. Hence, 'knowledge' of their businesses goes largely unexamined.

From the above we can infer that business owners consistently claim their knowledge of the firm's overall position which often leads them to undermine the need for formal systems and applications of financial managements. It has been observed that most of their knowledge of the business originates either from 'common sense' or attributed back to their ownership of the business. This usually puts the business future in the dark because there is no formal planning system and therefore decisions are usually made spontaneously. Especially, financial decisions are made in consideration of avoiding financial insolvency through allocating the business finance to different

activities and or through applying a strict control over expenses and payment procedures. This apparent problem that owners are not willing to use formal information proper decision-making to take place required reconciliation. Nayak and Greenfield, suggest that: "Although most MSEs were aware of their firms activities, information tended not to be formalized" (Nayak and Greenfield, 1992, p. 49).

Training programs and texts reviewed strongly suggests that small business owners need to be more forward looking and engage themselves in proactive and formal overall management style. This includes being able to have abroad view of the business and set strategic directions, being able to identify the business capacity and set achievable goals and objectives and being able to undertake the required operational planning and closely follow up the overall operation progress in regard with achieving the objectives. There is also reviews suggesting that small business owners are usually focused on short term goals, reactive in their managerial style, and that they make very little systematic use of the managerial planning and control techniques (R. McMahon and S. Holmes 1991, p. 23).

Recently, the tradition of using informal management tools has declined dramatically to the extent that now one can say it is becoming the new orthodoxy in research studies into financial management and small firms.

## **2.7 Financial Management Practice Differences in Large and Small Businesses**

Financial management practice requires a distinct approach when it comes to small businesses. This is not only because they have different resources, but also face various difficulties compared to large enterprises. (Moore and Yuen, 2001: Cited in Howard M., Alan Webb & John G 2016, p. 34) argues that in relation with businesses operation scale and complexity, considering small businesses as just simply a “downsized” version of a big company is wrong conclusion. Basically, majority of small businesses, particularly those in start-up stage tends to focus on identifying target market and customer, while large companies typically engage themselves primarily on developing a control system for ongoing business activities.

MSEs given their simple organizational structure has the characteristic of being more flexible, dynamic and adaptable to its surrounding. However, MSEs usually are disadvantageous when it comes to access to financial resources and is difficult for them to attain economies of scale. Small businesses therefore, are supposed to use their

resources efficiently through proper information and control systems so that they can stand against harsh competition they face from large businesses (Mitchell and Reid 2000, P. 385-390). Application of proper financial management systems within the business can support MSEs in helping to utilize the limited financial resource available effectively and efficiently. Thus, financial management is an important management function that supports the main business activities by providing information that is valuable for management decision (Foster and Young 1997; Burns and Scapens 2000: cited in Oro Lavia & Martin R. 2015, p 81-119).

Given their resource constraints, MSEs are often unable to afford or acquire a professional financial manager. Their lack of resources may also result in limiting their ability to train their employees on financial management skill and other necessary areas (Mitchell and Reid 2000, p. 385-390). Consequently, small businesses are forced to either use informal tools and methods in managing their finance or use less formal and less complex financial decision-making tools and systems than that of their larger business counterparts. Consequently, small business owner or entrepreneur gets limited information to be based for planning and making decisions leaving the fate of the business to his/her personal intuition and experiences (Quinn 2011, p. 337-357).

In relation to this, empirical findings show that if there is proper financial management application in MSEs, can reap the advantage of good performance in their business. Financial management and accounting techniques need to be adapted not directly rather the simplified version is necessary to implement in MSEs' (Welsh and White 1981). Changes in the size of the business also tends to change the application of financial management systems. Thus, simply taking the financial management approach applied in large firms and implement the same concept in the same manner with smaller version in small businesses seems insufficient. As Welsh and White (1981, 18) noted, "a small business is not a little big business"; this refers to the need for distinct adjustments to the financial management tools, in alignment with constrained resource of MSEs compared to large enterprises, is necessary (Oro Lavia & Martin R. 2015, p. 81-119). For instance, some studies show that, MSEs adopt financial management information systems only in a situation where working with large business partners or other external entities such as banks which require a certain amount of formal financial information. Unless and otherwise they do not use financial management information's as a tool or input for planning and decision making.

Given this knowledge, further study in the area of small business financial management helps MSEs overcome problems related with limited resource or other barriers that hinder them making effective and efficient use of resources available. Also, it can add value through developing more convenient tools for practitioners to be able to provide sufficient financial information for decision making and improve MSE performance. In addition, such application contributes in saving the limited resource of MSE by focusing only on the most suitable applicable financial management tools that are easily adoptable and are easy for implementation (Perren and Grant 2000, p, 391-411). Such studies would help also reduce the magnitude of MSE failure due to poor or improper usage of financial management techniques. In relation to this, it is also important to note that small businesses neither have their own research and development centers nor able to support financially research activities in this area.

In summary, the reviewed articles in this regard concedes the existence of direct relationship between the application of financial management system and company size. But, it also witnesses the existence of 'small' large firms where 'best practice' concept applied to a large firm works considering the wide and sophisticated nature of their business operations. In this case, it is an implied notion that the same problems and solutions that face a large organization are equally applicable to the smaller enterprise dismissing the size effect and ignoring the heterogeneity of small firms (Stanworth & Gray, 1991: cited form Geoffrey Lightfoot 1998, p, 130-137).

## **2.8 Cash and Working Capital Management in Small Businesses**

The following section deals with literature reviews regarding cash which is considers as the most liquid asset a business has, and the impact cash management system (cash flow) has on small businesses. Furthermore, this section also highlights working capital management and its importance for small businesses.

### **2.8.1 Importance of cash flow in small business**

Cash flow refers to the amount of money actually received (inflow) or released (outflow). This is, unlike to the concept of Income which is claimed when earned, even though cash is not received, and expense incurred although there is no cash out flow (Brigham, 1995). Cash flow is considered as a crucial concept in financial management since it shows the amount of cash in correspondent with exact real cash available. According to (Sheridan (1996): cited in Yusnidah I 2000, p. 428), cash on hand is the

most important asset available to businesses. For small business, it is usually considered as the life-blood of their business. Practitioners in financial management area usually describe the importance of cash referring it as 'cash is king'. (Williams, 1994, p. 307) states the importance of cash to small businesses as follows: *"If your cash runs out, your business will fail. It is as simple as that"*. In addition to this, (Petty et al. 1993, p.125-137) put cash inflow as the actual money that are readily available for reinvestment, while cash outflows are those transactions which directly affect businesses pocket when transaction occurs.

As part of financial management, small businesses need to manage their cash effectively given their limited resource. (Philip Campbell: cited in G. Longenecker, J. William and Leslie E., 2006, p. 312-347), a CPA and former chief financial officer in several companies stated that most business owners do not give emphasis to cash flow management resulting more business failures today than ever before. For this reason, it is necessary for small business owner to recognize the importance and understand the sources and uses of the firm's cash. Among the various tools used to manage firms finance, Cash flow statement deals with reporting the source of firm's cash and its use of the cash depicting where the cash came from and where it went

Business owners/ managers need to know the difference between the information obtained from company's income statement and its cash flows statements. While income statements show a positive (profitable) position of the company, it doesn't necessarily mean everything is going smoothly. In fact, companies may go broke and run out of cash. This is because, although profitable income statement, income statement doesn't consider the actual amount of cash out flow and cash inflow. In case the latter is less, the business will stand without adequate cash flows, leading to file bankruptcy cases. This shows that little problems, lack of cash flow management, could lead businesses to serious problems. Therefore, small businesses need to use the cash budget as a primary tool in controlling the amount of cash inflows and outflows. It helps the business managing its daily operations, avoid cash flow problems in case of opportunities for short term investments and cash needs (G. Longenecker et al, 2006, p. 312-347).

Businesses can achieve their objective of profit and welfare maximization of the company and shareholders through effective application and control of cash flow tool of the organization's financial management (krylov, 2005: cited in Y. P. Vetrov1, O. G. Vandina, A. R. Galustov, 2017, p. 428). Businesses financial problems can best be solved

using strategic financial management of cash flows. Strategic cash flow management can be considered as a part of the strategic financial management where the information obtained can be used in setting up and decision-making for long term cash flow objectives. This requires a deep analysis and study of cash flows internal and external factors that influence the overall financial process and, as a result, the financial situation of an organization. Generally, from the traditional financial management point of view, cash flow is considered as the most important financial management tools that decision makers should pay close attention rather than considering profit/loss and other secondary tools.

### **2.8.2 Importance of working capital**

The importance of controlling working capital emanates from its function which shows required working capital reconciling the gap between payment receiving date from customers, and payment date to their suppliers and their overhead costs. It is also related with decisions regarding short-term financing investment levels in various types of current assets. These decisions could be on making investments on short term securities, overdraft decisions, or considering extending and adjusting necessary terms of trade credits by taking in to account the firm's advantage. But, these decisions may not encompass areas of capital investment and financing decisions taking in to consideration that they belong to long term decisions (David S. & Nicholas W. 2006, p. 399).

The research study done by (Peel and Wilson 1996, P 14) regarding the application of small businesses capital budgeting and working capital shows that, generally a significant number of small businesses taken for study are found using quantitative capital budgeting and working capital techniques. In addition, the study showed that businesses were using discounted cash flow capital budgeting techniques, or those who minimized their stock levels or the debtors' credit period, on average are found to be practicing working capital management practices.

In addition, studies conducted by (García-T and Martínez-S 2007 and Thalassinou and Curtis 2005: cited in I Jindrichovska 2013, p. 80-82) through gathering data from 8,872 small to medium sized enterprises between 1996–2002 shows that, working capital affects profitability positively by decreasing inventories and the number of days for which their accounts are outstanding. Moreover, it helps increasing the liquidity of

the business thereby also increasing the firm's profitability. (Czarnitzki and Hottenrott 2011, P65-83) in their studies also examined the relation between working capital management and profitability of small businesses located in Germany by controlling for unobservable heterogeneity and possible endogeneity. This study showed the existence a non-monotonic (concave) relationship between working capital level and firm profitability, which means that MSEs have an ideal working capital point that maximizes their profitability. In addition, the study also witnessed that firms' profitability has an inverse relationship with their optimal level.

## **2.9 The Need for Financial Forecasting and Planning in Small Business**

Business owners need to come up with financial forecast and plan for their operation which serve as a financial road map of the company. Financial plans and forecasts may be needed for various reasons. For example, when looking for finance source, lenders and investors would want to know the business in terms of its financial prospects. They usually look in to the pro forma financial statements to decide the payback probability of the business. A small business consultant, (Paul A. Broni cited from J. Longenecker et al 2006) p. 331), stated the importance of preparing financial forecasting for a business in many scenarios like seeking finance from a bank or looking for a venture capital or debt financing. Because financial institutions, while considering investment/loan, need to find the financial forecast attractive enough promising the re payment of their investment/loan. Generally, businesses prepare financial statements to show the expected profitability of the business taking in to account estimated sales levels and expenses. They also show the source of finance (debt or equity) that is going to be used in running their operation and the source and availability of actual cash needed for their operation.

Preparing financial forecast, unlike historical financial statements like income statements, balance sheet and cash flow statements, is not a simple task. They pose a serious complexity and are even more difficult when it comes to small businesses that are newly established. This is because, for new businesses there will not be historical data available regarding the required amount of input materials, cost of goods, needed manpower, sales level etcetera in order for entrepreneur's base decision making. But, this information's can be obtained alternatively by attending related exhibitions at a trade show which creates the opportunity to contact and communicate with different business

entities in the industry. Contacting industry association also can be another way to get the necessary information for financial forecasting (Gentry, J. 1988, p. 41-57).

While forecasting, small business owner should consciously analyze every possibility the business may encounter and should come up with alternative solution plans. For example, a business owner should have a plan not only how to increase its sales level but also it should put a clear measure of actions in case sales are too below expected or experience unprecedented sales growth. In addition, (J. Longenecker et al 2006 p. 332) states that the forecast should clearly state crucial information's like the amount of money required, how it is determined, how will it be used and the length of repayment time & repayment method of the debt. Only careful financial planning can provide answers to these questions.

In addition, because financial forecasting involves working capital, which is limited for small businesses, it makes the activity so critical and error intolerant. It becomes more serious when the business on spot is new business making asset and financial requirement estimations difficult. Even for old business, forecasts are encountered with many surprising situations. While preparing financial forecast, an entrepreneur may gather relevant information's from different sources reaching from banks, trade associations, related companies financial forecast, publicly available data, common sense and educated guess. In addition, while forecasting, a special attention to the owner's personal financial situation is needed. This helps clearly draw the line between the money disposed for the business and for personal expenses (Hyvönen, J. 2005, p. 97-120).

According to Brigham, F. E. & Ehrhardt, C. M. (2013), failure to do so will create an intermixed financial management system between the business and personal monetary flows thereby raising cash flow problem in the business. Neglecting personal expenses in incorporating to financial forecast is often prevalent in small businesses. This, in the long run, absorb a big amount of personal wealth locked up in the business. Former SBA director Hector Barreto explains this: small businesses often do financial planning reactively, instead of acting proactively, when problem raises, or circumstances force them to do so. Although basic financial forecasting is not time consuming, they are usually busy engaging themselves in other aspects of the business.

Generally, according to (Norman M. and W. Zimmerer 2003 and J. Longenecker et al 2006 p. 350) the process requires the owner to have wide knowledge of the business environment and is critically important considering that financial forecast serves as basis

for raising capital. The overall all approach to forecasting usually depends on owners speculation skills in determine financing requirements. This activity is usually prone to overprotection or under projection of the needed finance. Therefore, to avoid this from happening, its necessary to follow these steps:

The first is developing realistic sales projections. Owners usually make the mistake of setting overstretched goals, especially when it comes to forecasting future sales. It is always important to clearly state the estimated number of unit sales taking a reasonable market consideration. Owners also fall in the mistake of expecting unrealistic profit margins. The profit margin estimation should not be both over estimated and under estimated. It should take in to consideration of the industries average margin with similar revenues and numbers of employees. There may be an assumption that the business will grow faster than the industries average and will able to achieve economies of scale hence gross and operating profit margins will improve. Although often the reverse, business growth leads to an increase in its fixed costs thereby profit suffer in the short run is true. The position taken in achieving quick economies needs to be explained in the forecast. The other issue that need consideration is, avoiding the forecast to be limited to an income statement. It is often noticed that Entrepreneurs frequently provide only income statement projections excluding balance sheet projection and cash flow statement. But financial institutions are specifically interested to see those planes in print, and they particularly need to evaluate the businesses cash flows. There should be also a match between what is stated in the paper and what is there on the ground. Difference between these two raises an issue of reliability for the business. In doing all these, owners should be careful in providing too much information creating information overload. Often its advised to present the most likely projection in comparison with the breakeven point of the industry. Finally, at least a monthly follow-up plan must be organized to check the prepared the pro forma financial statements against actual results (S. Hatten, 2006 and J. Longenecker et al 2006, p. 351).

## **2.10 Financial Sources of MSE**

For any business owner finding out how to fund its business operation is critical. Finding finance source is not an easy task especially in today's turbulent economic situation. Small businesses, especially those in less developed countries or those just starting out, are the most to suffer from finding finance sources. Because, Many formal

financial institutions are less interested in providing funds to start-ups, while venture capitalists need even larger return margins, private investors have grown cautious limiting and focusing their investment on good track records and fast-growth businesses (Norman M. and W. Zimmerer (2003, p. 408).

Thus, businesses are expected to act more professionally and smartly to successfully secure and maintain finance to conduct their business activities. In doing so, there are four basic determinants which determine businesses finance. These are: the firms' economic potential for growth and profit, the company's size and maturity where the more the firm is large and old the more has the possibility of access to finance, the nature of its asset where the more tangible assets the business have the more preferable by financing institutions and finally the personal preference of the business role as for the combination amount of debt and equity finance to the businesses finance plays an important role in making financial source decision (Justin G. Longenecker et al (2006 p. 359).

According to (Gebrehiwot and Wolday, 2004:54) businesses can source and secure their funds internally through retaining earnings and personal savings or can approach external bodies like formal financial institutions including banks and other informal and traditional institutions in financing their business. In case of firms or countries where developed primary and secondary capital markets are not available for access, either because of the absence of the market structure and system in general or the limited capability of the business to engage in this kind of market, the only option open for this firms will be through direct borrowing of fund from formal or informal financial institutions. But often their chance of access to bank loans for small businesses are near to zero due to absence of proper financial management tools to consider and evaluate in order for banks to make lending decision. On the other hand, unable to invest their savings in high-return/high-risk investments via an organized market, investment for small investors is only possible for "creating one's own enterprise or financing the enterprises of close friends and relatives whose skills and performance can be monitored" (Fafchamps, 1994:8-9).

In Ethiopia, the available financial institutions (debt) for businesses include conventional banks, micro finance institutions MFIs, cooperatives, government projects, and other informal lenders, as well as trade credit. Whereas equity finance in Ethiopia is arguably limited due to the reason one could expect much more equity finance to be

forthcoming in a situation where equity holders could liquidate their holdings quickly and with relative ease when they want to (Gebrehiwot and Wolday, 2004:54).

Finance sources can be categorized differently depending on various parameters. For this study sources of finances are classified depending on the degree of formality of operating within a given financial system. Thus, the sources of finance are classified as formal, semi-formal and informal sources of finance.

### **2.10.1 Formal financial sources of MSE**

Formal sources of finance are described as those institutions that are subject to banking laws of the country where the firm is located and are engaged in loan extension to customers and diversified financial intermediation (Tewodros Giday, 2005: cited in Ermiyas W. 2011 p. 18-21). In the Ethiopian, the formal finance sources include Commercial Banks (private or public owned), Development Bank of Ethiopia, and Construction and Business Bank. Commercial banks are engaged in giving financial service activities for businesses and any firms operating in any economic activity through deposits mobilization, working capital and loan extension for enterprises operating in any economic sector, and financing promising projects for a range of time including short term, medium term and or long-term period. Invariably commercial banks assess the credit worthiness of the applicant using the traditional five parameters, namely: capacity, collateral, capital, condition and character.

Conventional banks in Ethiopia are not engaged in financing activities for small businesses regardless of the number, nature, and type of loan extension criteria. The reason can be traced to absence of financial management tools in small businesses that banks require for loan evaluation. Also, it could be lack of commercial banks capability especially the availability of branch network, extensive and dense enough to effectively reach *MSEs* throughout the country (in rural areas in particular). (Gebrehiwot and Wolday, 2004:55).

### **2.10.2 Semi-formal financial sources of MSE**

Semi-formal sources are those institutions that are engaged in financing activity which are mostly registered as non-governmental organizations NGOs and MFIs with special charter. In Ethiopia NGOs are restricted to make financial activities at least officially, since the issuance of micro-finance law, proclamation number 40/1996, which requires those involved in the provision of micro-finance to be established as share

companies (owned only by Ethiopian nationals). This law of action prevented NGOs not to engage directly in credit and savings activities. This has created a conducive opportunity and environment for MFIs and thereby in the last years, the micro-finance industry showed remarkable growth in terms of outreach and performance (Gebrehiwot and Wolday, 2004:55-56). MFIs support micro and small businesses from initial start-up phase throughout their growth and development stages by providing loans which will be difficult to get from the main banking system of Ethiopia.

MFIs play's a crucial role in reducing poverty through supporting and facilitating finance for *MSEs*. But in doing so MFIs face a serious challenge regarding responding to the huge demand available from *MSEs*. There are currently not enough MFIs that qualify to receive financial support. Hence capacity building activities are required from MFI side. Plus, the fact that the market is at its enfant stage of development, and thereby offer opportunities only for substantial returns to limited firms. MFIs must commercialize to realize its full potential; only then will it be able to satisfy the needs of *MSEs*. MFI industries should be lucrative enough to attract private investors willing to participate in this venture of significant social and economic benefits. Indeed, MFIs were important component for meeting the United Nations' Millennium Development Goals for 2015, with the Millennium Declaration calling for "micro-finance projects which meet local community priorities".

### **2.10.3 Informal financial sources of MSE**

The informal sources of finance, opposite to the formal and semi-formal financial institutions, do not have clear structure and category. The study has included some of the informal sources like credit and saving, unions, cooperative societies, traditionally best known as '*iqqubs*', '*idir*', money-lenders, friends and relatives, trade credit suppliers are in this category. This sector is the best option *MSEs* have in case access to formal and semi-formal financial institutions are not possible. Informal sources are important source of initial as well as working capital requirement of *MSEs*. Getting access a significant amount of money is most evident in informal sources than formal or semi-formal sources (Martin *et al.*, 2001:30). The following informal financing institutions are widely operating in Ethiopia.

**Credit and saving unions:** These institutions are primarily engaged in giving financial support for salary and wage earners usually located in urban centers, there by excluding

the bulk of *MSE* operators. Although there is a continuous increase in the number of credit and saving institutions and members, it has entirely excluded *MSEs*.

**Cooperative societies:** are organized in a group formation giving financial service for working institutions. In the Ethiopian context, these types of financial institutions are long associated as a political tool and hence are not probusiness oriented. therefore, many of business owners are reluctant to reach this kind of organizations for financial support. (Wolday, 2002).

**'Iqqub':** A study by (Mulugeta Y. 2011, p. 28) who examines the role and functioning of the '*iqqub*' in Ethiopia states, that '*iqqub*' is a type rotating savings association with an element of chance in the awarding of the amount in each cycle. Basic principles and underlying procedures are analyzed in general and for a number of specific cases. The '*iqqub*' is conceived as a form of traditional savings institution:

**'Idirs':** are indigenous institutions collecting a specified set of money from their members to pay out a specified lump sum of money and assistance to a member, at his/her bad times especially at times of mourn. Despite the need to mobilize resources kept by the '*idir*', they, so far, are not reported that they provided loan or assistance to business activities (Tewodros Giday, 2005).

**Money-lenders:** covers a wide range of credit arrangements that differ across countries, with interest ranging from zero to as many as 100%. Discussions with traders operating at '*Mercato*' has revealed that there are money-lenders both individually and employees in branches of some government institutions that provide them with finance at about 10-15% per month. Due to high cost of borrowing, *MSEs* use money-lenders as a last resort. Most of the informal moneylenders base their lending disciplines on a first-hand knowledge of the borrower (Nisanke *et al.* cited in Gebrehiwot and Wolday, 2003:6).

**Own savings, relatives, and friends:** personal savings is by far the most common source of equity financing used to start a new business. it gives the owner a considerable level of freedom as to decisions related with the business. Next, friends and family come in distant second. They provide almost 80 percent of start-up capital beyond the entrepreneur's personal savings. using this kind of financial source has risk of putting more than just their financial futures on the line, it may also jeopardize the relationship (J. Longenecker *et al* 2006, p. 365).

**Trade credit suppliers:** are significant sources of informal credit in an enhanced credit

rating system. Trade credit refers to loans suppliers extend to their customers in connection with product sales. They supply either input or cash advances to *MSE* operators. Enterprises may receive trade credit either as a substitute for or complement to bank credit. Trade credit has attraction feature of not being guaranteed by mortgageable assets, which is advantageous for enterprises lacking collateralizable assets. Enterprises could resort to trade credit both as a means of financing purchases (i.e., receive trade credit from suppliers) and promoting sales (i.e., grant trade credit to customers). In the context of Ethiopia, it is reported that the practice of providing trade credit exists for either purpose (Tegene et al, 2010, p.37). However, trade credit suppliers are unwilling to extend trade credits.

## **2.11 General Problems and Factors Affecting Financial Management of MSE**

MSEs are the backbone of the economy constituting a significant part of total employment in many of developing countries. (Broom and Lengenecker 1975, Haswell and Holmes 1989, Bates and Nucci, 1989, and Watson and Everett 1996: cited in Solomon T. 2017 p. 19-20), in their studies presented that large businesses are more successful than small businesses. Although their huge potential contribution for economic development, small businesses face extensive growth and development problem especially in regard with access to formal financial sources, which is mainly the reason for their underdevelopment. In addition, (Chittenden et al., 1999, Broembsen, 2003 & Hashim and Wafa, 2002: cited in Solomon T. 2017 p. 19-20) stated that, the main reason for the failure of small businesses resides in their poor financial management applications. (Gaskill and Van Auken, 1993, 18-31) added that, most of the prominent problems that are causing small businesses failures in US and UK is related with internal problems like insufficient capital, poor working capital management and inadequate long-term financing, poor cash flow management, inventory control and generally absence of sound financial management practices.

In addition, according to (Tushabomwe K, 2006, p. 27-35), the main reason for Poor performance of small businesses in Africa is absence of well managed recordkeeping system and owners/ managers lack basic business management skills like inventory management, financial management, human resource management and marketing). This leads in to a complex and confusing work environment where tracing appropriate cost and profit of the business becomes difficult. Given these, the possibility

of business failure due to lack of sound financial management practices became a serious issue that seeks special attentions.

Considering all the above, some studies suggest that small businesses will be benefited if legal and financial institutions are developed in a way that especially helps small firms access to finance. In addition, even in the absence of a well-structured and develop financial institutions, some financing tools like leasing and factoring can be used in enabling greater access opportunity for small firms. This will help adjust the widening gap between large and small businesses creating a fair play ground and competition. (Thorsten B & Asli D., 2006, p. 2931-42).

## **2.12 Factors Affecting Financial Management Techniques**

We have seen in the above discussion how much financial management practice of a firm affects the overall success of the business. Therefore, to have a sound financial management strategy, first we should be able to identify the factors that can possibly affect the financial management practices. To this regard, both Financial and non-financial motives can affect the financial management approach in different ways. For example, some researches revealed the important contribution both financial and non-financial motives have on cash flow, which its importance is discussed before. The study showed the impact owners / entrepreneurs personal characteristics and employees' attitude towards financial-orientation has resulted in the application and utilization of 'cash flow per piece' method instead of 'cash flow per hour' while making decision for investment opportunity of machinery. Similarly, other non-financial motives which includes improved image, increased owner manager's self-satisfaction and increased production flexibility has an impact in financial management activities.

This relationship between motives and financial management approaches in the case firms, however, is not conclusive. This is because, it is difficult to exactly identify and trace the owner-managers' financial motives which lead to his/her financial decisions and also the motives that were claimed to have triggered their decision-making are not the real motives in light with the financial management theory. For example, for some business owners, increase the firm's profit was meant to be the aim to receive a satisfactory level of net cash flow (Yusnidah I., 2000, p. 282). Other study findings state that, the most important factor affecting financial management practice

is capital size. This is in a sense, application of some financial management techniques are mostly related with the availability of capital.

According to (Baxter and Chua, 2003: 108 cited in Nadia A & Catalin N 2012, p. 271-272) the most important elements that create difference between small businesses in different countries include national culture, legislation, and historical background. Accordingly, financial management practice is becoming a highly situated phenomenon affected by the above-mentioned conditions that are specific to given times and places. Therefore, this creates demands for further study regarding the influence of various settings on management accounting systems.

## **CHAPTER 3: RESEARCH METHODOLOGY**

A research methodology, providing an overview of the approaches and methods applied, was used in this thesis to analyse the potential impacts of financial management practice on growth and development of MSEs. This chapter discusses procedures and activities under taken, focusing on the study's research design, questionnaire design, data collection, sampling strategy, data processing and analysis and instrument development. Besides, the section deals with a discussion on the ethical issues and the study area profile.

### **3.1 Research Design and Methodology**

“Research design is the conceptual structure within which research is conducted; it constitutes the blueprint for the collection, measurement and analysis of data” (Kothari C.R. 2004: p. 31). In other words, it helps us set up the road map as for how to identify the relevant method in gathering the necessary information and which sources are used in collecting the data. It also enlightens us regarding the target population understudy and the sampling strategies needed to conduct the study. Above all it ensures that the study would be relevant in addressing the research problem the study tries to answer and that it uses feasible procedures.

The same author has classified types of research in to: exploratory (formulative) which focuses on finding ideas and insights, descriptive (diagnostics) which deals with determining the frequency with which an event occurs and or explaining the characteristics of an individual, group or situation, and explanatory which is about determining the cause and effect relationships.

Taking the above, the researcher has used a descriptive and explanatory research method to best conduct the study. The use of Descriptive type of research was aimed to understand the current situation of MSEs in relation with financial management practice and applications. Whereas the major purpose of using explanatory research was in order to estimate & explain the various relationship that exist between variables that affect the growth and development of MSEs. Thus, using these research designs, the study describes and critically assesses the impact of financial management practices on growth and development of MSEs.

Moreover, in this study, a quantitative approach, that addresses research objectives through empirical assessments involving numerical measurement and analysis, of doing research was employed.

### **3.2 Sources of Data**

In this section, the various types of data resources which were implemented in the study were discussed. Generally, the study employed both primary and secondary sources of data collection.

#### **i. Primary Sources**

To realize the study target, the study used well-designed questionnaire as best instrument to collect the necessary data required. Babbie (2004) questionnaire is a document containing questions and other types of items designed to solicit information appropriate for analysis. Questionnaire for quantitative research is usually designed with the intention of collecting information that reflect strength of attitudes, perceptions, views, practice and opinions.

The questioner was designed first in English language but was translated in to Amharic language (which is the national language of Ethiopia) and strictly forwarded to the owners or managers of the micro and small business enterprises. The reason behind choosing business owners or managers is the assumption that, business owners or managers have an overall view of the business including, but not limited to, the financial area of the business and that they usually are directly responsible for financial decisions in MSEs. The questionnaire collected data from MSEs owners/ managers through physically addressing them.

The questionnaire was developed by taking in to consideration research problem the study wants to address supported by literature reviews made. The data instrument used by the study was structured and closed questionnaire. 13 close ended questions were developed to avoid complexity for respondents and ease coding that follows data collection process. These close ended questioners involve demographic and business-related sections which are multiple choice and dichotomous in nature.

In addition, A Likert scale, which is the most widely used approach, questioner was designed. The Likert scale measures financial management practice application rates of MSE business owners/ managers. The most common scale, which is 1 to 5 scale often being 1 = strongly disagree, 2 = disagree, 3 = I do not know, 4 = agree, and 5 = strongly agree was considered in designing Likert scale questioners. Taking this, the researcher adjusted the labels in a way that fits the question asked as follows: 1 =Never Applied, 2 = Not Applied, 3 =Somewhat Applied, 4 =Applied and 5 = Strictly applied (Bryman and Cramer, 1994).

The Likert scale consisted four sections which are: general financial management approach section (policies, rules and regulations, recording, reporting, follow ups and work in capital management), financial management skill section (training, financial management knowhow, professional service), financial data usage and application (Fund sourcing, planning sales, budgeting, investment decision, control mechanism, AIS) and growth and development (performance).

## **ii. Secondary Sources**

Secondary data sources were obtained from various related literature reviews including books, journals, pamphlets, office manuals and circulars were used to provide additional information where ever appropriate. Besides, different published and/or unpublished government documents, websites, reports and newsletters were reviewed to enrich and provide the study a firm background.

## **3.3 Sampling Strategy and Procedures**

The target population area selected for this study was Addis Ketema sub-city. It is one of the 10 sub cities found in Addis Ababa city. The purpose of choosing this area, among others, is mainly due its proximity and convenience nature of the population for the researcher to collect the necessary data for the study.

*MSEs* in this sub-city are engaged in different developmental oriented sectors which include textile and garment, construction, food processing, cobble stone, metal and wood works, municipal services, urban agriculture, and others. Among these sectors, the researcher confined the target population for the study in to: textile and garment, food processing and metal and wood work sectors. The reason behind drawing this sampling frame lies on, first, these three sectors take the lion share of micro and small businesses operating in the sub city, absorbing significant number of operators, which helped the researcher to easily access and collect the data required. Second, some of the sectors are so minimal and are widely distributed throughout the sub city that makes accessibility difficult (Tegegne and Meheret (2010:36-37).

### 3.3.1 Sampling technique and sample size determination

Determination of sample size usually depends on the nature of the population to be sampled. Here in this study, the total population of this study is 896 enterprises which is a finite population. It includes food processing (375), textile and garment (314) and wood and metal work (207) according to Addis Ababa city up to August 2015 (AAMSEDA, 2015). Taking this in to account, the researcher used the commonly preferred and frequently used approach of determining the sample size necessary by specifying the precision of estimation desired (C.R. Kothari 2004 p. 175- 180).

Hence, the following formula was implemented taking the researchers interest to estimate a sample size with 95 percent confidence level ( $z_{\alpha/2}=1.75$  from z-distribution table) and accepted 7 percent tolerable error (e). In addition, the researcher used the most conservative sample size i.e.: 50 percent success proportion (p) and hence estimation proportion of failure will be ( $q=1-p$ ). Then, substituting this value in formula:

$$n = \frac{z^2 \cdot N \cdot p \cdot q}{(N - 1)e^2 + z^2 \cdot p \cdot q}$$

Where, n = sample size required

N = number of population = 896

p = estimated success proportion = 50%

q = estimated failure proportion = 50%

e = margin of error = 7%

Z = confidence level = 1.96 for 95% confidence

Hence, Applying the formula:

$$n = \frac{1.96^2 \cdot 896 \cdot 0.5 \cdot 0.5}{(896 - 1)0.07^2 + 1.96^2 \cdot 0.5 \cdot 0.5}$$

$$n = 160.96 \approx 161$$

Since the above sample size is more than 5% of the total population and that samples are taken once without replacement in addition to over or under estimation, the researcher wants to check its objectivity by applying the concept of finite population correction factor (formula) as follows:

$$N = \frac{(z_{\alpha/2})^2 pq}{e^2} \times \sqrt{\frac{N-n}{N-1}}$$

$$= 161 \times \sqrt{\frac{896-161}{896-1}}$$

$$= 145.9 \approx 146$$

Therefore, as shown below in table 3.1, 146 MSEs were selected proportionally from the total population according to size of each stratum. Then the sample units from each sub sector were taken using a non-probability sampling method called convenience method.

**Table 3. 1 MSE Sample size to be taken**

MSE Sector	Total Number	Percentage %	Sample Units
Food processing	375	42	61
Textile and garment	314	35	51
Wood and metal work	207	23	34
Total	896	100	146

### 3.4 Reliability Test

A test of reliability measurement called “Cronbach Alpha” is applied to measure if the instrument used provides consistent result. The result is usually expressed as a correlation coefficient, which measures the strength of association between variables where coefficients of .90 or greater are nearly always acceptable, .80 or greater is acceptable in most situations, and .70 may be appropriate in some exploratory studies (C.R. Kothari 2004 p. 74). With this consideration, table 3.2 below shows a 0.939 reliability result which is nearly always acceptable. This is because, the instruments were developed based on research questions and objectives and hence it is possible to collect necessary data from respondents.

**Table 3. 2 Result of reliability test**

Reliability Statistics	
Cronbach's Alpha	N of Items
.939	36

### 3.5 Data Analysis and Presentation

Once the raw data is collected through the questionnaire, quantitative methods of data analysis is used. A descriptive statistical analysis method was used first followed by inferential analysis. Descriptive statistics allow researchers to present the current status of a certain phenomenon (Kothari, 2004 P 2). It involves gathering data that describes events and then organizes and describes the phenomena using tabulation, graph or chart methods. As a result, data obtained via the questionnaire were tallied and frequencies, percentages, mean, median and standard deviation values were applied and presented. In addition, according to (Abdulah R. 2010 p. 465) the following performance grading criteria, in table 3.3 here below, was applied to Likert scale questions forwarded.

**Table 3. 3 Performance grading criteria**

Performance Grading	Criteria		
	Mean	Median	Cumulative
High	3.6 & Above	4 & 5	80% & Above
Acceptable	2.6 - 3.6	3	60% - 80%
Improvement required	less than 2.6	1 & 2	Less than 60%

**Source:** *Abdulah R. (2010)*

On the other hand, according to (Zikmund et al ,2010 P 415), inferential statistics help us to deduce the characteristics that exists between various variables from the data through providing various tools of analyzing the relationship among them i.e. how several independent variables might explain the variance in a dependent variable. Hence, This study employed correlation and regression analyses. According to Kothari (2004 p. 139), the Pearson correlation analyses is used to show the association among variables (dependent and independent). It is the most commonly used statistical tool by researches for obtaining an index of the relationships between two variables keeping linear relationship between the variables and therefore, correlation analysis is used to test hypothesis. The value lies between  $\pm 1$  where positive values indicates positive correlation between variables, negative value indicates negative or inverse correlation between variables and zero indicates no correlation. In addition, interpretation criteria's presented in table 3.4 below was used to interpret the correlation result obtained.

**Table 3. 4 Interpretation of correlation coefficient r**

Range	(-r)	r
1	Perfect Negative	Perfect & Positive
1 – 0.7	Strong & Negative	Strong & Positive
0.69 – 0.5	Significant & Negative	Significant & Positive
0.49 – 0.3	Weak & Negative	Weak & Positive
0.29 – 0.1	Low & negative	Low & Positive
0.09 – 0.01	Negligible and Negative	Negligible & Positive
0	No Linear Association	No Linear Association

**Source:** (Alwadael, 2010)

The regression analysis, which according to (Zikmund et al ,2010 p. 567) is used to explain the relationship between variables. In our context, it is implemented to examine the impact relationship among three independent variables with MSEs growth and development in terms of employment growth, market share and profit growth. In this study, regression and correlation analysis which help to establish relationships as well as impacts among variables were applied and presented by using tables, charts, and diagrams followed by conclusions. The researcher used statistical analysis program called statistical package for the social sciences SPSS in applying the above-mentioned methods.

### **3.6 Variable Measurement**

This section specifically deals with as to why the researcher took certain variables than others in order to determine or analyze the impact of financial management practices on MSEs.

#### **3.6.1 Dependent variable**

The study used MSEs growth and development measured in terms of profits, market and number of employee's growth as the dependent variable. This is according to (Walker and Brown (2004) cited in Tiruneh 2011 p. 13), although there are various measurement tools for growth, traditional measures of business performance have been based on employee numbers or financial performance, such as profit and market share.

### 3.6.2 Independent variables

The study took financial management approach, financial management skill and financial data usage and application as an independent variable. This is, according to (Solomon T., 2014, P 19-20) among the important activities that affect financial performance are, the availability financial management control and reporting mechanism. Meanwhile, (Savina & Saksonova 2016, p. 50-51) states that, in order for businesses to achieve their goals, financial management practices of planning, implementation, control and management decision-making activities are crucial. In addition, according to (Irena Jindrichovska I. 2013, p. 79) a business will never be successful in the long term if it does not have the right policies, rules and regulations for activities like liquidity management and cash flow management, funding and capital structure while finding a way of systematic approach and comprehend the use of modern financial instruments and technologies. On the other hand, (Yusnidah I 2000, p. 284) states that lack of application of some essential financial management tools constrain the firm's through having a wrong concept and assumption of 'return', 'wealth', 'profit' and generally the business performance. Plus, absence of deep and real financial management skills in small businesses hampers the growth and development of these businesses in a sustainable way. Similarly, according to Hatten (2006, p. 218) the laxity, negligence and lack of attention to financial management practices by business owners is that usually tend to become deadly at the end of the day.

### 3.7 Model Specification

Based on the conceptual relationships described above and given the nature of our data which is categorical and closed, a regression model and a statistical software called, statistical package for the social sciences (SPSS) techniques were used to analyze the data.

The regression model to associate and identify the impact of financial management approach, financial management skill and financial data usage and application on MSE growth and development (growth in profit, market share and employment) use linear regression model as presented below:

$$\Delta Y_i = a + \beta_i X_i + \epsilon$$

Growth & Development in (profit, market share & employment growth) =

$$a + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3$$

Where by  $\beta_1$ ,  $\beta_2$ ,  $\beta_3$  and  $x_1$ ,  $x_2$ ,  $x_3$  were represent parameters of estimation of coefficient financial management approach, financial management skill and financial data usage and application respectively, while  $a$  and  $\epsilon$  were the constant and error terms for variables, respectively.  $\Delta Y_i$  was also growth and development of MSE measured in profit, market share and employment growth.

### **3.8 Research Ethics**

According to Creswell (2003) as researchers anticipate data collection, they need to respect the participants and sites for research. Research code of ethics is a set of guidelines that states the standards and operating procedures for ethical practices by the researchers. Some of the ethical issues that arise during the research stage.

In this study, researcher does not put participants at risk and respecting the right to voluntary participation so that individuals are not coerced into the research study getting permission from authorities to study participants at given research site. I obtained informed consent from participants, considering to harmful information being disclosed during data collection.

In the analysis and interpretation of quantitative data, issues of good ethics are also considered and researcher should follow protecting the anonymity of individuals, roles and incidents in the study thesis, discarding of data after a given period of time so that it does not fall into wrong hands, providing an accurate account of the data analyze, use unbiased language when describing participants, I do not suppress, invent, or falsify findings, report the details of the research fully and honestly.

## **CHAPTER 4: DATA PRESENTATION, ANALYSIS AND INTERPRETATION**

To facilitate ease in conducting the empirical analysis, a statistical program used for the analysis and presentation of data called Statistical Package for the Social Sciences (SPSS). The results of descriptive analyses are presented first, followed by the inferential i.e. regression and correlation analysis to better explain the impact of financial management practices on growth and development of MSEs in *Addis Ketema* sub-city. Data was collected from business owners or managers of MSEs found in the sub city.

One hundred forty-six (146) questionnaires were distributed across the three sectors found in the sub-city, out of which 139 were completed and retrieved successfully, representing 95% response rate. Out of the 146 questionnaires administered 51, 61 and 34 were distributed to textile and garment, food processing and wood & metal work respectively. The number of questionnaires retrieved from textile and garment, food processing and wood and metal work are 49, 60 and 30 respectively. This represents a response rate of 96 %, 98 % and 88 % for textile and garment, food processing and wood and metal work respectively.

Generally, this section is organized in a manner where first, the general information about MSEs were presented and analyzed followed by, inferential i.e. regression and correlation (Pearson) method of data analysis.

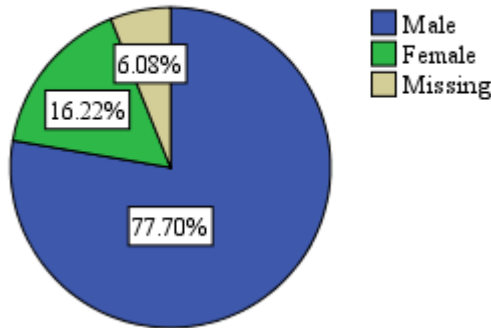
### **4.1 General Profile of MSEs**

This section describes the current status of MSEs taking various parameters. Based on the characteristics of these general parameters and by relating these with the financial application of MSEs using inferential and correlation analysis, which is done later, this section serves as a takeoff ground for analyzing the data obtained.

#### **4.1.1 Gender distribution of MSEs**

The figure 4.1 below reveals that 77.7% of the selected sample populations were males and 16.2% were females while 6.08% of the respondents were missing. This indicates that most of the owners of MSEs were found to be males, hence, the involvement of females as an owner or manager was limited.

**Figure 4.1** Gender Distribution of MSEs

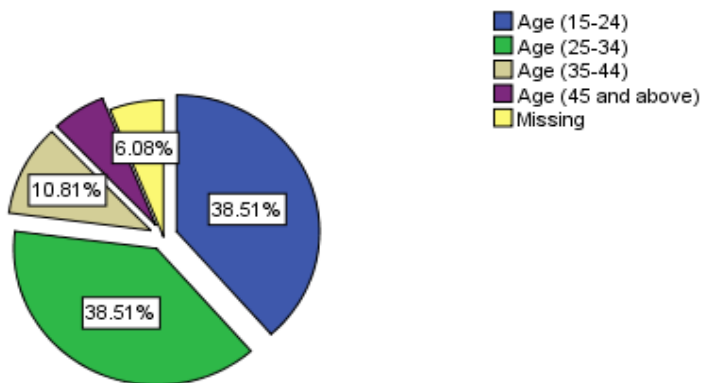


(Sample survey, 2018)

#### 4.1.2 Age distribution of MSE owners or managers

The age of the workforce varies usually from developed country, which is prone to more old age work force, to developing countries dominated by a younger work force. As Ethiopia is among the developing countries, the survey data collected regarding the age distribution of MSEs confirms domination of young age group work force. Displayed here below in figure 4.2, approximately 77 % of the respondents are found to be between the age of 15-34 showing a considerable engagement of young work force in MSE business. Meanwhile, 10.81 % of the sample population is between the age 35-45 and only 6.08 % is above the age 45. The remaining 6.08 % belongs to the non-respondent portion.

**Figure 4.2** Age Distribution of MSE Owners or Managers

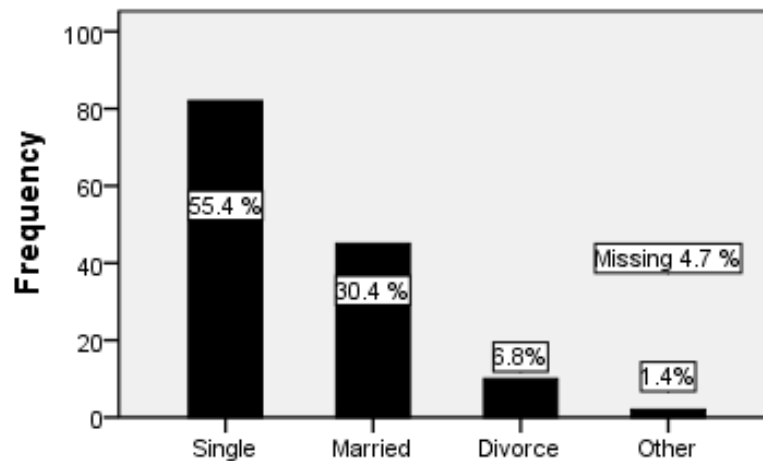


(Sample survey, 2018)

#### 4.1.3 Marital status of MSE owners or managers

The figure 4.3 below clearly shows that most of the respondents are single (55.4%), followed by married (30.4%), and divorce (6.8%). Elizabeth G. 2000 revealed that married peoples tend to be unsatisfied with their financial status than their single counterparts. Given this, large number of single MSE owners or managers has its impact on financial decision making and risk taking.

**Figure 4. 3** *Marital Status of MSE Owners or Managers*

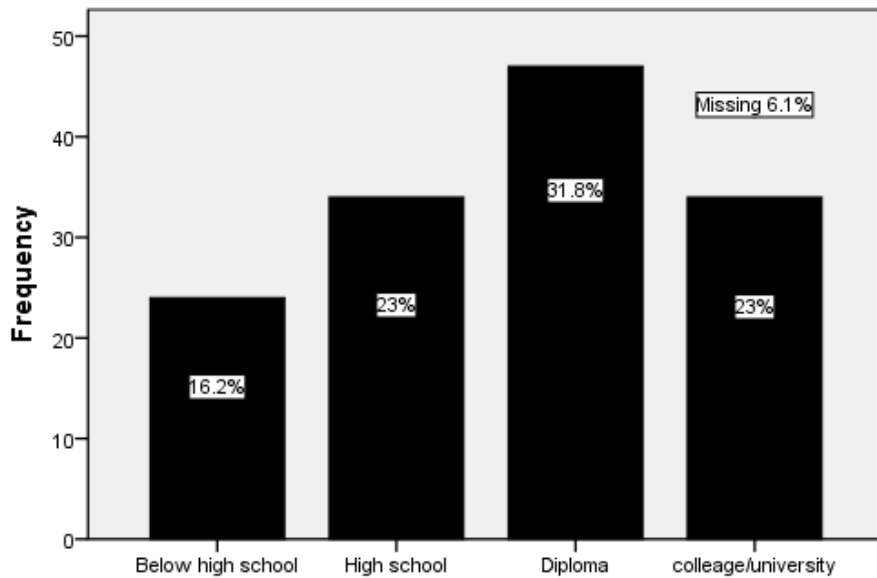


*(Sample survey, 2018)*

#### 4.1.4 Educational status of MSE owners or managers

The level of education has a significant impact not alone in business areas but also in every aspect of our life. It has a direct relationship with growth and development by harnessing the understanding and application of various concepts. Figure 4.4 here below shows that 31.8% of the respondents have a diploma degree followed by University degree holders and high school attendants both having 23 % each. Meanwhile, those respondents with educational level below high school degree are found to be 16.2% of the sample population. 6.2% represents the percentage of non-respondents in this study.

**Figure 4.4** Educational Status of MSE Owners or Managers

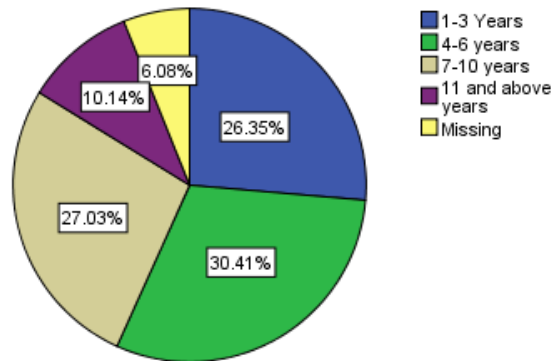


*(Sample survey, 2018)*

#### **4.1.5 General business experience of MSE owners or managers**

The more individuals or business owners spent time with in a business, the more they acquire various set of business soft/ hard skills and broaden their understanding of business environment. This skill can also be manifested in the area of administering businesses financial issues like widening finance sources, effective finance forecasts and the like. Keeping this in mind, the survey data in figure 4.5 here below for this study showed that, 30.41% of the sample population has a total business experience of 4-6 years, followed by 23% having 7-10 years of experience. 26.35% of them have 1-3 years of experience and only 10.14% of them are found to have more than 10 years of experience.

**Figure 4. 5** *General Work Experience of MSE Owners or Managers*



Source: (Sample survey, 2018)

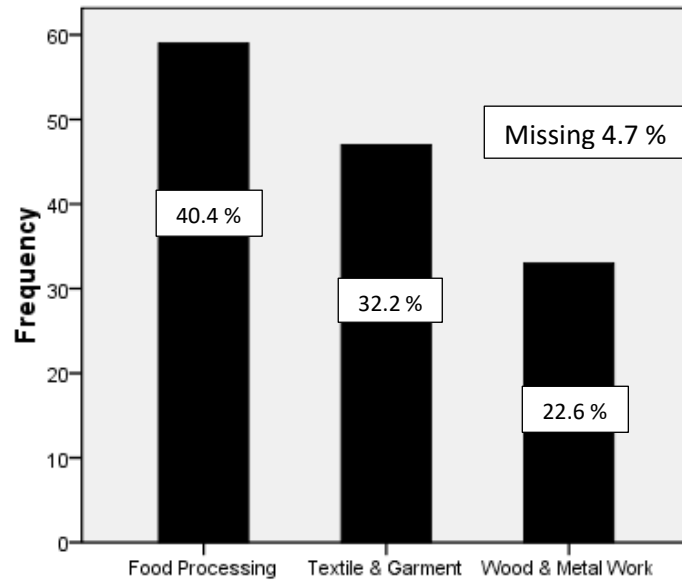
## 4.2 Business Related Profile of the MSEs

In this section the scope is narrowed and focused on business related characteristics of MSEs. It gives us up to date information of MESs from business perspective taking various parameters. These parameters latter serve as firsthand information in determining the impact and relationship of financial practices with growth and development of MSEs using a crosstab and correlation analysis.

### 4.2.1 Working sector of MSEs

The figure 4.6 here below shows that, out of 61, 51 and 34 units of predetermined sample size for food processing, textile & garment and wood and metal work respectively, was able to reach 59, 47 and 33 sample units respectively achieving 96.7%, 92.1% and 97% of the target sample size for each. From the total respondents, 40.4% of them are from food processing followed by 32.2 and 22.6% for textile & garment and wood and metal work respectively. The study couldn't reach a total sample of 7 units which is 4.79%.

**Figure 4.6** Working sectors of MSE

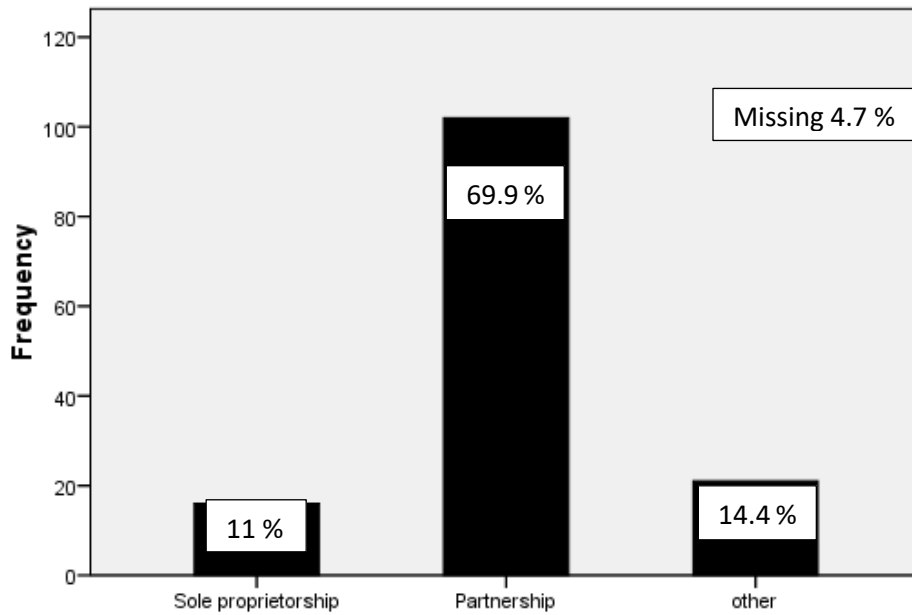


*Source: (Sample survey, 2018)*

#### **4.2.2 Ownership form of MSEs**

The form of business ownership has its own impact generally on the overall business and specifically on how financial decisions are taken. The major forms of business being sole proprietorship, partnership, cooperative and corporation, the study conducted revealed in figure 4.7 below that out of the total sample population, 16 units which is 11% are found to be owned by sole proprietorship followed by 102 units (69.9%) established in a partnership form. 21 units (14.4%) of the samples have other forms of business. From this, being partnership form of business is applied mostly, we can infer that most of these enterprises have high flexibility in taking decisions including that of finance whereas, at the same time bear all the risk and consequence of their decision with unlimited liability.

**Figure 4. 7** *Form of business ownership of MSEs*

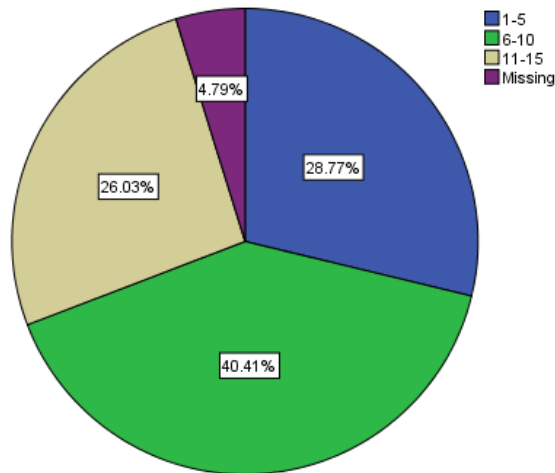


**Source:** *(Sample survey, 2018)*

#### **4.2.3 Number of employees in MSEs**

The study also included the number of employees engaged in the MSEs from which the sample size is drawn. Accordingly, figure 4.8 here below shows that 59 (40.4%) are found to employ 6-10 number of employees followed by 42 (28.8%) having an employee size of 1-5 whereas, MSEs that have employees between 11-15 are found to be 38 (26%). Thus, the MSEs under consideration meets the number criteria of (Ronge et al, 2002 cited in Mulugeta, 2011:15) which distinguish micro and small firms as those with less than 10 employees as micro enterprises whereas those with 10-15 are referred as small businesses.

**Figure 4. 8** *Number of employees in MSEs*

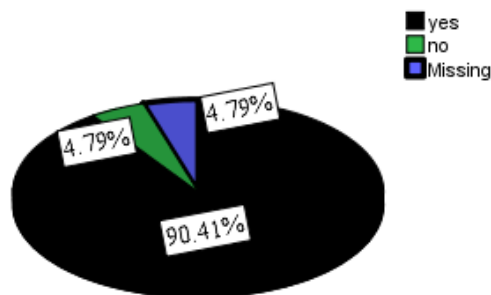


**Source:** *(Sample survey, 2018)*

**4.2.4 General financial status of MSEs**

Before drilling deep to financial management performance and practice of MSEs, the study confirmed the lack of finance that these enterprises face as many of their counterpart enterprises operating in developing countries. Among several studies reflecting this, (Sargent and Young cited Ermias Werkilul 2011: P15) states that keeping other factors in consideration, financial problem is by far the common and most challenging problem facing the MSEs affecting their growth and development. Figure 4.9 here below shows that 90.4% of the respondents which is 132 MSEs face financial shortage during start up and or while operating their business while only 4.7% of the respondents that is 7 MSEs disclosed absence of financial shortage problem. The study couldn't get response from a total of 7 MSEs.

**Figure 4.9** *The Number of MSEs Facing Financial Shortage*

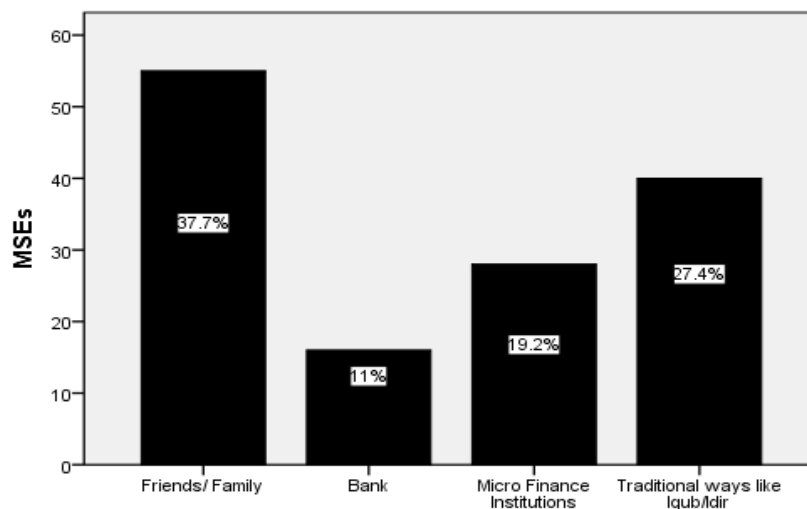


**Figure:** *(Sample survey, 2018)*

#### 4.2.5 Financial sources of MSEs

Businesses can raise money to start up or develop their business in different ways. Basically, we can categorize these sources as debt and or equity sources. While equity sources require owners to fund their business by their own means, debt sources entail reaching for external financial entities to raise capital. Regarding this, figure 4.10 shows that the majority of MSEs which is 55 (37.7%) depend on family or friends to raise the initial capital required or run their businesses followed by traditional financial institutions with 40 (27.4%). The study also revealed that the involvement of formal financial organizations like Micro finance institutions and banks are limited with only 28 (19.2%) and 16 (11%) respectively. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

**Figure 4. 10** *Financial Sources of MSEs*



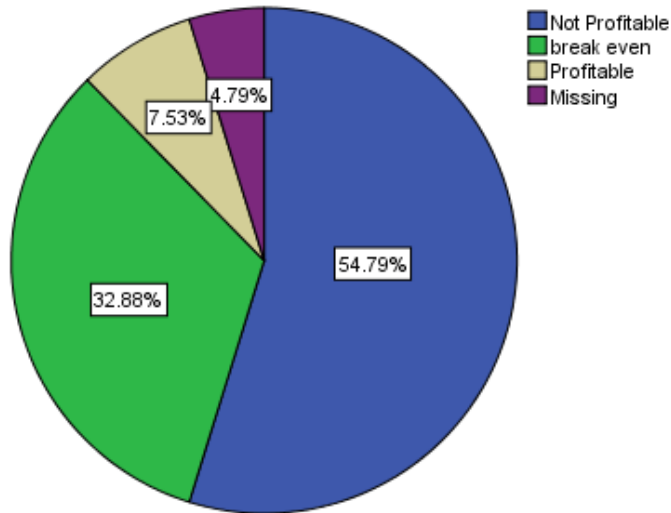
**Source:** (Sample Survey, 2018)

#### 4.2.6 Profitability trend of MSEs

Businesses are established to maximize profit and or to minimize cost. Financial management therefore represents the process by which profits of the business are increased through investment decisions, financing or dividends. Taking this, figure 4.11 here below shows the profitability trend of MSEs. Accordingly, 54.8 % (80) of the MSEs has disclosed that their business is not profitable while 32.8% (48) of them said that they are operating without loss and without profit. It is only 7.53% (11) MSEs that revealed

profitable business trend. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

**Figure 4. 11** Profitability trend of MSEs

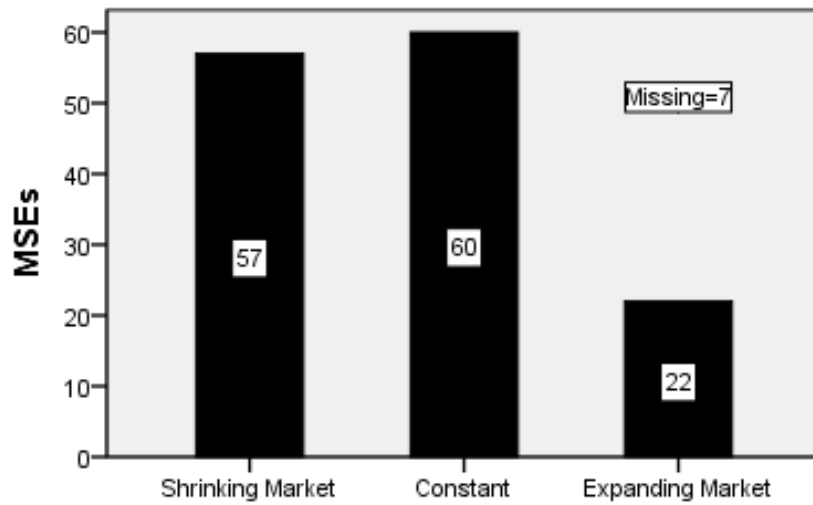


Source: (Sample Survey, 2018)

#### 4.2.7 Market share trend of MSEs

A growing market network is one of the key indicators of successful business. An expanding market comes up with additional demand for goods and services thereby increasing sales volume. This in turn raises the profit of a business. The study conducted regarding the market trend of MSEs in figure 4.12 here below shows that 60 (41.1%) of MSEs are witnessing a constant market trend which is not increasing or decreasing while, 57 (39%) of the respondents declared that they are experiencing a shrinking market trend. Meanwhile, 22 (15.1%) of them stated that their market is expanding. The study couldn't get response from 7 (4.79%) of the sample size population. This trend is shown in the following bar graph.

**Figure 4. 12** Market share trend of MSEs

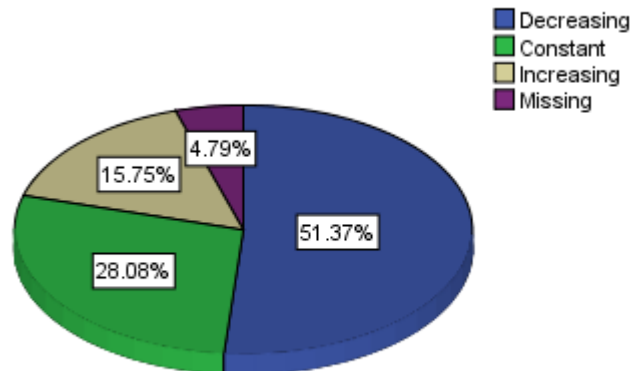


*Source: (Sample survey, 2018)*

#### **4.2.8 Trend of employment opportunity creating of MSEs**

Another growth and development indicator of a business is employment opportunity creation. We have seen in the literature part of this study that based on the number of employee's, micro and small businesses are categorized under those who have 15 or less employees. keeping this limit, the respondents were asked to answer the direction (increasing or decreasing) trend of their business employment opportunity creation. As shown in figure 4.13 below, 51.37% (75) of MSEs witnessed a drop in their number of employment while 28.08% (41) of them saw no change in their number of employments. Meanwhile, it is only 15.75% (23) of MSEs has shown an increase in the number of their employment headcounts. Therefore, generally seeing we can say that MSEs are facing difficulties which are responsible for either for employee cut off actions or to the stagnancy of their operation. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

**Figure 4. 13** *Employment trend of MSEs*



**Source:** *(Sample survey, 2018)*

### **4.3 Financial Management Practices of MSEs**

Managers and or business owners of MSEs in Addis Ketema sub city of Addis Ababa were asked regarding their application and practice of various financial management activities. These activities were structured and organized in to three sub sections which include, the general financial management attitude and application of MSEs, financial management skill related areas and financial data usage and application. Measures of central tendency specifically percentage, median and standard deviation was used to analyze the results. Median was chosen over mean due to discrete nature of the Likert scale questioners used. The median result was compared against the performance grading criteria where according to Abdulah R. 2010 p. 465, 4 & 5 are regarded as Good indicator, 3 as acceptable performance and 1&2 as poor performance which requires improvement.

#### **4.3.1 General financial management approach of MSEs**

Business owners or entrepreneurs in small business sector usually seems to neglect the financial management aspect of their business. This part presents the general approach that MSEs use towards financial management activities. The results of measures of central tendency, as per mentioned above, were obtained from the sample of respondents of textile and garment, food processing and metal and wood works are shown in the following tables.

**Table 4. 1 General financial management approach of MSEs**

	Never Applied	Not Applied	Somewhat Applied	Applied	Strictly Applied	Median	Mean	Std. Deviation
General financial management application								
MSEs degree of giving the required attention for financial management	16.4%	28.1%	37.0%	10.3%	3.4%	3	2.54	1.016
MSEs degree of having financial management rules and regulations	13.7%	35.6%	28.1%	17.8%	0.0%	2	2.53	0.958
MSEs degree of observing finance rules with in the business	11.0%	54.8%	23.3%	6.2%	0.0%	2	2.26	0.745
MSEs degree of developing sound financial policy using financial information	7.5%	43.2%	27.4%	15.8%	1.4%	2	2.58	0.908
MSEs degree of recording financial transaction activity	13.7%	35.6%	38.4%	7.5%	0.0%	2	2.42	0.833
MSEs degree of developing and applying financial reporting mechanism	0.0%	43.2%	36.3%	15.8%	0.0%	3	2.71	0.735
MSEs degree of following up and managing working capital	2.7%	48.6%	35.6%	8.2%	0.0%	2	2.52	0.695

**Source:** Sample Survey (2018)

The table 4.1 above depicts the relationship between the approach MSEs have towards some general practices of finance and financial management activities. In relation to this, several finance related issues were surveyed to see the stance where these MSEs are currently. As a result, business owners/ managers were asked the extent to which they emphasize and stress on the need for financial management activities to their business. According to this, the survey found that 44.5% of the respondents has either never gave the necessary attention required or just simply overlooked this practice, directing their focus on other functional areas. Meanwhile, 37% of the respondents gave attention somewhat as part of the overall management function while, it is only 10.3 % of them who recognized the importance and only 3.4 % who recognized and strictly gave the attention necessary. To give us clearer picture, measure of central tendency tools, the Median and Standard Deviation, was applied. The result of the median, which is 3, shows

that generally there is an acceptable level financial management attitude where it can be said that some consideration is given to financial management. A Standard Deviation of 1.016 refers to that approximately, most of the respondents lie between the range 1.54 and 3.54 enabling us to conclude that, although financial management is given attention somehow, it is not stressed enough by these MSEs and therefore there is a space for improvement. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

Another issue forwarded to the respondents was, weather they have clear and formal financial rules and regulations applied in their business to allow smooth financial management process. To this extent, 49.3 % of the MSEs have no any, what so ever, formal financial rules and regulations that help govern their finance related activities of the business. 28.1 % of the respondents indicated that they have somewhat rules and regulation when it comes to how to manage businesses finance while, it is 17.8 % of them that have a clear formal financial management rules which can be applicable. The median value of "2" shown in table 4.1 implies the absence of acceptable level of clear and formal financial rules and regulations. Meanwhile, a standard deviation of 0.958 depicts that most of the responses lies between  $\pm 0.958$  of the mean value. In relation to this, the observation extent of these financial management rules and regulations were also considered in the study. Accordingly, 65.8 % of the response implied that no observation was made to financial management rules and regulations. This makes sense in the presence of 49.3 % of MSEs that does not even have any formal financial management rules and regulations as shown above. On the other hand, 23.3 % of the respondents' have poor observation of financial management rules and regulations while, it is only 6.2 % of them are found to observe those rules. This was also shown with "2" median value which indicates poor performance and that it needs improvement strictly. The standard deviation of  $\pm 0.745$  shows the upper and lower boundary most of the responses lie in reference to the mean value. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

Businesses set their own target goal and objectives considering resources available on their hand. Among these important resources, finance is the most critical in identifying and setting the business capacity. In this regard, MSEs were asked if they use financial information's to develop a sound financial policy to help them achieve their

business target. the study above shows that, 50.7 % of the respondents do not use financial information's in setting finance policies for their companies. 27.4 % of the respondents stated that they use some financial information's while defining their financial policies. On the other hand, it is only 17.2 % of MSEs who were found setting their financial policies based on financial information. Generally, most of the respondents were found between  $\pm 0.908$  of the mean value. This result was further indicated by median value of 2 referring a poor performance of MSEs regarding the use of financial information to develop sound policy that need to be strictly improved. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

Financial information is basically generated from a group of financial data's. These data's, that emanate from businesses various daily activities, is related with finance directly or indirectly. Businesses should keep record of these transactions to have clearer picture of their business, analyze trends, decision making and others. In short, it can be said that there is no financial management activity without financial data. Hence, sample MSEs were surveyed regarding their degree of keeping financial transaction records. Given this, 49.3% of the respondents are found not keeping financial transaction records while, 38.4% of the respondents keep financial transactions in a loosely manner. Meanwhile, it is only 7.5 % of MSEs that has good financial transaction record keeping methods. Generally looking most of the respondents belong in between the range  $\pm 0.833$  of the mean value. This result was further cemented with the median value of "2" which indicates the presence of unacceptable level of recording financial transaction activity with a room for improvement. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

As far as financial transaction is concerned, only record keeping is not enough by itself for businesses to effectively utilize financial data. Businesses need to have a well-developed reporting mechanism for communicating these financial data. Thus, MSEs were requested to reflect on to what extent they have developed and applied financial reporting mechanism in their business organizations. Accordingly, table 4.1 reveals that, 43.2 % of the MSEs do not have a clear financial reporting mechanism while, 36.3 % of them have a poor reporting mechanism. On the opposite side, those who developed good reporting mechanism counts only 15.8 % of the respondents. But, looking to a median value of "3", it tells the existence of acceptable level of developed reporting mechanism for these MSEs. Most of the respondents were located within a standard deviation of  $\pm$

0.735 of the mean value. Therefore, it can be concluded that although most of them have developed some kind of reporting mechanism, it still needs improvement to effectively use for financial management purposes. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

The other area of interest the study concerned was management of working capital resources in MSEs. A close follow up and planning is required for businesses in order not to tackle unprecedented cash runouts the business need to operate daily activities. Accordingly, 51.3 % of MSEs were found lacking follow up and management of their working capital while 35.6 % of them apply loose follow up and management. It is only 8.2 % of the respondents who were found to closely monitor their working capital which help avoid unnecessary operation breakdowns. This poor performance was also expressed with a median value of "2" and with a standard deviation  $\pm 0.695$  of the mean value where most of the respondents lie in. Therefore, it can be generally concluded that, working capital management practice in these MSEs is poor. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

All in all, it can be said that there is acceptable level of financial management attitude in MSEs with a room for improvement. Thus, MSEs need to shade light more on financial management concepts of their organization.

#### **4.3.2 Financial management skill and related factors of MSEs**

Poor execution of financial management practice has been identified as one of the root causes for small business failures (McMahon and Holmes, 1991; p 19-29). Depending on this, the study has identified financial management skill as a crucial factor that affects the financial management practice of MSEs thereby affecting growth development. As a result, financial management skill related questions were forwarded to the respondents and results of were disclosed in table 4.2 here below.

**Table 4. 2 Financial management skill related factors of MSEs**

Financial Management Skill related factors	Never Applied	Not Applied	Somewhat Applied	Applied	Strictly Applied	Median	Mean	Std. Deviation
MSEs degree of using a skilled manpower in finance area to manage finances	3.4%	40.4%	27.4%	21.9%	2.1%	3	2.8	0.9
MSEs degree of using professional financial service from external institutions	3.4%	28.1%	55.5%	8.2%	0.0%	3	2.7	0.7
MSEs degree of engaging in financial management skill development activities	17.1%	61.6%	9.6%	6.8%	0.0%	2	2.1	0.8

**Source:** *Sample Survey (2018)*

Table 4.2 above dealt with allocating and or using of skilled manpower in areas that require finance skill. The conducted survey result showed that, 43.8% of the sample MSEs either never used skilled personnel in finance or avoided allocating. Whereas, 27.4 % of them somehow used a skilled manpower to manage their finances. On the other hand, it is only 21.9% of them which effectively apply the use of skilled manpower and a rare percentage of them (2.1%) are found to strictly make sure the use of skilled labor in finance. The median value of “3” indicates that most of the surveyed MSEs has an acceptable performance but also which needs to be improved while allocating skilled workforce in the area of finance to manage their business. This was further displayed by chunk presence of the respondents approximately in between 1.863 and 3.697 having a standard deviation of .917 from the mean value. Hence, it can be said that most of the MSEs financial management activities are loosely run creating difficulties for these businesses. Meanwhile, the study couldn’t get response from 7 (4.79%) of the sample size population.

Also, in table 4.2, MSEs were asked if they reach out external financial management service providers for general and technical advice and assistance. Accordingly, the survey result showed that, 31.5% of the respondents has, in any ways, never approached external financial management service providers to fill the skill gap available in finance area of their business. on the other hand, it is 55.5% of the respondents

who somehow reached financial service providers while, it is only 8.2% of the respondents use external financial management skills in running their finance and related activities. The median measurement of “3” indicated above affirms that the usage level of professional external financial management service for these MSEs is acceptable while a room for improvement is available. Simultaneously, the standard deviation of 0.671 showed above refers that most of the respondents are found in the range of 2.049 – 3.391 showing low level of application. Meanwhile, the study couldn’t get response from 7 (4.79%) of the sample size population.

Table 4.2 above also showed to what extent business owners or managers are engaged in financial management skill development of themselves or the employees in charge of financial activities. Accordingly, 78.7 % of MSEs responded that there are no any skill development activities undertaken in their business to raise the understanding and application level of finance personnel’s. 9.6% of MSEs somehow engage in training & briefing of finance skill while, only 6.8 % of them are the ones who gave emphasis for developing their financial management skills. This poor performance is also reflected with a median of “2” and a standard deviation of 0.754 making most of the responses between 1.32 – 2.814 of the mean value. Meanwhile, the study couldn’t get response from 7 (4.79%) of the sample size population.

#### **4.3.3 Financial data usage and application of MSEs**

Financial data is generated from businesses day to day transactions. These generated data’s, once analyzed properly, serve as a primary input for reviewing and measuring current financial performance of businesses thereby helping business owners or decision makers to draw various future course of actions necessary. MSEs were presented with some of the essential financial management tools and asked to evaluate the usage extent of these tools for managing their finances.

**Table 4. 3 Financial data usage and application of MSEs**

	Never Applied	Not Applied	Somewhat Applied	Applied	Strictly Applied	Median	Mean	Std. Deviation
Financial data usage and application of MSEs								
MSEs degree of using financial data for fund sourcing	23.3%	45.2%	12.3%	13%	1.4%	2	2.2	1.009
MSEs degree of use financial data for planning sales and expenditure	0.0%	67.8%	27.4%	0%	0%	2	2.29	0.454
MSEs degree of using financial data as a control mechanism of financial status of the business	4.8%	63.0%	17.8%	9.6%	0%	2	2.34	0.728
MSEs degree of using financial data for budgeting activity	6.2%	68.5%	14.4%	6.2%	0%	2	2.22	0.657
MSEs degree of using financial data for managing cash payables and receivables	6.8%	57.5%	19.9%	11%	0%	2	2.37	0.782
MSEs degree of using financial data for long term investment decisions	0.0%	67.8%	26%	1.4%	0%	2	2.01	0.577
MSEs degree of using accounting information system	15.1%	63.7%	16.4%	0%	0%	2	2.3	0.491

**Source:** *Sample Survey (2018)*

In the table 4.3 above, MSEs were asked if they use the information generated from their business transaction to propose or convince various financing institutions in the process of raising finance to operate their business. The survey conducted shows that, 68.5% MSEs do not use or provide financial data while looking for fund sources. On the other hand, 12.30% MSEs disclosed the occasional use of financial information for finding finance while 13% and 1.4% apply and strictly apply the usage of financial information to support their finance sourcing from different organizations respectively. Consequently, the median value of “2” indicated above tells the poor performance of MSEs in using financial information in the process of fund raising. This was reaffirmed with the value of  $\pm 1.009$  standard deviation from the mean (2.2) where most of the responses lied in. Meanwhile, the study couldn’t get response from 7 (4.79%) of the sample size population.

Sales and expense planning is another major area that needs focus from business owners. While drawing the roadmap of their business, especially those related with sales and expense, MSEs were asked if they consider financial data generated and, if so, the degree of application was requested. Accordingly, 67.8% (99) of MSEs were, surprisingly, found not using financial data in planning sales and expenditure of their businesses while, it is only 27.4% (40) of them somehow use financial data as an input in the process of planning. This was reflected with median value of “2” representing poor performance that needs to be improved and standard deviation of 0.454 making most of the responses between 1.836 – 2.744 of the mean value (2.29). Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

Another function of financial data could be that it provides information regarding the financial status of business creating accurate follow up mechanisms for managers. Hence, MSEs were asked the degree of using financial data as a control mechanism of their financial status. The study found that, 67.8% of MSEs were either never used financial data for mentioned purpose or not applied. While 17.8% of them fall under those who somewhat applied and 9.6% fall under those who uses financial data as a control mechanism of their financial status. This poor performance was also portrayed in a median value of 2 with  $\pm 0.728$  standard deviation from the mean where most responses were located. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

In order for business to be profitable, financial resources should be allocated in an effective and efficient manner, which is why budgeting activity is essential for firms' success. Budgeting requires a reliable financial data regarding the overall business operation so that it can determine the finance required. MSEs were asked to what extent they use financial data in their budgeting activity. Accordingly, 74.7% (109) of MSEs either never used financial data for budgeting or do not apply in their budgeting activity. While, 14.4% (21) of them use financial data to some extent, only 6.2% (9) of them were found to use financial data in budgeting activity. A median value of “2” represents the poor performance of MSEs regarding the use of financial data in their budgeting activities. In addition, 0.657 value of standard deviation from the mean value shows the upper and lower boundary where most of the respondents lie that is, 1.563 – 2.787. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

The most liquid asset of a business is cash. Although profitable balance is shown on the income statement, absence of adequate cash to run may cause business bankruptcy. Taking this, MSEs were asked if they use financial data in a way which helps to manage the flow of cash in to and out of the business, payables and receivables. The study found that, although crucial the issue is, 64.3% of MSEs either never used or not applied financial data for managing their cash and related issues. Whereas, 19.9% (32) of MSEs somewhat use financial data from their company to manage cash while, only 11% (35) of MSEs were able to use financial data in managing their most liquid asset (cash). This poor situation was reflected with a median value of 2 that needs improvement. On the other hand, a standard deviation value of .782 from the mean (2.37) indicates that most of the responses are between 1.588 - 3.152. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

Among the most important and difficult decisions that business owners or managers are expected to take includes long term investment decisions. This is because, these types of decisions usually imperil, not only a large lumpsum amount of capital to be invested, it may also jeopardize the whole business in general. Therefore, it is necessary that decision taken should be based on proper and careful analysis of financial data. With this note, MSEs were asked if financial data is considered before taking long term investment decisions. The study revealed that, 67.8% (99) of MSEs do not consider financial data as main source of taking long term investment decisions. Whereas, 26% (38) were found to give some consideration to financial data prior to making decision while, only 1.4% (2) of them replied that long term investment decisions are based on financial data analysis. This poor performance was shown with a median value of "2" where improvement is required. This was reaffirmed with the value of  $\pm 0.577$  standard deviation from the mean (2.01) where most of the responses lied in. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

The use of technological products like accounting information system (AIS) in assisting financial management process was also one of the areas where MSEs were requested to response. Accordingly, 78.8% (115) of MSEs do not by any means apply AIS while, 16.4% (24) of them has limited application level. This poor performance was also portrayed in a median value of "2" with  $\pm 0.491$  standard deviation from the mean (2.3) where most responses were located. Meanwhile, the study couldn't get response from 7 (4.79%) of the sample size population.

#### 4.3.4 Growth and development of MSE

MSEs performance was measured in terms of growth and development. Accordingly, respondents were asked if financial management practices are affecting the profitability, market and employment capacity in Table 4.4 below.

**Table 4. 4 Financial management practice and growth and development of MSEs**

Growth and Development	Strongly Agree	Agree	Somewhat Agree	Disagree	Strongly Disagree	Median	Mean	Std. Deviation
Do you think that the presence or absence of effective financial management approach has affected profitability your company	0%	19.9%	43.8%	24%	7.5%	3	2.8	0.861
Do you think that the presence or absence of financial management skill has affected profitability your company	0%	9.6%	41.1%	39.7%	4.8%	3	2.58	0.741
Do you think that the usage and application of financial management has affected profitability your company	0%	6.2%	52.7%	31.5%	4.8%	3	2.63	0.683
Do you think that the presence or absence of effective financial management approach has affected the market share of your company	1.4%	17.1%	58.9%	17.1%	0.7%	3	3.01	0.67
Do you think that the presence or absence of financial management skill has affected the market share of your company	0%	18.5%	48.6%	28.1%	0%	3	2.9	0.695
Do you think that the usage and application of financial management has affected the market share of your company	0%	6.2%	40.4%	40.6%	2.1%	2	2.53	0.652
Do you think that the presence or absence of effective financial management approach has affected the employment capacity of your company	0%	6.2%	24%	53.4%	11.6%	2	2.26	0.755
Do you think that the presence or absence of financial management skill has affected the employment capacity of your company	0%	0%	19.2%	54.1%	21.9%	2	1.97	0.659
Do you think that the usage and application of financial management has affected the employment capacity of your company	0%	0%	33.6%	58.9%	2.7%	2	2.32	0.528

**Source:** Sample Survey (2018)

In the table 4.4 above, MSEs were asked if the presence or absence of effective financial management approach has affected profitability of the company. The survey conducted shows that, 69.7% MSEs agree that financial management approach affects the profitability of their company. On the other hand, 24% MSEs disclosed that financial management approach does not affect profitability of their firms while, 7.5% of MSEs

does not see any relationship between profitability and financial management approach. Consequently, the median value of “3” indicated above tells the existence of acceptable relationship between financial management approach and profitability. On the other hand, MSEs were asked if financial management skills affect the profitability of their firm. Accordingly, 50.7% of the respondents generally agree that financial management skill affects the profitability of the firm. Meanwhile, 39.7 % of the respondents does not believe that financial management skill affects profitability and that 4.8% of them does not see any relationship between financial management skill and profitability. Financial management data usage and application and profitability of MSEs was also another area that respondents were asked. 58.9% of the respondents replied that financial management data usage and application affects profitability while, 31.5% of them disagree on the effect. In addition, 4.8% of them does not see any relationship between financial management data usage and application and profitability.

The effect of financial management approach, financial management skill and financial management data on the market share of MSEs was asked to managers of MSEs. Accordingly, a median value of 3, 3, and 2 was obtained from the respondents. This implies the existence of acceptable level of effect for financial management approach and financial management skill while, there is little effect of financial management data usage and application on the market share according to the respondents.

On the other hand, respondents were also requested to answer if financial management approach, financial management skill and financial management data affects the employment capacity of MSEs. Consequently, a median value of 2 was obtained for all which showed the existence of poor relationship between these financial management practices and employment capacity of MSEs.

#### **4.4 Results of Inferential Statistics**

This section deals with discussion of results obtained from Pearson’s product moment correlation coefficient and multiple regression analysis. Taking the results of these tools, decisions were made, and conclusions were drawn regarding the hypothesis made and the research in general.

#### 4.4.1 Pearson's product moment correlation coefficient

According to (Kothari, 2010, p. 139), Pearson's product moment correlation coefficient is the most widely used method of measuring how strong variables are related to one another keeping one is dependent and the other is independent. In other words, it is used to determine whether there is a significant relationship between financial management approach, financial management skill, financial management usage variables, on one hand, and performance (growth and development) on the other hand. The table 4.4 below indicates that the correlation coefficients for the relationships between performance and its independent variables are linear and positive ranging from moderate to strong correlation coefficients.

**Table 4. 5 The correlation of performance (growth & development) with financial management approach, skill & usage and application in MSEs**

		<i>Financial Management Approach</i>	<i>Financial Management Skill</i>	<i>Financial data usage and application</i>	Performance (Growth and development)
<i>Financial Management Approach</i>	Pearson Correlation	1	.816**	.698**	.788**
	Sig. (2-tailed)		.000	.000	.000
	N	139	139	139	139
<i>Financial Management Skill</i>	Pearson Correlation	.816**	1	.679**	.759**
	Sig. (2-tailed)	.000		.000	.000
	N	139	139	139	139
<i>Financial data usage and application</i>	Pearson Correlation	.698**	.679**	1	.768**
	Sig. (2-tailed)	.000	.000		.000
	N	139	139	139	139
Performance (Growth and Development)	Pearson Correlation	.788**	.759**	.768**	1
	Sig. (2-tailed)	.000	.000	.000	
	N	139	139	139	139

\*\* . Correlation is significant at the 0.01 level (2-tailed).

**Source:** Sample Survey (2018)

The result indicated above in table 4.4 reveals the existence of a strong positive relationship between performance (growth and development) and financial management usage and application ( $r = 0.768$ ,  $P < 0.01$ ) which means it is statistically significant at

99% confidence level. This implies at 1% level of significance, it was shown that financial management usage and application is strongly associated with the performance of MSEs in Addis Ketema sub-city. Similarly, a strong positive correlation was observed between financial management skill and performance ( $r = 0.759$ ,  $P < 0.01$ ) at 99% confidence level. Hence, financial management skill is also significantly related with growth and development of MSEs. Moreover, a remarkably strong positive relationship was found between financial management attitude and performance with ( $r = 0.788$ ,  $P < 0.01$ ) which is also significant at 99% confidence level.

#### 4.4.2 Regression analysis

In this section the result of multiple regression analysis was presented and discussed. In Multiple regression, determination of the degree to which multiple explanatory variables explain the variance in dependent (explained) variable.

**Table 4. 6 Regress financial management approach, skill & data usage and application of MSE as independent variable on performance (growth & development) as dependent variable.**

##### Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.854 <sup>a</sup>	.729	.723	.20303

a. Predictors: (Constant), *Financial Management Approach*, *Financial Management Skill*, *Financial Data usage and application*

##### Coefficients<sup>a</sup>

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Collinearity Statistics	
	B	Std. Error	Beta			Tolerance	VIF
1 (Constant)	.877	.094		9.289	.000		
Financial Management Approach	.232	.056	.343	4.159	.000	.295	3.388
Financial Management Skill	.132	.048	.222	2.760	.004	.310	3.224
Financial Data Usage and Application	.342	.059	.378	5.835	.000	.478	2.094

a. Dependent Variable: *Performance (Growth & Development)*

*Source: Sample Survey (2018)*

The table 4.5 above reveals the estimates of the multiple regression of performance against its variables for the sample of 146 operators. The multi collinearity test value, which measures the degree of relationship between independent variables, shown in the variance inflation factor VIF reveals that the relationship between the independent variables is acceptable since it has a value less than 7 and at the same time, tolerance values are >0.1. In addition, the result shows that all variables are significant with value < 0.05. Given these, the correlation between the observed value of performance and the optimal linear combination of the independent variables (Financial management approach, Skill & Data usage and application factors) is 0.854, as indicated by multiple R. Besides, given the R Square value of 0.729 and adjusted R square value of 0.723, it may be realized that 72.3% of the variation in performance can be explained by the independent variables. The remaining 27.7 % of the variance is explained by other variables not included in this study. The unstandardized coefficients B column gives us the coefficients of the independent variables in the regression equation including all the predictor variables as indicated below.

$$\text{Predicted performance score} = .877 + .232 (\text{F.M Approach}) + .0132 (\text{F.M Skill}) + .342 (\text{F.M data usage and application})$$

Table 4.5 above further shows that; the standardized beta coefficient column shows the contribution that an individual variable makes to the model. The beta weight is the average amount the dependent variable increases when the independent variable increases by one standard deviation (all other independent variables are held constant). As these are standardized, where metric dilemmas are avoided, they can be compared easily. Thus, the highest influence on the performance of MSEs is from the financial management data usage and application (.378) followed by financial management approach factor (0.343). On the other hand, financial management skill with the beta value of .132 is the poorest predictor of performance when it is compared with the other explanatory variables under study.

Taking the above results in to consideration, the following statements could be made regarding the hypothesis of the study. These are:

- ⊗ The hypothesis which is stated as “Financial management practice has a significant impact and positive relationship with the growth and development of *MSEs* in Addis ketema sub-city” was tested at a 1% level of significance. It was

discovered that financial management practices do play a significant role in determining the performance of MSEs. Thus, the hypothesis may therefore be accepted. In addition,

- ⊠ The hypothesis which states that “The approach, management and administration practices of financial management has a significant impact and positive relationship with the growth and development of *MSEs*” was found significant and hence may therefore be accepted. Similarly,
- ⊠ The hypothesis which states that “Usage and application of financial data has a significant impact and positive relationship with the growth and development of *MSEs*” tested at a 1% level of significance was discovered to have a significant role in determining the performance of MSEs and thus may therefore be accepted.
- ⊠ The hypothesis which states that “Financial management knowhow and skills have a significant impact and positive relationship with the growth and development of *MSEs*” was also found significant and may therefore be accepted.

#### 4.5 Summary of The Results

- ⊗ Business owners of MSEs in Addis Ketema Sub-city of Addis Ababa were found to be Male 77.7% where most of them 77% are found to be between the age 15-34 showing a considerable young involvement with most of them 55.4 % being single. In addition, most of the respondents 31.8% were found to have diploma degree and that 30.41% of them has business experience of 4-6 years.
- ⊗ In the study, 40.4% of them were from food processing followed by 32.2 and 22.6% for textile & garment and wood and metal work respectively. Most of these enterprises 69.9% of them were established in partnership form of business with majority of them 40.6% having employees between 6-10.
- ⊗ 90.4 % of the respondents revealed that they face financial difficulties while running their business. The study also showed that 37.7% of MSEs depended on family or friend as first source of finance. In addition, there was a constant trend in market share and profit growth for 41.1% and 54.8% of MSEs respectively.
- ⊗ The survey conducted regarding financial management approach showed that, those MSEs that give the required attention for financial management activities were found to be low (13.7%). Also, MSEs that have financial management rules and regulations were limited with 17.8% of application. In addition, only 6.2% of MSEs were found observing finance rules with in the business. Whereas, there was only 17.2% them that have developed sound financial policy using financial information. Another important aspect of financial management was, recording financial transaction activity where, 45.9% of them were found. Developing and applying financial reporting mechanism & degree of following up and managing working capital were also found both limited with 15.8% and 8.2% respectively.
- ⊗ Results of survey regarding financial management skill related factors of MSE showed that, only 24% MSEs use a skilled manpower in finance area to manage finances. Meanwhile, only 8.2% of MSEs were found to use professional financial service from external institutions. In addition, financial management skill development activities were limited to 6%.
- ⊗ The survey made in relation with financial data usage and application of MSEs revealed that, 68.5% of the respondents do not use financial data for fund sourcing whereas, 67.8% of them do not use financial data for planning sales and expenditure of their business. In addition, the usage of financial data as a control

mechanism of financial status of the business were only limited to 9.6% while, using financial data for budgeting activity is also limited to 6.2%. In addition, the study found that 64.3% of MSEs do not use financial data for managing cash payables and receivables and that 67.8% of MSEs also do not use financial data for long term investment decisions. This is including 78.8% of MSEs who do not implement accounting information system in their businesses.

- ◊ The Pearson's product moment correlation coefficient analysis made showed the presence of a strong positive relationship between performance (growth and development) and financial management usage and application ( $r = 0.768$ ,  $P < 0.01$ ). Also, a significant positive correlation was observed between financial management skill and performance ( $r = 0.759$ ,  $P < 0.01$ ). In the same manner, a strong positive relationship was found between financial management approach and performance with ( $r = 0.788$ ,  $P < 0.01$ ).
- ◊ The multiple regression analysis done revealed that, the correlation between the observed value of performance and the independent variables (financial management Approach, Skill & Data usage and application factors) is 0.854. Moreover, given the R Square value of 0.729 and adjusted R square value of 0.723, it may be realized that 72.3% of the variation in performance can be explained by the independent variables. The remaining 27.7 % of the variance is explained by other variables not included in this study. Furthermore, the standardized beta coefficient column showed that the largest influence on the performance of MSEs is from the financial management data usage and application (.378) followed by financial management approach factor (.343) and financial management skill factor with the beta value of (.222).

## CHAPTER 5: CONCLUSIONS AND RECOMMENDATIONS

Based on the results of this study, the impacts of financial management practice were measured in relation with their effect towards MSEs growth and development in Addis Ketema sub-city of Addis Ababa. In doing this, the researcher used the median value, Pearson correlation result and regression analysis result to draw conclusions which are drawn in relation with the hypothesis and the research objectives of the study. Finally, relevant suggestion & recommendations are made to owners of MSEs, government bodies researchers and other concerned bodies.

### 5.1 Conclusions

- ⊗ MSEs approach towards financial management activities like financial transaction recording, finance policy with in the business, observing finance rules and regulations and others were found unsatisfactory. Keeping their strong association with the dependent variable, growth and development, the existence of poor performance in these areas has strongly affected growth and development of MSEs. In other words, MSEs in *Addis Ketema* sub-city of Addis Ababa has poor approach towards financial management activities which significantly affected its performance. That is, there is a notable gap in management and administration activities of finance, which are important part and parcel of overall management. This can be attributed to various factors, including but not limited to, lack of proper understanding about financial management, negligence of these administrative activities, owners reluctance to adopt financial management and lack of motivation to change traditional way of doing business. Reaffirming this result, Hatten (2006, P. 218) stated that, it is laxity, negligence and lack of attention to financial management practices by business owners that usually tend to have negative implications on the performance of the business at the end of the day.
- ⊗ Results of survey regarding financial management skill factors of MSEs located in Addis Ketema Sub-city of Addis Ababa showed, the presence of a wide gap in using skilled manpower that handles the financial management activities, where neither skilled financial manager were allocated with in the business nor external professional financial service providers were approached to handle their finance. This implies the existence of high possibility, for MSEs, to inefficiently manage

financial resources which are limited by their nature and scarce in developing countries. It can also be inferred that financial management in these MSEs is usually run by “common sense”. This poor financial management skill performance therefore has a negative impact towards growth and development of MSEs. In relation to this, (Yusnidah I 2000, P284) was also mentioned that absence of deep and real financial management skills in small businesses hampers the growth and development of these businesses in a sustainable way.

- ◊ The other important aspect shown in the study was, the degree of financial management data usage and application. The study showed the presence of strong association between development of MSEs and financial management data usage and application variables. In addition, the magnitude of impact, financial management usage and application exerts, on growth and development is significant. Keeping this, the usage and application of financial data for planning sales and expenditure, fund raising, finance controlling, investment decisions and others were poorly executed in MSEs. Hence, it can be easily derived that inability to apply and use financial management tools for these and other activities has significantly contributed to the stagnation of profit and market share thereby affecting their overall performance of MSEs. One evidence showing the effect of poor application of financial data in raising fund could be, according to (Gebrehiwot and Wolday, 2004:55), the low tendency of Ethiopian commercial banks to provide loan for small businesses due to absence of formal financial management tools.
- ◊ Generally, it has been observed from this study that, financial management practices greatly affect the performance of MSEs located in Addis Ketema sub-city of Addis Ababa. Despite this, low level of application and implementation has been noted throughout MSEs impeding their overall growth and development.

## 5.2 Recommendations

The main aim of the study was to assess the impact financial management and practice has on the growth and development of MSEs. Regarding this, the study has conducted a survey study, analyze and reached up in to conclusion. Based on this, the following recommendations were forwarded addressing mainly the MSE managers/ owners, the government and researchers.

- ◊ The study revealed the presence of a wide gap in the financial management approach, financial data usage and financial skills of MSEs which strongly affected their performance. To alleviate these problems, MSEs especially, business owners/ managers need to take the lion share steps towards changing the poor financial management performance residing in their businesses. This could be done through,
  - First, recognize the impact that absence of good financial management has on the growth and development of MSEs.
  - Changing the long standing traditional and common-sense way of managing finance and the business in general.
  - Engage in small business financial management skill training and development activities through approaching financial management professionals, self-development by reading publications related with small business management, experience sharing from model or exemplary MSEs.
  - Develop well designed financial management system which incorporates the establishment of clear and concise financial data recording, storing, retrieving and reporting mechanisms.
  - Develop the trend and culture of generating financial management reports thereby, using those reports to assess the performance of the business, plan and forecast sales and expenditure, determine cash flow and working capital needs, take short, medium and long term investment decisions and base fund raising activities MSEs engage in to overcome finance needs.
  - As technology is swiftly changing, the business code of conducts practiced both internally and externally are also changing rapidly. Hence, MSEs need to adjust their working models, if not adopting technologies

immediately, so that they can smoothly align and integrate themselves with this rapid change.

- ⊠ The government can help MSEs develop financial management systems through facilitating B2B seminar, workshop, idea exchange and experience sharing programs, motivating the adoption and implementation of financial management systems by awarding good performers, enacting policies, laws, rules and regulations.
- ⊠ Finally, this research shades light only on the internal factor, specifically financial management, that affects the performance of MSEs. This implies the presence of wide space for further study through considering various internal and external factors that affect the growth and development of MSEs. Hence, it is strongly recommended for researchers interested in MSE development to engage themselves and conduct further researches that contribute to better identify, analyze and find out more effective way to tackle bottlenecks and broaden success factors of MSEs.

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**APPENDIX A**  
**REPUBLIC OF TURKEY**  
**ANADOLU UNIVERSITY**  
**GRADUATE SCHOOL OF SOCIAL SCIENCE**  
**DEPARTMENT OF INTERNATIONAL BUSINESS ADMINISTRATION**  
**MBA PROGRAM**

**SECTION 1: INTRODUCTION**

Dear respondent,

I am a graduate student of International Business Administration studying at Anadolu University in Eskisehir, Turkey. Currently, I am conducting a research entitled '*The Impact of Financial Management Practice on growth and Development of Micro and Small Enterprises in Addis Ketema Sub-Cities of Addis Ababa Ethiopia*'. The objective of this questioner is to help me get first-hand information from business owners, entrepreneurs or business managers like you regarding the topic mentioned above. Thus, your free will and cooperation in giving Reliable and Timely information is very important. The confidentiality of the information you provide is kept completely anonymous and it is only used for academic purposes only. No individual's responses will be identified as such and the identity of persons responding will not be published or released to anyone. Thank you in advance for your kind cooperation and dedicating your time.

Sincerely,  
Seyfedin Mohammed

**INSTRUCTIONS**

- ✓ No need of writing your name and enterprise's name.
- ✓ Giving more than one response is allowed, where ever applicable.
- ✓ For Likert scale type statements and multiple-choice questions indicate your answers with a check mark (✓) in the appropriate block.

## **PARTICIPANTS PROFILE.**

1. Gender:

Male

Female

2. Which age group do you belong?

15-24

35-44

25-34

Above 45

3. Marital status:

Married

Single

Divorce

Others

4. Level of formal Educational:

No formal education

Below high school

High school

College/ University

Diploma

Second degree and above

5. Year of experience generally in business:

1-3 years

4- 6 years

7-10 years

11 and above years

## **BUSINESS INFORMATION**

1. What is the main activity of the business?

Textile and garment

Food processing

Wood and metal work

2. What is the form of ownership in this business?

Sole proprietorship

Partnership

Other \_\_\_\_\_

3. what is the number of employees in your business?

1-5 Employees

6-10 Employees

11-15 Employees

Above 15 Employees

4. Did you came across in financial shortage while doing your business?

Yes

No

5. How did you raise funds to start-up and or manage your business?

- Personal saving                       NGOs
- Micro finance institutions
- Friends/ Family                       Traditional ways like Iqub/Idir
- Banks                                       Others (specify)-----

6. How do you see your overall business profitability?

- Profitable                       Not Profitable                       break-even income

7. What is the market share tendency of your business?

- Expanding market share                       Shrinking market share
- Constant market share

8. What does the employment opportunity creation trend of your company look like?

- Increasing                       Decreasing                       Constant

**FINANCIAL MANAGEMENT PRACTICES OF YOUR BUSINESS**

The most important financial management practices are listed below. Please indicate the degree to which these practices are being applied in your business enterprise. After you read each of the practices, evaluate them in relation to your business application and then put a tick mark (√) under the choices below.

No.	Financial Management Practices	Strictly Applied	Applied	Somewhat Applied	Not Applied	Never Applied
General Financial Management Approach						
1	Giving the Required Attention for Financial Management					
2	Have Financial Management Rules and Regulations					
3	Observe Finance Rules with In the Business					
4	Develop Sound Financial Policy Using Financial Information					
5	Management of Financial Transaction Record Activities					
6	Develop and Apply Financial Reporting Mechanism					
7	Closely Monitor Working Capital Status					

Skill related factor in Finance area						
8	Using Professional Financial Service from External					
9	Using A Manpower Skilled in Finance Area to Manage Finances					
10	Engage in Financial Management and Application Skill Development					
Financial Data Usage and Application						
11	Use Financial Data for Fund Sourcing and assessing cost of fund					
12	Use Financial Data for Planning Sales and Expenditure					
13	Use Financial Data as A Control Mechanism of Financial Status of The Business					
14	Use Financial Data for Budgeting Activity					
15	Use Financial Data for Liquidity management					
16	Use Accounting Information System					
17	Use Financial Data for Long Term Investment Decisions					
No.	Growth and Development	Strongly Agree	Agree	Somewhat Agree	Disagree	Strongly Disagree
18	Do you think that the presence or absence of effective financial management approach has affected profitability your company					
19	Do you think that the presence or absence of financial management skill has affected profitability your company					
20	Do you think that the usage and application of financial management has affected profitability your company					
21	Do you think that the presence or absence of effective financial management approach has affected the market share of your company					
22	Do you think that the presence or absence of financial management skill has affected the market share of your company					
23	Do you think that the usage and application of financial management has affected the market share of your company					
24	Do you think that the presence or absence of effective financial management approach has affected the employment capacity of your company					
25	Do you think that the presence or absence of financial management skill has affected the employment capacity of your company					
26	Do you think that the usage and application of financial management has affected the employment capacity of your company					

❖ Any remark that you would like to add.

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**I thank you again for your kind cooperation!**



ዲፕሎማ

ዩኒቨርሲቲ

ድህረ ምረቃ

5. አጠቃላይ በንግድ አለም ያለዎት የስራ ልምድ

1-3

4-6

7-10

ከ10 በላይ

**ንግድ ነክ መረጃ**

1 የተሰማሩበት የስራ መስክ ምንድነው?

ጨርቃ ጨርቅና አልባሳት

የምግብ አዘገጃጀት

እንጨትና ብረታ ብረት

2. የድርጅትዎ የባለቤትነት ሁኔታ

የግል (ብቸኛ)

ጥንድ ባለቤትነት

ሌላ

3. በአሁን ጊዜ የድርጅቱን ባለቤት ጨምሮ ስንት ሰራተኛ ይገኛል ?

1-5

6-10

11-1

ከ15 በላይ

4. በስራ አለም የገንዘብ ችግር አጋጥሞት ያቃል ?

አዎ

አይ

5. የንግድ ስራዎን ለመጀመር ወይም ለማካሄድ የሚያግዝ ገንዘብ እንዴት ያገኛሉ ?

የግል ቁጠባ

ማይክሮ ፋይናንስ ተቋማት

ቤተሰብ/ጓደኛ

ባንክ

መንግስታዊ ያልሆኑ ተቋማት

ደ የገንዘብ ተቋማት እቁብ

ሌላ

6. የድርጅቱን የትርፋማነት ሁኔታ እንዴት ይገልጹታል ?

ትርፋማ ነው

ትርፋማ አይደለም  ም ኪሳራም የለም

7. የድርጅቱን የገበያ ድርሻ አዝማሚያ እንዴት ያዩታል ?

እየጨመረ ነው

እየቀነሰ ነው

ለዉጥ የለም

8. የድርጅቱ ለሰራተኞች የስራ እድል የመፍጠር ሁኔታን እንዴት ያያሉ ?

እየጨመረ ነው

እየቀነሰ ነው

ለዉጥ የለም

**የድርጅትዎ የገንዘብ አስተዳደር አፈፃፀም ትግበራ**

ከዚህ በታች ለድርጅት የገንዘብ አስተዳደር የሚረዱ ዋና ዋና ትግበራዎች ተዘርዝረዋል። የድርጅትዎ እነዚህን

ተግባራት አፈፃፀም በተመለከተ እያንዳንዱን በደምብ ካነበቡ በዉኃላ (✓) ምልክትን በመጠቀም የትግበራ

መጠኑን ይግለጹ።

ተ.ቁ	የገንዘብ አስተዳደር ተግባራዎች	በጥብቅ ይተገበራል	ይተገበራል	በከፊል ይተገበራል	አይተገበርም	በፍጹም አይተገበርም
አጠቃላይ የገንዘብ አስተዳደር ተግባራት አመለካከት						
1	ለገንዘብ አስተዳደር አስፈላጊውን ትኩረት መስጠት					
2	የገንዘብ አስተዳደር ህግና ደምቦች መኖር					
3	የገንዘብ አስተዳደር ህግና ደምቦችን መተግበር					
4	የገንዘብ ነክ መረጃዎችን መሰረት ማድረግ ጥሩ የገንዘብ ፖሊሲ ማርቀቅ					
5	አጠቃላይ የገንዘብ ነክ እንቅስቃሴ ምዝገባ					
6	የገንዘብ ተጠሪነት ዘዴ ማርቀቅና መተግበር					
7	የስራ መንቀሳቀሻ መዋለነዋይ እንቅስቃሴን በቅርበት መከታተል					
የገንዘብ ሞያ ነክ ሁኔታዎች						
8	ሞያዊ የገንዘብ አስተዳደር አገልግሎት የሚሰጡ ተቋማትን መጠቀም					
9	በገንዘብ አስተዳደር የተካነ የሰው ኅይልን በድርጅቱ የገንዘብ አስተዳደር የስራ መደብ ላይ ማስቀመጥ					
10	የገንዘብ አስተዳደር ክህሎትን ማዳበር					
የገንዘብ ነክ መረጃ አጠቃቀምና ትግበራ						
11	የገንዘብ ነክ መረጃን በመጠቀም የገንዘብ ምንጮችን መሳብ					
12	የገንዘብ ነክ መረጃን በመጠቀም ወጪና ሽያጭን ጥላን ማድረግ					
13	የገንዘብ ነክ መረጃን የድርጅቱን የገንዘብ አቋም ለመቆጣጠር መጠቀም					
14	የገንዘብ ነክ መረጃን በጀት ለመበጀት መጠቀም					
15	የገንዘብ ነክ መረጃን በመጠቀም ክፍያዎችን መቆጣጠር					
16	Accounting Information System መጠቀም					
17	የገንዘብ ነክ መረጃን ለ የረዥም ጊዜ ኢንቨስትመንት ወሳኔ መጠቀም					
ተ.ቁ.	እድገትና ብልፅግና	በጥብቅ እስማማለው	አስማማለው	በከፊል እስማማለው	አልስማማም	በጥብቅ አልስማማም
18	በድርጅታችሁ ውስጥ ውጤታማ አጠቃላይ የገንዘብ አስተዳደር ተግባራት አመለካከት መኖሩ ወይም አለመኖሩ ትርፋማነት ላይ ተፅዕኖ ያሳድራል ብለው ያስባሉ					
19	በድርጅታችሁ ውስጥ ውጤታማ የገንዘብ ሞያ ዘርፍ ክህሎት መኖሩ ወይም አለመኖሩ ትርፋማነት ላይ ተፅዕኖ ያሳድራል ብለው ያስባሉ					
20	በድርጅታችሁ ውስጥ ውጤታማ የገንዘብ ነክ መረጃ አጠቃቀምና ትግበራ መኖሩ ወይም አለመኖሩ ትርፋማነት ላይ ተፅዕኖ ያሳድራል ብለው ያስባሉ					
21	በድርጅታችሁ ውስጥ ውጤታማ አጠቃላይ የገንዘብ አስተዳደር ተግባራት አመለካከት መኖሩ ወይም አለመኖሩ የገበያ ድርሻ ላይ ተፅዕኖ ያሳድራል ብለው ያስባሉ					

22	በድርጅታችሁ ውስጥ ውጤታማ የገንዘብ ሞያ ዘርፍ ክህሎት መኖሩ ወይም አለመኖሩ የገበያ ድርሻ ላይ ተዕኖ ያሳድራል ብለው ያስባሉ					
23	በድርጅታችሁ ውስጥ ውጤታማ የገንዘብ ነክ መረጃ አጠቃቀምና ትግበራ መኖሩ ወይም አለመኖሩ የገበያ ድርሻ ላይ ተዕኖ ያሳድራል ብለው ያስባሉ					
24	በድርጅታችሁ ውስጥ ውጤታማ አጠቃላይ የገንዘብ አስተዳደር ተግባራት አመለካከት መኖሩ ወይም አለመኖሩ በሰራተኛ መቅጠር አቅም ላይ ተዕኖ ያሳድራል ብለው ያስባሉ					
25	በድርጅታችሁ ውስጥ ውጤታማ የገንዘብ ሞያ ዘርፍ ክህሎት መኖሩ ወይም አለመኖሩ በሰራተኛ መቅጠር አቅም ላይ ተዕኖ ያሳድራል ብለው ያስባሉ					
26	በድርጅታችሁ ውስጥ ውጤታማ የገንዘብ ነክ መረጃ አጠቃቀምና ትግበራ መኖሩ ወይም አለመኖሩ በሰራተኛ መቅጠር አቅም ላይ ተዕኖ ያሳድራል ብለው ያስባሉ					

❖ መጨመር የሚፈልጉት ሀሳብ ወይም አስተያየት ካለ.

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በድጋሚ ለትብብራቶ አመሰግናለዎ