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Study on Financial Management in Small & Medium Enterprise [SMEs]

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Abstract: *This paper's major objective is to analyse recent research on small and medium-sized businesses in order to focus on the most important problems with SMEs' financial management. Three fundamental components of financial management are: (1) The issue of managing cash flow and liquid assets. The company's most valuable nonhuman asset is cash. (2) The issue of long-term asset purchase, which determines how a corporation will operate over the long term. (3) Concerns about funding, capital structure, and funding costs. The liquidity management issue is the most pressing one. If a company is unable to develop a suitable policy to manage its working capital successfully, it will never see the long term. Typically, the fundamental factor underpinning SMEs' issues is owner-managers' inadequate financial management.*

Keywords: Financial failure, capital structure, liquidity management, SMEs.

I. INTRODUCTION

Many people who establish their own businesses tend to avoid dealing with money-related issues. The reasons may be that they are too occupied in other business-related activities, such as managing people, sales, purchasing, and production, to have sufficient understanding of or interest in recording transactions, preparing financial statements, or analysing them. These business owners rely on their accountants to manage their company's finances.

Even though financial management is an essential component of a company's overall management, managing its assets may be the most significant aspect of this role. In the long run, an asset purchase determines the direction that the business will follow throughout the duration of that asset, but if a corporation cannot develop an acceptable working capital management policy, it will never see the long term. In reality, the fundamental factor behind the issues in SME financial management is owner-managers' subpar or nonexistent financial management.

Many small businesses fail because they are not run like businesses, not because the entrepreneur does a terrible job or offers a subpar service. The majority of small business owners only understand 50% of what it takes to be successful. They are lacking the ability to run and expand their firm. Small business entrepreneurs who are successful in this area either already know the solutions to these problems or pick them up on the job.

II. PREVIOUS RESEARCH ON SMALL BUSINESS FINANCING

The body of literature on small enterprises' financial management is fairly extensive and focuses on several facets of firm management. We only chose a small number of papers from the most recent time for our study report, focusing mostly on various financial management and small business strategy difficulties. The following table compiles research from throughout the world and highlights the key findings.

2.1 Research on the reasons why businesses fail financial failure forecast

To lessen the collapse of small firms, some studies tried to forecast small business failure. Using the following four factors, McNamara et al. (1988) created a model to predict small business failures. As a filter during the credit evaluation process, it serves the following purposes: a) to enable management to react swiftly to changing conditions; b) to educate lenders on the critical elements that determine an enterprise's propensity to fail; c) to help lending organisations in their marketing by better identifying their customers' financial needs. The authors made the case that small businesses differ significantly from large ones in terms of their ability to borrow money, the absence of long-term debt financing, and tax laws.

Bhunia (2012) looked at the connection between SME default behaviours and their owners' credit histories. Since SMEs appear to be more directly and significantly influenced by their owners than large corporations, it is important to identify and measure the credit risk of SMEs differently than that of large corporations. This will allow for the practical application of a more appropriate and efficient method of credit management of SMEs. After separating the owners' characteristics data into variables of fundamental aspects, credit capacity aspects, and credit will aspects, this study employs an empirical study of logistic regression analysis with repeat sampling data. The findings show that variables reflecting credit capacity characteristics have a stronger link with how SMEs handle credit defaults. This suggests that "credit will" factors and "personal credit" history have the strongest associations with the likelihood of default for businesses and the percentage of past-due loans. These extremely significant variables serve as useful indications in the model of default risk estimation.

2.2 Growth and development of SMEs Research on the expansion and development of small businesses

McMahon (1998, 2000, and 2001) tried to create an explanation of small- and medium-sized organisation growth that was theoretically sound and empirically validated in order to provide a broad conceptual framework for study and policy-making on the subject. The study makes the case that a conceptual framework that depicts SME growth as a series of stages of development that the business may pass through in an enterprise life-cycle should be reconsidered after critically evaluating recent research in the area.

As part of ongoing research to develop, characterise, and apply empirically based development taxonomies for SMEs in the manufacturing sector using panel data recently made available from Australia's Business Longitudinal Survey, the author significantly expanded his previously completed pilot study in the follow-up study from 2000. In order to determine whether any steady development pathways seem to be clearly visible in the data, cluster analysis was employed with key variables such as enterprise age, size, and growth variables. In order to compare the results of the cluster analysis over time, each of the four annual data collections was evaluated separately. The interpretation of the cluster analysis results is made easier by descriptive data for key enterprise parameters. The longitudinal panel data show three very steady SME development routes that can be identified using the clusters as markers or signposts. First, there appears to be a low growth path that leads to the classic or lifestyle SME configuration (around 70 per cent of the panel). The second is a pathway with modest growth that can lead to the SME setup with capped growth (around 25 per cent of the panel). The third option is a high growth route that appears to lead to the configuration of an entrepreneurial SME (around 5 per cent of the panel).

The results of a statistical analysis showed that there were highly significant disparities between the identified SME development pathways in terms of enterprise age, size, and growth characteristics. In 2001, the author revisited the subject once more in his working paper, "Stage Models of SME Growth Reconsidered."

A study of the effects of financial management traits on business growth and performance among small and medium-sized firms (SMEs) engaged in manufacturing is presented by McMahon in a paper dated 2001. According to the author, other than the usage of external finance, financial management traits are rather negligible when it comes to their influence on SME accomplishment. The two qualities of an enterprise that seem to have the most impact are development orientation and the presence of both internal and external limitations.

2.3 Model for family businesses in development

Rutherford et al. (2006) focused on family businesses and added to the literature by offering the first empirical examination of the Gersick, Davis, Hampton, and Lansberg-created Developmental Model for Family Business (DMFB) (1997). The authors were able to isolate important groupings of characteristics that can be used to explain the growth of family businesses through the testing of the DMFB model. They specifically performed hierarchical regression analysis on 934 enterprises to discover owner, firm, and family variables to supplement the DMFB. The basic model, according to the authors, offers a strong framework for categorising family enterprises, but the expanded model significantly greater variety in family firm development.

2.4 Capital structure studies on SMEs' debt levels

Using panel data of SMEs in the UK, Michaelas and Chittenden (1999) conducted quantitative study on the financial structure of SMEs. The capital structure of small and medium-sized businesses (SMEs) in the UK was examined using financial panel data. In order to develop testable hypotheses about the levels of debt in small enterprises, a variety of capital structure theories were evaluated. To test the assumptions, a number of regression models were created.

The findings indicated that the majority of the capital structure determinants described by the theory of finance appeared to be applicable to the UK small business sector. The amount of both short-term and long-term debt in small businesses appears to be influenced by a variety of factors, including size, age, profitability, growth and potential for future growth, operating risk, asset structure, stock turnover, and net debtors. The article also offers evidence to support the idea that small businesses' capital structures vary over time and by industry. The findings showed that the maturity structure of loans raised by SMEs was influenced by time and industry-specific factors.

Important research revealed that, generally speaking, typical short-term debt ratios in SMEs appear to be rising during times of economic recession and falling when business conditions improve. The average long-term debt ratio, however, shows a favourable correlation with changes in economic growth (Michaelas and Chittenden, 1999, 114).

2.5 Accounting adjustments for SMEs

The International Financial Reporting Standard for Financial Management in Small and Medium-sized Enterprises (IFRS for SMEs) and Its Effect on Financial Management were compared by Struhaová (2010). The former was used for financial reporting under Czech law (CZ GAAP). The shift-related modifications were examined in the paper. The changes that affect a firm as a whole as well as the accounting departments of SMEs were defined by the author. Also described is data from financial reporting that is used in financial management. The changes in financial reporting connected to developments affecting SMEs' financial management were also examined in the research. Similar effects for Romania and Turkey, respectively, have been assessed by Fekete et al. (2010) and Asuman Atik (2010).

2.6 Impact on profitability and performance influence of outside counsel

Robson and Bennett (2000) conducted a multivariate analysis, controlling for the impact of SME characteristics such as age, manufacturing/services, high technology and innovation, level of workforce skill, exporter, and number of competitors, to examine the relationship between SME growth and the acquisition of external business advice. Only a few sources and fields have statistically significant relationships between external business advice and SME performance. Getting outside counsel in areas like corporate strategy and hiring new employees is linked to improved firm success. Lawyers, suppliers, customers, and business friends/relatives are just a few examples of the private sector sources that have a significant influence over advice and performance. Collaboration with local suppliers has a significant positive association with increase in profitability; collaboration with national/international suppliers has a strong positive relationship with employment and turnover growth. There is scant proof that business performance and government-backed business advising firms like Business Link have statistically meaningful correlations.

Escribá-Esteve et al. (2008) concentrated on the variables that modify the association between performance and small- and medium-sized enterprises' strategic orientation. Prior research has mostly concentrated on identifying the environmental factors that support the strategic orientation approach's efficacy. The relationship between strategic orientation and performance, however, includes internal moderators that need to be investigated, according to recent study. The authors provide a contingency approach, taking into account how top management traits, business and competitive strategies, and environmental factors may mitigate this association. The study demonstrates that the environment factors, the prior experience of the top management team, and the corporate and competitive strategies created by the firm may all moderate the positive influence of the firm's strategic orientation. The study was based on a survey of 295 Spanish small and medium-sized enterprises from seven manufacturing sectors.

The literature on financial management in small businesses is quite diverse and draws from many facets of business operations. The initial focus of research on SMEs default risk and bankruptcies has expanded to include studies on capital budgeting, small business development and growth models, and the connection between default behaviours of SMEs and the credit profiles of their owners. The capital structure, working capital management, and financing trends were all fascinating areas to look into.

In this essay, we'll focus on two key topics: working capital management and the risks businesses run when investing a sizable amount of their cash in long-term assets.

III. CONCLUSION

Outcome of this study should be used to the following suggestions for small businesses.

There is a need for further information on fundamental financial principles, which can be obtained through reading books or publications or by attending workshops on the subject. It is meant to draw attention to the reality that owner-managers frequently have expertise or training in only a few functional areas, despite the fact that they must handle every element of their small businesses with very little internal and external support. Due to the fact that they could be making everything from phone conversations to product orders, this is also not always or typically enforced.

According to one school of thought, "well-run corporate enterprises should be as attentive of their money as healthy and fit people are of their breathing." Production, marketing, distribution, and related activities must be achievable without consistently putting financial pressure on the company. But that doesn't imply a small business owner-manager can ignore financial management or, as is sometimes done, delegate it to an accountant. The owner-managers of successful small businesses themselves have a good understanding of the concepts of financial management and are actively involved in applying them to their own circumstances, whether it is visible to the casual observer or not.

The questions brought up in this research study are intended to spark additional theoretical and empirical contributions on this somewhat understudied but crucial area of small company research.

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