

# Role of Financial Planning on Performance of Small and Medium Scale Enterprises

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**Abstract:** *Small and Medium enterprises (SMEs) contributes immensely to economic growth and social development of any country. Majority of SMEs have failed to recognize the importance of proper financial planning towards successive operation and output performance. The study sought to assess the roles of financial planning on performance of small and medium scale enterprises in Nigeria. Primary data was used for this study and they were sourced from Centremog Limited in Ibadan through administration of structured questionnaire. The research used simple random sampling technique. Survey research design method was used via structured questionnaire. A well-structured questionnaires were given to respondents working at Centremog limited. A total number of fifty (50) questionnaires were administered and retrieved from staffs at Centremog Limited. The data collected were analyzed using descriptive statistics such as tables, charts, frequencies, percentages while hypotheses were tested by using the chi-square ( $X^2$ ) method. The results showed that SMEs adopt financial planning systems and there was a link between financial planning and organisational survival. Also, financial planning had positive effect on organisation profitability. The findings revealed that most SMEs had adopted several financial planning strategies with cash management, accounting receivable management, inventory management and investment significantly influencing SME's Return on Investments. The study recommends SMEs to deepen their financial planning strategies and align them with their returns on investment goals. Also, Financial training programmes should be arranged for SMEs to enable them sharpen and enhance their petty financial skills and to help them in their operations*

**Keywords:** Financial planning, Small and medium enterprises, Investment planning, Financial reporting, Centremog Limited, Chi-square

## 1. INTRODUCTION

Small and medium-sized enterprises (SMEs) plays a pivotal roles in the business growth and economic development of countries; however, for successful growth and development of SMEs, funding is fundamental and paramount [1, 2]. In order to encourage the development of enterprise in Nigeria, Financing SMEs is necessary [2]. SMEs account for approximately 96% of the country's businesses and are important part of Nigeria's economy [2].

SMEs encounter a wide range of problems, despite roles they played, the hope that it is envisaged to bring, and their contribution to economy of countries. Though close to one million small enterprises are established each year, Of all established small enterprises established in a year, at least 40% of them close within one year and 80% of them will be out of business within 5 years and 96% will be closed by their 10th year (Gerber, 2001). This clearly shown a serious challenge to the Sector and there is need to expedite action for unified interventions in order to change the trend. Lack of capital, poor managerial experience, lack of capacity to respond to emerging challenges and poor planning are current problems impeding the growth of SMEs in Nigeria [3].

One of the major problems facing small and medium scale enterprises in Nigeria is paucity of fund, for business development. Majority of people operating this type of firms rely solely on loan and credit facility from banks and other financial institutions. Apart from credit facility from various financial bodies, there has been a little support from government and private organization and such assistance involves little or no interest. Recently, the effort from government is taking new direction as a result of failure of operators of small and medium scale enterprises to fulfil their own part of agreement. Majority of owners of small and medium scale businesses are presently running away from government aids/packages/stimulus because of stringent measures and others procedural steps attached to it.

Presently, many SMEs in Nigeria are forced to close down their businesses because of unavailability of sufficient capital to stay in business and inability to access the necessary funds to boost their operation [2]. Weak capital base, poor financial records of SMEs, and market competition are reasons why most commercial banks find it challenging to cover the high costs of credit associated with lending to SMEs [1]. Despite several efforts targeted at bringing last solutions to aforementioned challenges facing smooth operation of SMEs in Nigeria, the problems still persisted and the fall out of dismal operation is affecting economy growth likewise crippling development of a country as a whole. In order to revive the closed down enterprises and enhance normal functioning of the existing one, effort should shift toward proper financial planning.

Financial planning is a continuous process that seeks to direct and allocate financial resources towards the attainment of strategic goals of an enterprise (Gerber, 2001). The result of any financial planning process is a defined financial plan and a guiding tool for revenue and expenditure usually in the form of budgets. Financial planning encompasses a number of considerations in its formulation that must be considered based on the objectives and the context in which planning takes place. Maintenance of optimal cash levels sets the foundation on which the business can minimize liquidity risks while maximizing on its income generating abilities by minimizing idle financial resources.

The core objective in any financial planning process is cash flow optimization, this is as a result of its influence on other financial performance outcomes [4]. To generate either a positive or a negative impact on an enterprise or business, investment choices play a vital role. There is possibility of significant increase in negative returns in a situation where investments are not aligned with cash flow projections and cost of capital. Poor and improper financial planning opens up uncertainty that unduly increases the vulnerability of an enterprise to both internal and external shocks.

Financial planning remains to be a very important survival tool for business intending to make any significant growth especially among Small and Micro Enterprises facing capital limitations and hostile operating environment. However, with a high investment in SME by both the government and non-governmental agencies on financial management practices, the continued trend of failure is least justified putting into question, the effectiveness of their financial planning strategies. If growth and largeness reduce failure, then there is need for concerted efforts in finding the roles of the financial planning on control of SMEs, the essence on which this study sought to establish.

It is believed that a key organizational success factor is sound financial planning and management, while a stable sound financial management system to efficiently govern the incomes, expenses, assets and liabilities of the organization is key to organizational performance. Hence, this study therefore was conducted to investigate the roles of financial planning on control of small and medium scale enterprises, case study of Centremog Limited.

### **1.1 Statement of the Problem**

Small and Medium-Sized Entities are important for national development. This entities accounts for about 85 percent of manufacturing employment and contribute significantly to the economic growth of Nigeria. In spite of the invaluable contributions of SMEs, they are fraught with a myriad of challenges threatening the very fabric of their survival. It is argued that a larger number of SMEs do not survive beyond their fifth anniversary.

The failure of SMEs business in the first 5 years of their operation in Nigeria is links to inadequate preparation for financial management and poor control of financial planning [5]. Inadequate preparation of the owners for financial management and planning is a major factor responsible for failure of the Ninety-two percent of SMEs in business within the first 5 years [6, 7]. Also, 60% of SMEs are unable to make a profit from the date of inception to the closing of the business as a result of similar problem.

One of the challenges confronting SMEs in Nigeria is the management of finance [8, 5] One of the most challenging problem is that the financial management and planning tasks required and needed for the effective management and prompt operation of SMEs in Nigeria are not taught explicitly to SMEs' owners before they assume responsibilities as leaders of their businesses. So, most SME owners are inadequately prepared to perform the financial management required for business sustainability in Nigeria [6].

Starting and operating a small business includes a possibility of success as well as failure [9]. Because of their small size, a simple management mistake is likely to lead to sure death of a small enterprise hence no opportunity to learn from its past mistakes. This may be attributed to lack of planning, improper financing and poor management has been cited as the main causes of failure of small enterprises in Nigeria. Though it is clear that SMEs play a critical role in economic development the rate in which newly established SMEs collapsing it is wanting. It is against this realization that the current study aims to investigate the role of financial planning on control of small and medium scale enterprises in Nigeria with the case study of Centremog Limited, Ibadan, Oyo State.

## 1.2 Research Objectives

The main objective of the study is to examine the role of financial planning on performance of Small and Medium scale enterprises in Nigeria with case study of Centremog Limited, Ibadan, Oyo State.

### Specific Objectives

- i. To examine the extent of adoption of financial planning systems by Small and Medium Scale Enterprises
- ii. To determine the link between financial planning and organizational survival
- iii. To assess the effect of financial planning on organization profitability

### Research Hypotheses

To provide answers to these research objectives the following hypothesis will be tested

- i. SMEs does not adopt financial planning systems
- ii. There is no link between financial planning and organisational survival
- iii. Financial planning do not have effect on organisation profitability

## 2. LITERATURE REVIEW

### 2.1 Conceptual review

The word SMEs covers a wide range of perceptions and measures, varying from country to country and between the sources reporting SME statistics. Some of the commonly used criteria are the number of employees, total net assets, sales and investment level. However, the most common definition used is based on employment, but, there is a variation in defining the upper and lower size limit of an SME [10].

The capital involved, revenue, and number of workers are yardsticks for SMEs classification in Nigeria [6]. One of such classification indicates that an SME is an enterprise with an asset base (without land) of between N5 million and N500 million (\$138,888 to \$1,388,888), and with a labor force of between 11 and 300 employees [6]. This definition is adopted by Small and Medium Enterprises Credit Guarantee Scheme (SMEECGS) in Nigeria [1].

In spite of the absent of a universal definition for small and medium scale enterprises (SMEs) there is a general consensus regarding the variable used in identifying SMEs, the critical include capital investment fixed assets annual turnover gross output and employment.

According to CBN publication [11], SMEs is defined small scale industries as those with annual turnover, SMEs defined enterprises with a maximum assets base of 200 million excluding land and working capital with number of staff employed by the enterprises of not less than 10 and not more than 300.

Enterprises may be classified by size, sector, organisation, technology and location. From the perspective of policy and planning, size provides the most practical basis for classification. The usual criteria include one or more of the following; employment, turnover, assets, and paid-up capital [12]. However, definitions vary from country to country relative to the overall size and structure of the domestic economy.

In countries such as the USA, Britain, and Canada, small-scale business is defined in terms of annual turnover and the number of paid employees. In Britain for instance, small-scale business is defined as that industry with an annual turnover of 2 million pounds or less with fewer than 200 paid employees.

According to the European Commission (EC) Small enterprises are defined as those employing less than 50 persons and with annual sales or total assets that do not exceed \$13 million, while, micro enterprises are defined as those which employ fewer than 10 persons and with annual sales or total assets that do not exceed \$3 million.

In Japan, small-scale industry is defined according to the type of industry, paid-up capital and number of paid employees. Consequently, small and medium-scale enterprises are defined as: those in manufacturing with 100 million yen paid-up capital and 300 employees, those in wholesale trade with 30 million yen paid-up capital and 100 employees, and those in the retail and service trades with 10 million yen paid-up capital and 50 employees [13].

In Nigeria, the Third National Development plan defined a small scale business as a manufacturing establishment employing less than ten people, or whose investment in machinery and equipment does not exceed six hundred thousand naira.

The Federal Government Small Scale Industry Development Plan of 1980 defined a small scale business in Nigeria as any manufacturing process or service industry, with a capital not exceeding N150, 000 in manufacturing and equipment alone.

The small scale industries association of Nigeria (1973) defined small scale business as those having investment (i.e. capital, land, building, and equipment of up to N60, 000 pre-SAP Value) and employing not more than fifty persons.

The Federal Ministry of Industries defined it as those enterprises that cost not more than N500,000 (pre-SAP Value) including working capital to set up.

The Centre for Management Development (CMD) view of small industry in the policy proposal submitted to the federal government in 1982, defined small scale industry as, —a manufacturing processing, or servicing industry involved in a factory of production type of operation, employing up to 50 full-time workers.

Ogechukwu et al (2013), were of the view that Small scale business, small scale industries and small scale entrepreneurship are used interchangeably to man a small scale industry firm.

## 2.2 Empirical Review

Olagunju [15] explained planning as a set of managerial activities designed to prepare the organization for the future and ensure that decisions regarding the use of people and resources to achieve organizational objectives are taken. Planning is particularly critical in small firms because of its extensive resources. A plan establishes the basic objective of the firm, determines how these objectives can be attained, puts into consideration various aspects of the environment and determines the amount of resources necessary for successful implementation [16].

Egbuna and Agali [17] findings on an effect of planning on the performance of small and medium enterprises in south-western Nigeria show that inability to gain access to source of finance among other problems is a major challenge facing SMEs. From the study, one can deduce that accessing financial source without difficulty by the SMEs contributes meaningfully to the overall performance of its activities.

In the view of Adigwe [18] on project finance for small and medium scale enterprises, he sees consistent policies changing as an obstacle for SMEs in accessing financial assistance from formal source like banks which is in most cases affecting the smooth running of the business.

Furthermore, SAEED [19] in his study on Formality of Financial Sources and Firm Growth: Empirical Evidence from Brazilian SMEs 1999-2005 revealed that internal or owners’ funds and formal sources of finance had been found significantly related to the performance of SMEs and that informal source of finance seem not significantly related to SMEs performance. It stressed further that developed financial institutions is imperative to firm’s growth in developing countries.

## 3. METHODOLOGY

### 3.1 Research Design

This work used a descriptive research design. This design define a subject by creating a profile of a group of problems, people, or events, through the collection of data and tabulation of the frequencies on research variables or their interaction, (Cooper & Schindler, 2006). It involves describing the characteristics of a particular individual, or of a group. In this study, the focus is to examine the role of financial planning on control of small and medium scale enterprises in Nigeria, with a case study of Centremog Limited (farm, water factory, Laboratory and herbal), Ibadan, Oyo State. The research design employed in this work defines questions, people surveyed, and the method of analysis before data collection.

### 3.2 Population

The population used in this work is respondents from Centremog Limited (farm, water factory, Laboratory and herbal), Ibadan, Oyo State. Centremog Limited is consist of four subsidiaries which include farm, water factory, Laboratory and herbal (Table 1). Fifty (50) respondents were selected from four subsidiaries (farm, water factory, Laboratory and herbal) of Centremog Limited (Table 1)

### 3.3 Sample Population

The study used simple random sampling technique in coming up with the sample of the study. A well-structured questionnaire was prepared were administered on fifty (50) respondents from CENTREM OG LIMITED (farm, water factory, Laboratory and herbal) Table 1.

Table 1: Quantity of Questionnaire Distributed and Retrieved from Staffs of Centremog Limited, Oyo State

S/N	Centremog Limited Subsidiary	Quantity of Questionnaire Administered and Retrieved
1	Farm	15
2	Water factory	15
3	Laboratory	10
4	Herbal	10
TOTAL		50

Source: Field Survey, 2020

### 3.5 Data Analysis

The data were analyzed using frequency distribution while the hypotheses were tested using the chi-square test. The tools used in analyzing the data in this work include; tables, frequency and simple percentage method and chi-square method.

## 4. RESULTS AND DISCUSSION

The analysis and presentation of data is reported through the questionnaires distributed which were also retrieved in order to ascertain the role of financial planning on control of small and medium scale enterprises, case study of Centremog Limited (farm, water factory, Laboratory and herbal), Ibadan, Oyo State. The responses were collected and chi-square method adopted in analyzing the responses and testing the hypothesis. A total of fifty (50) copies of the questionnaires were administered and all were retrieved after adequate filling.

### 4.1 Respondents' characteristics and classifications

**Table 2: Responses Related to the Bio data Variables of the Respondents from Centremog Limited**

S/N	CLASSIFICATION	ITEMS	FREQUENCY	PERCENTAGE %	TOTAL %
1	Gender	Male	38	76	100
		Female	12	24	
2	Age	Below 25 years	8	16	100
		25-35 years	20	40	
		36-45 years	15	30	
		Above 45 years	7	14	
3	Education Background	WAEC/NECO	5	10	100
		ND/NCE	13	26	
		HND/B.Sc	18	36	
		MBA/M.Sc	8	16	
		Professional	6	12	
4	Working Experience	1-2 years	15	30	100
		3-5 years	20	40	
		5 years and above	15	30	
5	Business Ownership	Sole proprietorship	-	-	100
		Partnership	50	100	
		Family Business	-	-	
		Limited liability	-	-	

Source: Field Survey, 2020

Table 2 shows that thirty eight (38) respondents representing 76% of the sample size were males while twelve (12) respondents representing 24% of the sample size were females. Eight (8) respondents representing sixteen (16%) percentage of the sample size were of the age group below 25 years, twenty (20) respondents representing 40% of the sample size were of the age group 25-35 years, fifteen (15) respondents representing 30% of the sample size were of the age group 36- 45years while option above 45 years attracted seven (7) respondents representing 14%. Thus, majority of the respondents were of the age group 24-35 years. Five (5) respondents representing 10% of the sample size were secondary school leavers, thirteen (13) respondents representing 26% of the sample size were ND/NCE holders, eighteen (18) respondents representing 36% of the sample size were HND/B.Sc holders, eight (8) respondents representing 16% of the sample size were MBA/M.Sc holders while another six (6) respondents representing 12% of the sample size were professionals. Thus, majority of the respondents were HND/B.Sc holders. Fifteen (15) respondents representing 30% of the sample size have been on the job for period of 1-2 years, twenty (20) respondents representing 40% of the sample size have been on the job for a period of 3-5 years, fifteen (15) respondents representing 30% of the sample size have been on the job for a period above 5 years and above. The business ownership indicated in table 6 shows that all respondents agreed that the business is partnership business

### 4.2 Analysis of the research question and testing of the research hypothesis

**Table 3: Respondents view on whether Small and Medium Scale Enterprises adopts financial planning system**

Responses	Number of Respondents	Percentage (%)
Yes	50	100
No	0	0
<b>Total</b>	<b>50</b>	<b>100</b>

Source: Field Survey 2020.

From Table 3, it is shown that all the respondents agreed that the business adopts financial planning system.

#### 4.2.1 Financial planning system adoption in SMEs

**Table 4: Respondents View Related to Cash Management**

S/N	Cash Management	Responses	Number of Respondents	Percentage (%)
1	Responses Related to whether the business sell services/goods by cash	Yes	40	80
		NO	10	20
		Total	50	100
2	: Does the business give cash receipts to customers?	Yes	45	90
		No	5	10
		Total	50	100
3	Responses Related to whether the business make cash flow projections	Yes	20	40
		No	30	60
		Total	50	100
4	Responses Related to whether the business carry out daily cash reconciliation	Yes	50	100
		No	0	0
		Total	50	100
5	Responses Related to whether the business maintain a cash operating limit	Yes	43	86
		No	7	14
		Total	50	100
6	Respondents View on if the business have a full time cashier	Yes	40	80
		No	10	20
		Total	50	100

Source: Field Survey 2020.

From above (Table 4), it can be seen that majority of the respondents declared that the company adopts cash management system in which forty (80%) respondents agreed that business sells goods and services by cash while ten (20%) respondents disagree. Forty-five (90%) respondents agreed business gives cash receipts while five (10%) respondents said their company does not give cash receipt to the customers. (Table 4). Above table (Table 4) shows that twenty (40%) respondents said business makes cash flow projections and thirty (60%) respondents said company does not make cash flow projection. All respondents in this study agreed that they carry out daily cash reconciliation (Table 4). Forty three (86%) respondents agreed business maintain a cash operating limit while seven (14%) respondents view is contrary to this submission. Forty (80%) respondents said business have a full time cashier while opinion of ten (20%) respondents is different (Table 4)

#### 4.2.2 Account Receivable Management and Inventory Management

**Table 5: Respondents View Related to Account Receivable Management and Inventory Management**

S/N	Account Receivable Management	Responses	Number of Respondents	Percentage (%)
1	Responses Related to whether the business sell services/goods by credit	Yes	6	12
		No	44	88
		Total	50	100
2	Respondents View on whether the business prepare an aging schedule	Yes	46	92
		No	4	8
		Total	50	100
3	Responses Related on whether the business have a credit policy	Yes	35	70
		No	15	30
		Total	50	100
<b>Inventory Management</b>				
4	Respondents View on whether there is any inventory register	Yes	50	100
		No	0	0
		Total	0	100
5	Responses related to whether period summaries of inventory usage are prepared	Yes	49	98
		No	1	2
		Total	50	100
6	Respondents View on whether the business carry out period inventory counts	Yes	48	96
		No	2	4
		Total	50	100

7	Responses related to whether the business use computer assisted software in managing inventory	Yes	40	80
		No	10	20
			50	100

Source: Field Survey 2020.

From Table 5, majority of respondents declared that business does not sell goods/service on credit, with six (12%) agreed to the disposition of selling goods on credit while forty four (88%) respondents disagreed. Forty six (92) of the respondents said business prepare aging schedule while four (8%) respondents were of view that business did not prepare for aging schedule (Table 5). This study shows that thirty five (70%) said business has credit policy and fifteen (30%) said business does not have credit policy (Table 5). Fifty (100%) of respondents agreed that there is an inventory register for the business (Table 5). Forty nine (98%) of respondents agreed that there are period summaries of inventory usage and one (2%) said there is not. Forty eight (96%) respondents said business carry out period inventory counts while two (4%) respondents said the business did not carry out period inventory counts (Table 5). The table above (Table 5) shows that forty (80%) of respondents said business used computer assisted software in managing inventory while ten (20%) respondents were of opinion that business did not use computer assisted software in managing inventory.

#### 4.2.3 Investment, Financial reporting and analysis

Table 6: Respondents View Related to Investment, Financial reporting and analysis

S/N	Investment	Responses	Number of Respondents	Percentage %
1	Respondents View on whether the business invested in long term assets	Yes	50	100
		No	0	0
		Total	50	100
2	Responses view on whether the business invested in short term assets	Yes	50	100
		No	0	0
		Total	50	100
3	Respondents View on whether the business seek professional advice before investing	Yes	50	100
		No	0	0
		Total	50	100
4	<b>Financial reporting and analysis</b> Respondent View on whether the business prepare financial statements	Yes	50	100
		No	0	0
		Total	50	100



5	Responses related to whether the business the engage the services of a qualified accountant	Yes	40	80
		No	10	20
		Total	50	100

Source: Field Survey 2020.

For investment, all respondents agreed that business invested in short and long term assets (Table 6). All fifty (100%) respondents agreed that said business seeks professional advice before investing (Table 6). All the respondents said the business prepare financial statements (Table 6). Forty (80%) of respondents said businesses do engage the services of a qualified accountant and ten (20%) of respondents said they do not (Table 6).

Table 7: Determination whether there is a link between financial planning and organizational survival

Centremog Limited Subsidiary	Duration of operation	Financial planning
Farm	Above 5 years	Yes
Water Factory	Above 5 years	Yes
Laboratory	Above 5 years	Yes
Herbal	Above 5 years	Yes

Source: Field Survey 2020.

From Table 7 above, it can be seen that the companies adopts financial planning system and has been surviving for the past five years. This shows that adopting a proper financial planning system can help encourage company survival.

**Hypothesis**

**H. Financial planning do not have positive on organization profitability**

Using the Chi-square ( $X^2$ ) Method for Computation

Responses	O	E	O-E	(O-E) <sup>2</sup>	$\frac{(O - E)^2}{E}$	X <sup>2</sup>	P
YES	45	25	20	400	16	32	<.001
NO	5	25	-20	400	16		

Source: Field Survey 2020.

From the calculations above chi( $X^2$ ) calculated value of 32 is greater than chi ( $X^2$ ) critical value of 2.49 at P <0.001 level of significance. Thus, Ho is rejected and H<sub>1</sub> accepted. Therefore, financial planning have positive effect on organization profitability.

**Interpretation**

From the analysis above,  $x^2$  calculated value is 32 while  $x^2$  tabulated value is 2.49. This shows that  $x^2$  calculated of 5.94 is greater than  $x^2$  tabulated of 2.49 i.e  $x^2$  calculated (32) >  $x^2$  tabulated of 2.49. Therefore, there is a strong link between financial planning and organization profitability

**5. CONCLUSION**

**Key findings**

Majority of SMEs moderately adhered to financial planning practices. There was also a strong positive relationship between adherence to financial planning and profitability of SMEs, so adherence to financial management practices and planning has positive effects on profitability.

**Based on the analysis and findings, the study concludes that:**

The financial management and planning practices employed in CENTREMOG LIMITED, include cash management, account receivable management, accounting receivable management, inventory management and investment. The study therefore rejects the hypothesis that SMEs in in CENTREMOG LIMITED employ no financial planning system.

From the above study,  $\chi^2$  calculated value is 32 while  $\chi^2$  tabulated values is 2.49. This shows that  $\chi^2$  calculated of 5.94 is greater than  $\chi^2$  tabulated of 2.49 i.e  $\chi^2$  calculated (32) >  $\chi^2$  tabulated of 2.49. Therefore, there is a strong link between financial planning and organization profitability. Finally, adherence to financial management and planning practices has positive effects on profitability. The study therefore rejects the hypothesis that financial planning has no effect on the Profitability of SMEs

**Recommendations**

The study strongly recommends higher adherence to financial management practices. Specifically: Financial training programmes should be arranged for SMEs to enable them sharpen and enhance their petty financial skills and to help them in their operations; SMEs should also strictly abide by working capital management principle; Proper and appropriate investment and financing decisions should be taken seriously by SMEs. Finally, SMEs should regularly do financial planning, reporting and analysis to be able to identify financial weaknesses early enough.

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