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Prepared by: Tilahun Begashaw Ayalkbet - GSD/1863/11

Advisor: Mengistu Bogale (PhD)

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Financial Management Decision Making Challenges - The case of Small and Medium Enterprises (SMEs) - In Addis Ababa city, Ethiopia

Prepared by: Tilahun Begashaw

Approved by a board of Examiners and Advisor:

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Advisor	Signature	Date
______________________	_______________	________________
Internal Examiner	Signature	Date
______________________	_______________	________________
External Examiner	Signature	Date

Student Declaration

I, the undersigned, declare that this project paper is a result of my independent research work on the topic entitled "Financial Management Decision Making Challenges - The case of Small and Medium Enterprises (SMEs) - in Addis Ababa city, Ethiopia'' the partial fulfillment of the requirements of Master of Business Leadership at Addis Ababa University, School of commerce. This project paper is original in nature and has not been submitted to any other college, institution or university. All the references are also duly acknowledged.

Name: Tilahun Begashaw

ID No: GSD/1863/11

Signed: ______________________

Date: ______________________

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Abstract

The purpose of this article is to uncover the principal obstacles preventing small and medium business owner or hired managers from making sound financial management decisions. These obstacles are generally related to the owner managers' reluctance to follow accepted theoretical norms (steps) in terms of information search and analysis. This reluctance is attributable to the decision makers' significant lack of knowledge and experience.

Data gathered with a structured questionnaire based on a sample of 200 from total population of 2021 small and medium enterprises registered with Addis Ababa Administration Trade and Industry office.

The study identified and studied on three broad principal factors that lead to inefficiencies in financial decisions making process. These broad factors are decision maker (business owner or manager) capacity and behavior, financial management practice, and non financial information consideration of the SMEs.

This study adapted purposeful sampling approach and used descriptive qualitative method. Data were collected using survey method and analyzed using descriptive analysis. Data sources were primary and secondary.

The results indicated that the three core-factors have significant contribution to influence decision-making process at SMEs in Addis Ababa. These results point to an absence of a proper theoretical framework for gathering and analyzing information necessary for effective decision making. Recommendations were also made to assist small and medium business owner managers to improve on their strategic decision making and resource allocation processes.

Acronyms

SME – Small and Medium Enterprise

WBG – World Bank Group

TL - Turkish lira

GDP – Gross Domestic Product

OECD - Organization for Economic Co-operation and Development

SEDA - Small Enterprise Development Agency

AABE - Accounting and Auditing Board of Ethiopia

EC – Ethiopian Calendar

GC – Gregorian calendar

GAAP – General Accepted Accounting Principles

IAS – International Accounting Standard

SPSS - Statistical Package for Social Sciences

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Chapter One - Introduction

1.1. Back ground of the study

The research focused on inhabiting factors in financial decision making process in SMEs that operated in Addis Ababa, Ethiopia which is the commercial center that has been growing at faster rate due to its strategic location and focal point of many international activities. The need for research on small and medium enterprises (SMEs) is because SMEs are regarded as the economic engine necessary for growth, poverty alleviation, job creation as well as ensuring a country's economic stability. The SME sectors are viewed as essential component of modern industrialized societies. SMEs play significant role in employment and income generation, producing import substituting products, mitigating rural-urban drift and mobilization of local resources (Ernst and Young, 2011). Governments and local communities worldwide have recognized that small and medium businesses are key to building prosperity and to stimulate economic growth (Fatoki, 2014: 100). Globally, small and medium businesses are regarded as the economic engine necessary for growth, poverty alleviation, and job creation (Smith and Chimucheka, 2014:160).

Consequently, it is worthwhile to assess the SMEs financial decision making efficiency and effectiveness as enablers of SMEs financial performance betterment. Effective SMEs financial decision contributes to the nation`s GDP and helps in jobs creation, and solving unemployment crises, while SMEs ineffective and inefficient financial decision lead to issues, such as low job creation, reduce its contribution to GDP and increase unemployment crises.

One of the leading factors contributing to ineffective and inefficient financial decision making is limited business financial information which are born from factors related to financial literacy, inappropriate financial management practices, weak feedback system and inappropriate strategies and objectives in SMEs. A background study for this intervention by the World Bank Group (WBG) in August 2020 identified that SMEs are constrained by limited business financial information which otherwise could have improved their business decisions.

Review of the literature and the practical evidence available give the impression that SMEs financial decision making in Ethiopia did not follow the theoretical standards. Therefore, it has become important to understand the inhabiting factors that deter to follow the theories of financial decision making process in SMEs so that their significance and importance can be identified and analyzed. As a result, this study aims to provide empirical evidence about the main inhibiting factors that detract from effective and efficient financial management decision making in Small and Medium Size Enterprise (SMEs). The process of making financial management decision is a complex and dynamic process involves analysis of number a number of factors closely associated with this phenomenon which include information search and analysis, risk and option consideration, efficiency in financial management practice, competency of employees in the firms, decision maker capacity, feedback system, existence of clear objectives of the firms and others. However, for this study, the three broad internal factors that are considered by the researcher are decision maker financial management capacity and behavior (financial literacy), financial management practice, and non financial information consideration of the SMEs.

1.2. Statement of the problem

The analytical model for decision making in small and medium size enterprise businesses in developed countries indicates that the decision maker is at the centre of the process, and provides an explanation of how strategic financial management decisions are made. However, lack of practical skills in financial management for decision making is vast amount barriers in SMEs in developing countries including Ethiopia.

Small and medium businesses in Ethiopia do not follow the necessary theoretical steps in terms of information search and analysis, risk and option consideration. The decision makers tend to focus more on the event than on the process. This explains why the decision making process in small and medium businesses is much less complex than suggested by theoretical models. There is an unconscious motion through the process, without due consideration of the actual steps to the final decision. A number of factors closely associated with this phenomenon emerge, including the small and medium business owner manager financial management literacy (educational qualification, training and experience); efficiency and effectiveness of financial management practice; clear objectives of firm; and feedback system in the firms among others. Little has been done in the literature to date to explain this anomalous practice in small and medium business. Many studies tend to focus on the functions within small and medium businesses, explaining or describing the mechanisms by which they arrive at final decisions.

The possibility of business failure due to lack of sound financial management decision making in Ethiopia became a serious issues that seeks special attentions. This study focuses on and identifies the principal factors and tackles on the principal reason why most small and medium businesses do not practice the theory in financial decision making process.

1.3. Research Questions

The research questions that the researcher developed to guide this study were the following:

i. What are the financial management skill gaps of SMEs owner or hired managers to make an effective and efficient financial decision making?

ii. What are the financial management practices that owner managers required to implement adequately to use the output as a strategic tool for overcoming the financial management decision making hindrance?

iii. How SMEs implemented feedback system as a tool to evaluate and control the outcomes of decisions in terms of the decision is being implemented, what results are obtained, and what adjustments are necessary to enhance those results?

iv. How small and medium business owner managers consider business objectives while they are making financial management decisions?

1.4. General and specific objectives of the study

1.4.1. General objective

The general objective of this study is to investigate and describe the main inhibiting factors that detract from effective and efficient financial management decision making in Small and Medium Size Enterprise (SMEs).

1.4.2. Specific objectives of the study

The specific objectives of the study are:

i. Understand and analyze skill gaps of SMEs owner or hired mangers which hider them to make an effective financial decision milking.
ii. Understand and analyze deterrent factors to make effective and efficient financial decision making related to financial management practices of SMEs.
iii. Suggest that future studies include more cases and other factors closely associated with financial decision making.
iv. Recommend that all concerned stakeholders give due diligence on SMEs financial operation and financial decision making.

1.5. Significant of the study

This study will contributes to the academic field of financial management decision through a suggestion as to the reasons for unsound decisions in small and medium business and citation of future study. It will be also significant for Small and Medium Enterprise (SMEs) to get them the concept that the effect of financial management decision making on performance of their business. In addition the study will contribute to a better understanding of the attitudes of SMEs business owners and managers toward financial decision-making. It will also be used for strategy creators to use the information gained from this study for their design and formulation regarding financial operation of the country.

1.6. Scope of the study

The study was employed with sample of 200 small and medium enterprises registered with Addis Ababa Administration Trade and Industry office and had business license and operating in ten sub cities in Addis. The study identified and studied on three broad principal factors that lead to inefficiencies in financial decisions making process. These are decision maker (business owner or manager) capacity and behavior, financial management practice, and non financial information consideration of the SMEs.

1.7. Definition of key words

1.7.1. Financial decision in SMEs

Financial decision making is the process of determining the most effective choice of action from a range of alternatives, in order to ensure the best outcome. Financial decision-making for small and medium businesses involves making decisions that will shape the financial fortunes of the business and maximize returns for the business owner(s).

1.7.2. Determinant factors of financial decision making

During the process of decision-making, starting from identification of the problem to a decision taking, there are many factors that could influence a decision. They could be the personality and capacity of decision maker, the state of organization, internal and external situation in organization as well as availability of information. Understanding how important these factors can be the best strategy to improve timely, reliable, accuracy, effectively and accountability of the decisions that eventually made.

1.7.3. Owner manager

Owner managers of SME are workers who hold a job in an incorporated enterprise, in which they alone, or together with other members of their families or one or a few partners, hold controlling ownership of the enterprise. The characteristics of owner manger are less concern with formal system, their decision making is more judgmental, involving fewer individuals in the decision making, and their decision is quicker.

1.7.4. Inhabiting factors in financial decision making

Inhabiting factors are commonly referred to as barriers. Financial decisions making inhabiting factors refer to the inability of decision maker to make financial decisions that drive the organization’s objectives.

1.7.5. Financial management

Financial management is the practice of handling a company's finances in a way that allows it to be successful and compliant with regulations. It is the business function of planning, organizing, directing, and controlling of financial undertakings in an organization and it is and a means to carry out its objective as satisfactorily as possible.

1.8. Limitation of the study

The study has a limitation regarding the target population group, which are not be representative of the entire population of SMEs in Ethiopia. The study further concerns the small and medium business sector only, excluding micro and large business group. It also limits itself to only the financial management aspects of the small and medium business, precluding other functions such as marketing, human resource, or production.

This study was based on a small sample of 200 cases and limited to the City of Addis Ababa. It is a descriptive study, setting the stage for further rigorous research in the field in whole of where there is a scarcity of research on financial management decision making. The researcher suggest that future studies should include more cases and other factors closely associated with financial management decision making, including information search and analysis, risk and option consideration, financial management attitude of owners, use of information technology, legal form of organization, pattern of ownership, liquidity position, asset structure, state of economy, government regulation, tax policy and size and age of enterprise. This would then enable results to be generalized, to provide a better and more detailed picture of which practices are followed by SMEs.

1.9. Organization of the study

This research documents are organized into five chapters. The first one is the introduction section which describes back ground of the study, statement of the problem, general and specific objectives, significance of the study, scope of the study, definition of key words, limitation of the study, and organization of the paper. The second chapter illustrates literature review. The third chapter deals with the research methodology which describes research design, research approach, research site and unit of analysis, sample size, sampling method, data collection method and instrument, pretesting, and data analysis. Chapter four includes presentation and discussion of the findings. Conclusion and recommendation is presented in fifth chapter.

Chapter Two - Literature Review

2.1 Decision making process

Decision-making is usually defined as a process or sequence of activities involving stages of problem recognition, search for information, definition of alternatives and the selection of an actor of one from two or more alternatives consistent with the ranked preferences. Decision making is very important activity for the process of choosing an alternative option from a situation that show good results to individual or investors. It begins with presence of problems or issues that must be solved in order to achieve the goals of organization. Identification and understanding of a problem considered as the basis for determining the next steps to be taken in decision making process.

This study considers two decision making theories (traditional and behavioral economics) to support the study how rational SMEs business owner or hiring managers behave under risk and uncertainty. Behavioral economics is about understanding common decision mistakes that people make and why they make them. This misconception stems from the fact that traditional economic theory assumes all people are rational, while behavioral economics does not make this assumption.

The theory of decision-making process in the literature is mostly base on a “traditional” model from Mintzberg (1976). Traditional economic theory relies on three fundamental assumptions, such as people are rational, people make decisions based on self-interest, and people will change their thoughts and beliefs based on new information. According to traditional economics, in an ideal world, people would always make the best decisions based on a careful analysis of the costs and benefits of each option available to them.

This idea assumes that rational people are unaffected by external factors and emotions and are capable of making decisions based purely on what would benefit them the most.

According to authors such as Corr et al. (2018), and Thaler (2015), behavioral economics focuses on understanding human psychology and particularly why people deviate from rational actions when they make decisions. The researchers confirm that people are inclined to choose an option that brings instant pleasure rather than the one which will beget long-term satisfaction at the expense of short-term gratification. Using behavioral economics, individuals and institutions can take advantage of this to manipulate individuals and groups into a specific course of action or purchase. Behavioral economics, which combines ideas from psychology and economics, provides valuable insights regarding the fact that individuals are not always behaving in their best interest. A knowledge mix from judgment and decision-making research is created in order to inform realistic assumptions about the thoughts, feelings and actions of individuals. Behavioral economics enriches the traditional field by utilizing theories from psychology, sociology, politics, and more to create a more realistic picture of the economy. Behavioral economics combines psychology and economic theory to examine why people sometimes make irrational decisions. It provides a lens through which we can understand anomalies in human behavior that traditional economic models cannot explain.

Financial decision is a crucial area where the critical decisions are considered as the most powerful. It isn't the decision of a single individual; indeed, decision-making is a process that may lead to the final point by considering the opinions of people linked to the relevant field. Financial decision making theories emerged from behavioral and traditional economics. Therefore, there are two schools of thought: traditional and behavioral finance theory.

2.1.1 Traditional financial theory

Traditional financial theory assumes that people make decisions by gathering all relevant data and possess the skills to process this information in a rational, unemotional way to arrive at an optimal choice. Traditional finance is more rational which focuses on mathematical calculations, economic models & checking the market behavior.

Traditional finance theory arose with the concept of Markowitz (1952) for portfolio selection that concepts are still used in investment Decisions. Traditional finance theory assumes that people possess and exercise the self-control to make financial decisions that are in their long-term best interests. Traditional finance theory support that financial knowledge and decision-making skills help people make informed financial decisions through problem-solving, critical thinking, and an understanding of key financial facts and concepts. Strong financial knowledge and decision-making skills help people weigh options and make informed choices for their financial situations, such as deciding how and when to save and spend, comparing costs before a big purchase, and planning for retirement or other long-term savings. It also acknowledges that accounting and financial concepts form the foundation of good business decision making, which enables managers to successfully achieve the goals of an organization. Under the traditional finance it's considered that financial decisions are made on rationality concepts that consider rational behavior of people. Rational analysis is focusing on the potential power for the decision-makers. It is a genuine and helpful tool to read more about the matters of decision-making in terms of the rational level. This may be affected by behavioral and other factors. Traditional finance theory is a normative plan to justify the situation for timely decision-making. It may desire for the possible level of decision making by involving the role of the person with the current decision-making features. It may demand the avail of the whole data available in the record regarding a specific issue. The rational decision and decision-making desires for the involvement of the highest possible decision-making details and data. This may strengthen the decision for the specific point in consideration (Challoumis, 2019).

2.1.2 Behavioral finance theory

Behavioral finance is the combination of psychological theory, cognitive and behavioral with finance and conventional economic that provides the conclusion about the irrational decision making of the people. Behavioral finance focuses on irrational decision of people. Cognitive behavior of investors is critical that suggests that human behavior cannot be ignored while making financial decision. Irrationality exists in behavioral finance due to factors of prospect theory which is decision-making depends on choosing among options that may themselves rest on biased judgments. Behavioral finance theory, which studies the psychological factors affecting financial behavior, challenges traditional assumptions. Behavioral financial decision-making is discussing the effect of decision making without the involvement of the mathematical and calculation tools. It is simply the use of human behavior in motivating the role of decisions of a financial sector of a firm (Zahera, 2018).

Behavioral finance theory does not agree that investors are perfectly well-informed and rational in making financial decisions. It also propagated that the reality shows that these assumptions are not valid and it is observed that investors exhibit irrational behaviors by acting with emotions even if they are well-informed. Statman (1999) stated that behavioral finance explain that how emotions and cognitive errors show their impact on the decision making process of the investor about the investment. Behavioral financial decision-making is discussing the effect of decision making without the involvement of the mathematical and calculation tools. It is simply the use of human behavior in motivating the role of decisions of a financial sector of a firm (Zahera, 2018).

This study is mainly base on the traditional finance theory.

2.2 The concept of Small and Medium Enterprise

Despite being relatively small and medium in size and made up of highly fragmented and heterogeneous industries, small and medium enterprises (SMEs) are characterized as the 'engines of growth' by economists (The Economist, 2010; OECD, 2010; Ng, 2016). SMEs account for significant contributions to GDP growth, new job creation, and poverty reduction.

SMEs are typically owned, operated and managed by proprietors in the form of sole or joint ownership. According to a study by Reuber and Fisher (2000) of SMEs in developing countries, most of firms under the broad category of SMEs are family owned and mainly providing the services by family members and hired external employees. Schmitz (2005) posits that given the low level of capitalization of SMEs most of them tend to operate in sectors utilizing extensive laborious techniques in contrast to largely established firms. Their primary activities according to Reuber and Fisher (2007) are mainly within the areas of primary sectors such as manufacturing, retail, service and trading.

There is no universally accepted definition of SMEs because in each economic system every country has its own classification according to their industrial regulation. The categorization of SMEs depends on qualitative judgment such as number of employees, size of enterprise, and amount of capital employed. In most developed countries, small and medium scale industries classified based on yearly gross revenue and the number of workers they employ. This indicates that the industrial regulation of different countries treat and categorize SMEs in different ways.

The 1985 U.K. Companies Act defined “small company” in respect of financial disclosure as companies employing 50 or less employees, turnover not greater than £2.8 million and balance sheet total not greater than £1.4 million. Japan classifies SMEs as manufacturing enterprises with total capital not exceeding 100 million yen with 300 employees. In South Africa, the three categories of business as defined by Small Enterprise Development Agency (SEDA) are micro enterprises, small enterprises, and medium enterprises, which are based on the number of employees considered regularly employed. Companies employing 51 – 200 categorized as medium sized enterprise, 21 – 50 categorized as small enterprise, and below 20 employees categorized as micro. According to the bylaw dated 04/ 11/ 2012 and published in the Official Gazette of Turkish Republic, the SME categorized in terms of employee number and annual revenue. Accordingly, the number of employees from 50 to 250 and annual turnover from 8 to 40 million Turkish lira (TL) categorized as small and medium sized enterprise.

The Accounting and Auditing Board of Ethiopia (AABE) classified Small and Medium Reporting Entities (SME) as per Directive No. AABE 804/2013 (EC) based on the size of resource or number of employees. A Reporting Entity which meets at least two of the criteria of annual revenue over Birr 20 million and less than Birr 300 million, total asset over Birr 20 million and less than Birr 200 million, total liability is over Birr 20 million and less than Birr 200 million, and number of employees is over 20 and less than 200 is categorized as small and medium business entity.

2.3 Empirical review of the study

Decision is a position, idea and judgment after investigation (Miller, 2009). It is a cognitive phenomenon and results from a complicated process of consultation, which include an assessment of potential and uncertainty results (Mooler et al., 2009).

Decision making in small and medium businesses in developed countries indicates that the decision maker is at the centre of the process, and provides an explanation of how strategic financial management decisions are made. However, lack of practical skills in financial management for decision making is vast amount barriers for growth of SME in developing countries. The main obstacles to growth and survival of SMEs are related to financial decision making (Olawale and Garwe, 2010:729; Fatoki, 2012:179).

The importance of financial decisions in small and medium business is apparent, since many of the factors that contribute to small and medium business failure can be managed by proper financial decisions. According to a number of studies, the main causes of business failure in small and medium business are the lack of financial management practice, low financial expertise and skill of business owner and mangers, lack of capital, unplanned growth, and low strategic and financial projection. All these causes related to financial decision making practice in small and medium business. According to Ibarra (2010), many of these causes of failure are challenges that can be successfully managed with financial strategies developed and implemented by the organization.

The significance of financial decisions is evident from the higher failure rate among small and medium firms because of their weak financial management (van Praag, 2003). Financial literacy of owners for the growth of firms seems really crucial (Adomako, Danso, & Damoah, 2015). Bad decisions threaten the firms sustainability and leaves the wide spread operational problems (Timmons & Spinelli, 2004).

Literature review of this study identifies the principal factors that lead to inefficiency in financial decisions making. An analysis of these inefficiencies reveals a need for a more in-depth examination of the problem. Broadly, three classes of factors identified through review of the literature which directly cause for inefficiency of financial decision making of SMEs operation in Ethiopia. These are business owner or/and manger capacity in financial management and financial decision making (financial literacy), financial management practice of SMEs, and non financial information consideration of the SMEs.

2.3.1 Business owner and manger capacity of financial management

Financial management knowledge is the capability to use relevant knowledge and understanding to make an efficient financial decision making. Eagly & Chaiken (1993) indicated that financial knowledge is a factor that has an impact on financial management decision making.

Owners of SMEs often do not have robust finance expertise and thus they may not completely comprehend the influence of their decisions on the firm. Many small and medium enterprise owners fail because they are unable to understand basic financial concepts or practices for financial decision making. Financial literacy has been identified as a vital knowledge resource for financial decision making, but insufficient attention has been given to how SMEs' financial literacy affects their financial decision making. Lack of adequate financial management skill of business owners and managers is one of the major reasons behind poor financial management practice of small and medium business enterprises (Jindrichovska, 2013). To make small and medium business enterprises more successful, a manager should acquire a wide range of management skills including more importantly financial management skill (Urban & Naidoo, 2012).

Limited finance and managerial expertise are challenges for the expansion of small and medium businesses (Bilal et al., 2017). Ropega (2011) and Griffin (2012) confirmed that most financial failures are caused by the business owner and managers of SMEs that are incompetent with lack of experience in financially managing the business and taking instant remedial action in a crisis.

Attitude (a state of mind, opinion, and judgment) has also a lot to do with a business owners' financial decision making and their financial situation. Parrotta and Johnson (2008) stated that financial attitude of business owner and manager can be considered as the psychological tendency expressed when evaluating recommended financial management decision with some degree of agreement or disagreement. Joo and Grable (2004) stated that business owner and manager with stronger perceptions and positive financial attitudes tend to more successful in financial management decision making.

2.3.2 Financial management practice of SMEs

Financial management practices are the practices of handling a business's finances in a way that allows it to be successful and compliant with applicable government laws and regulations; established financial policies, procedures and system; code of conduct of the firm; accepted accounting system (GAAP or IAS). Therefore, sound financial practice contributing for efficient and effective finical decisions making by way of generating the required financial information.

Financial management practice is a wide concept and encompasses activities related to financial record keeping of an entity, budgeting, reporting, cash flow management, capital planning, and working capital management among other financial management tasks (Turyahebwa, Sunday, & Sekajugo, 2013;Obazee, 2019).

A study by the International Finance Corporation (IFC, 2006) revealed that those involved with the management of SMEs are aware of the importance of accounting information and when it is available they use it for a variety of purposes.

However, lack of financial management practices are vast amount barriers for making effective and efficient financial decisions. SMEs, often owned and managed by the same person, have been found to be flexible in decision-making but lacking in internal expertise (Berry et a/, 2006). The informality of bookkeeping and the accounting information in SMMEs can complicate and prolong decision making (Perren and Grant, 2000).

Poor business performance has for long remained unexplained most especially in the developing countries perspective where the small and medium enterprises occupy the large part of the economy. Some studies from developed nations see (Nguyen, 2001) cite inefficient financial management practices to contribute immensely to SMEs poor business financial information.

One of the main features of small and medium businesses in Ethiopia is that they do not have useful financial information to make financial decisions. The information generated is utilized to pay taxes but this does not reflect the real situation of the business. Because small and medium business owners concentrate mainly on obtaining resources for operating expenses, it is neglected to develop financial planning and control, maintaining working capital management, implement management information system, and in place financial reporting system which are important for efficient and effective financial management decision. The fact that, most small and medium businesses in Ethiopia do not hired professional accountants; low cope up with technological knowhow; no working capital management and inventory control, weak financial planning and reporting which affect their financial decision making (Derese and Prabhakara, 2012). This implies that, in Ethiopia the issues of financial management practice in small and medium businesses are the contributing factors for inefficient financial decision making and hence the key areas that seek special attentions.

2.3.3 Non financial information consideration

Although financial criteria serve as the principal success indicators in business, there are often non-financial considerations to be taken into account in the process of financial decision making. McGee and Sawyer (2003:385), for instance, observe the role played by such personal ambitions on the part of small business owner managers as personal lifestyle, feedback, being own boss, independence and social status. Feedback, according to Frost (2003:49), serves as a tool to evaluate and control the outcomes of financial decisions. The on-going nature of the decision making process dictates constant monitoring, evaluation, choosing between alternative courses of action, and following up on choices made. In order for the decision maker to evaluate decisions made, there is a need to gather information, for which a formal information recording system is required. Generally, an evaluating system should provide feedback on how the decision is being implemented, what results are obtained, and what adjustments are necessary to enhance those results. This process is possible only with an information recording system in place in the business.

Non financial information consideration issues are related to find out if the business objectives as well as the feedback received from various stakeholders have been considered by the business owner and managers when making financial decisions. This section deals with the extent to which issues of the stake holders feedback and financial objectives of small and medium business are considered in the financial decision making process.

2.4 Literature gap

Reviewing of global literatures in regard to financial decision making of small and medium business enterprise, it is evident that most studies have focused on the analysis of the techniques used to make financial decisions rather than on the decisions themselves. This shows that finance research has not taken into account small and medium businesses' financial decisions. Likewise, researchers have not focused their attention on their study to aligning financial management technique and financial management decisions making to determine the effect of financial decision making on business performance.

In regard to Ethiopia context, although small and medium enterprises have significant role and potential in the progress of the country, still this sector overlooked and has not received sufficient attention from the researchers' side. Despite inefficient financial management decision making is a prevailing challenge in small and medium businesses found in Ethiopia, to own knowledge, there is a scarcity of Ethiopian literature in the field of small and medium business financial management decision making.

Therefore, this study is aimed at investigating the extent of financial management decision making employed by SMEs and narrowing the research gap existing in the literature through analyzing, summarizing, presenting and discussing the study.

Chapter Three - Research Methodology

3.1 Research Design

Research design is a general strategy for carrying out scientific research. It represents the basic structure of the study (Salkind, 2010). The design serves as a guide to the researcher in the research procedures, particularly in gathering, analyzing and interpreting the data. Salkind (2010) mentioned that research designs enable the researcher to answer research questions as to validity, objectivity, accurately and economically as possible.

The study was applied descriptive techniques to describe characteristics of financial management decision making practices in the sample SMEs. The researcher employed qualitative research approaches. The qualitative research approach is the most suitable to address the research problem identified in this study.

Since this is an empirical study, a structural approach for data collection and analysis were used to address the problem discussed in this research. In total, seven elements of research design were used in this research. These are research approach, research site and unit of analysis, sample size, sampling method, data collection method, pretesting, and data processing and analysis.

3.2 Research approach

Researchers are advised to identify research designs that are congruent with the intent of inquiry (Van Maanen, 2015). The types of qualitative research designs include the delphi technique, ethnography, grounded theory, narrative research, phenomenology, and case study (Marshall & Rossman, 2014). This study was used the qualitative case study approach after a careful assessment of the above mentioned options. The case study research design is preferred when insufficient knowledge on theories exists, and when a new theory might be developed through the outcome or result of the research being undertaken (Yilmaz, 2013; Yin, 2017). This research design is based on the premise of the purpose of the study and the types of data to be collected (Denzin & Lincoln, 2014; Halkier, 2013; Stake, 2013). The descriptive case study allows the researcher to explore and capture the participants' experiences and develop themes from emerging data.

3.3 Research site and unit of analysis

The area of the study included SMEs in nine sub cities of Addis Ababa Administration. The unit of analysis for this study is SMEs business. Thus, only one set of questionnaires were sent to each SME.

3.4 Sample size

According to Sekaran (2006), by studying the sample, the researcher should be able to draw conclusions that would be generalisable to the population of interest. Sekaran and Bougie (2010) suggested that sample size some-where between 30 to 500 would be useful for most of the research. In support, Roscoe (1975) stated the appropriate sample size should be higher than 30 and less than 500. This study is considering Hoe (2008) argument on minimum sample size and his recommendation to make that sample size minimum of 200 to provide enough statistical power for data analysis. Thus, this research was used 200 SMEs as an adequate sample size.

Accordingly sample of 200 small and medium businesses were taken from the total population of 2,021 registered with Addis Ababa Revenue Biro. Addis Ababa Revenue Biro indicated that it has 2,021 registered tax payers in small and medium size business as at Sene 30, 2012 (June 6, 2019) data base based on the threshold category determined by the Accounting and Auditing Board of Ethiopia.

3.5 Sampling method

This study adapted purposeful sampling approach to select research participants from SMEs who are provide data suitable for exploring how SMEs' owners or managers practicing financial decision making for their business growth profitability, and sustainability.

Purposeful sampling is based on intent and emphasizes choosing information-rich cases through a selective method (Rubin, 2015; Yin, 2013). Purposive sampling, also known as judgmental, selective, or subjective sampling, is a form of non-probability sampling in which researcher rely on his/her own judgment when choosing members of the population to participate in his/her survey. It allows the researcher to gather qualitative responses, which leads to better insights and more precise research results. It is also allow, the researcher to decide what needs to be known and sets out to find people who can and are willing to provide the information by virtue of knowledge or experience. It is typically used in qualitative research to identify and select the information-rich cases for the most proper utilization of available resources. Unlike random studies, which deliberately include a diverse cross section of ages, backgrounds and cultures, the idea behind purposive sampling is to concentrate on people with particular characteristics who are better be able to assist with the relevant research.

3.6 Data collection method and instrument

Data sources were either primary or secondary. Primary data were collected through closed form enumerator**s** administered structured questionnaires and where as secondary data were collected through document review.

3.6.1 Primary data collection

The study was employed a survey through which primary data were collected by means of a structured questionnaire. The questionnaires are enumerator administered with face to face interview to small business owner managers/hired manager in 10 sub cities in Addis Ababa administration. Face to face interviews aid an opportunity to obtain extensive insight into the persons acting as a participant; how they felt, what they think, what are the effects of certain events (Hazzan & Nutov, 2014). A collection of data in a qualitative method is often susceptible to subjectivity since as McCusker and Gunaydin (2015) indicated that a dominant and prevalent theme in qualitative research is the understanding derived from the linguistic meaning within the textual material. Serious consideration is attached to the selection criteria for research participants and data collection.

A combination of dichotomous and descriptive rating scale questions are used for the survey. These rating scales are enabled respondents to indicate their views on various aspects of financial management decision making in their businesses. The study purposely sampled the SMEs research participants to ensure diversity of gender and experience as representatives of SME business owners and managers. The questionnaires are divided into two sections: questions related to organizational formation and financial management decision making process. Four enumerators were recruited and trained on questionnaire.

The questionnaires were sent to 200 small and medium businesses. Out of that, 192 questionnaires were filled up and returned, which is representing a responses rate of 96%. Since most of the respondents did not have finance background the researcher had to explain most of the technical terms to help in obtaining the appropriate responses. To prevent a situation whereby some of the respondents tried to hide information, the researcher visited each to examine some of the documents requested for. Documents like profit and loss accounts, balance sheets, cash flow statements and business plans were examined. During the visits to the respondents, opportunity was taken to observe how things were done in SMEs office.

A pilot study was conducted on the survey instrument with 10 small and medium businesses in order to ensure face validity. The research assessed the clarity and ease of use of the research instruments and any biased items were identified and modified. Content validity of this study were determined by first critically reviewing the instrument to the extent to which the items on a test were fairly representative of the entire domain the test seeks to measure or not in relation to the research objectives.

Filled questionnaires were checked on daily base and correction was also made on inconsistent information for the purpose of data validation. Using data triangulation, a researcher crosschecked and validated data from the various data sources to achieve accurate and valid findings. Using multiple sources of data like the transcribe interviews, filed notes, and archived document and seeking convergence among them to form themes enhances the validity of the study (Yin, 2013).

3.6.2 Secondary data collection

The second instrument used for secondary data collection was documents review. Documents review provided support for the clarification of the research question and its significance both in practical and theoretical terms that detailed the methods used to answer the research question. Dworkin (2012) noted that the document review process is an adequate method for collecting data needed to provide answers to the research question and to demonstrate data triangulation. The document review served as a point of convergence and alignment of the researcher's goal, values, and ideas about the research and the strategy needed to propel and move the research process forward (Sue & Ritter, 2012). The documents that were reviewed provided practical proof needed to advance SMEs financial decision making practice. In conducting an examination of records, the searcher was search across a range of databases, such as papers, financial records and statements of sample SMEs, articles, and government websites.

3.7 Pretesting (validity and reliability)

Data were edited or checked for completeness, consistency and legibility for validity and reliability.

3.7.1 Validity test

Validity refers to the degree to which the measures of the instruments measure what it is supposed to measure (Joppe 2000; Mugenda, 2008. Content validity assesses whether a test is representative of all aspects of the construct. Content validity of this study were determined by first critically reviewing the instrument to the extent to which the items on a test were fairly representative of the entire domain the test seeks to measure or not in relation to the research objectives. Correlates of all the variables are significant with p-value less than 0.001.

Computed content validity index (p-value) for all variables were 0.001, therefore the measurement was in 99% confident level. All the variables are positively correlated. Therefore the measurement indicated the validity of the instrument was acceptable and statistically significant.

3.7.2 Reliability test

The study was check for reliability of the research instrument. Reliability of research instruments indicates the degree to which the research is without bias therefore ensured consistent measurement across time and the several items within instrument (Kothari, 2004). The study was used the Cronbach's alpha coefficient using the reliability command in SPSS to determine the internal consistency of the scale that was used to measure the reliability of the variables of the study. In this regard, a Cronbach's alpha of below 0.50 indicates inappropriate, 0.5 to 0.6 is considered satisfactory, 0.6 to 0.8 good, and greater than 0.8 is strong internal consistency (Cooper and Schindler 2008; Mugenda and Mugenda, 2003; Sekaran and Bougie, 2013).

The finding of the study for measurement of the reliability of the variables of the study is shown below:

	Cronbach's Alpha
Decision Maker Capacity	0.849
Financial Accounting and Recording	0.621
Financial Reporting	0.838
Cash Management	0.909
Account Receivable and payable management	0.617
Financial Planning	0.586
Financing and Investing activities	0.559
Financial Objectives and Strategies	0.680
Feedback System	0.807

The internal consistency of the scale that was used to measure the reliability of the variables of the study was in acceptable range. Four items (decision maker capacity, financial reporting, cash management, and feedback system) have strong internal consistency and three items (financial accounting, account receivable and payable management, and financial objectives and strategies) have good internal consistency.

Only two items (financial planning and financing and investing activities) have satisfactory internal consistency. These values indicating that the survey or questionnaire is reliable

3.8 Data analysis

After data collection, questionnaires were coded and entered into Statistical Package for Social Sciences (SPSS) version 20 for the analysis. Data were analyzed using content analysis as the data for the study are qualitative in their nature. The qualitative data analysis processes involved coding of the data, categorizing the coded data, and subsequent generation of themes in line with the research questions being addressed by the study (Godden, 2014). The data were also analyzed using descriptive techniques. Percentage and frequency counts were used to analyze the response obtained from the respondents. According to Cooper and Schindler (2008), descriptive analysis involves the process of transforming raw data into charts, tables with frequency distribution percentages to enable full interpretation of data.

A five-step data analysis procedure proposed by Yin (2015) was used for analysis of data for this research.

The first steps of the procedure were data familiarization. Once the data collection process for the studies is commenced, Yin (2015) suggests that the early analysis of the data is a critical step in the overall interpretation of the studies. The analyses began by building summaries of transcripts of structured questionnaires and secondary data. Due to the combination of different data sources, the researcher enhanced the credibility of the study. Starting from theoretical perspectives and with the research purpose in mind, the researcher were rereading filled questionnaires over and over again to enable him assimilating the information more thoughtfully to give him an opportunity to connect the data with the original research question. Finally, the researcher place the data into a consistent format, known as data record, which is used for further analysis, thus completing step one. During this analysis step, the researcher was constantly going back and forth from one type of research activity to another and between empirical observations and theory (Dubois & Gadde, 2002, p. 555). This enhanced the understanding of data and theory and leads to a good connection between the empirical findings and the theoretical view. Conducting this approach included a matching between theory and reality, a going back and forth between data and theory, which allows to strengthen the impact of the conclusion and findings (Yin, 2013).

After establishing familiarity with the data obtained in the field, the researcher was embarked on step two, data cleaning and coding. Data cleaning task was amended or removed incorrect or superfluous data as well as checking for incompleteness or inconsistencies. Following data cleaning the researcher started coding to the system.

In the third step, the researcher began contextual data analysis, comparison, look for hidden patterns and relationships, and find insight and predictions.

The fourth step was the interpretation, which is looking for a close alliance of the data with the research questions. In this phase, the researcher checked for attribute, completeness, fairness, empirical accuracy, and credibility of the analysis. In addition the researcher created visualizations by selecting the most appropriate charts and graphs.

After providing an extensive interpretation, the researcher put forward a focus and concise conclusion to wrap up the five-step data analysis process described in Yin (2015).

Chapter Four – Research Results and Discussion

The next part of the study presented the results and discussion of research question aimed at identifying key inhabiting factors that affect the financial decision-making process in SMEs. The results indicated that the important inhibiting factors are related to inefficient knowledge of owner or hired manger in financial management, inefficient financial information generated from financial management practices, and weak regulatory body support, monitoring, and enforcement mechanism.

The results of the survey are grouped into two sections. The first section analyses small and medium business organizational formation and the second section are devoted to the analysis of small and medium business financial management decision-making process.

4.1 Organizational formation

4.1.1 Legal form of SMEs

The legal forms ownerships of sample small and medium business are totally sole proprietorship or individual business (100%). The same is true for total population of the study. This is because the constitution of the country under Article 97 allows the local governments including Addis Ababa City Administration to form business as sole proprietorship only. The other legal forms such as private limited company, partnership, joint venture and others forms of business organizations allows to federal government. The constitution of the country prohibited to make a decision on the forms of business in which the investor to make a choice in local governments.

The legal form a firm chooses to operate is an important decision with implications for how a firm structures its assets. All SMEs under the study are sole proprietorship. Sole proprietorship is a firm that is owned by one person. From a legal perspective, the firm and its owner are considered one and the same. However this consideration is wrong from financial management perspective. In accounting, a business or an organization and its owners are treated as two separately identifiable parties. The main disadvantage of the restriction is oblige the investor to bear any lose arising from formation of business, which is the owner is personally responsible for the firm's losses and debts in the case of sole proprietorship. This presents a tremendous risk. If a sole proprietor is on the losing end of a significant lawsuit, for example, the owner could find his personal assets forfeited. The most important decision of business organization here in terms of financial decision making is the degree to which personal assets are at risk from liabilities arising from business formation.

4.1.2 Types of the industry

Based on secondary data provided by Addis Ababa Trade and Industry Biro and the category of SME as per Accounting and Audit board of Ethiopia, the total population of SMEs working in Addis Ababa city Administration as at sene 30, 2012 (June 6, 2019) categorized as 30% service, 63% trading, 6% manufacturing, and 1% others. This implies that, trading businesses constitute a sizeable number of small and medium business enterprises in Addis Ababa city Administration as compared to service and manufacturing sector.

Table 1 below reports the distribution of the sample of responded firms in terms of type of industry. 31% of businesses in the study sample are service, 47% are trading enterprises, 22% are manufacturing, while other industries which are insignificant and out of the research study.

Table: 1 Sample SMEs by industry

Industries	Frequencies	Percentage
Service	60	31
Trading	90	47
Manufacturing	42	22
Total	192	100

Sources: primary data

The process of selection of industry and making financial decision (investment decision) as a complex and dynamic process involves analysis of all factors such as access to finance, pursuing tax advantages; ability to attract potential partners, market opportunity, technology, location, and social issue. The business organizations need to analyze and evaluate the effects of all these factors to enable them to select the industry which give opportunities for SMEs financial performance. The government of Ethiopia recognized manufacturing enterprise as key SMEs and drivers of economic development and hence gives high priority compare to trading and service industry. Accordingly the government provides better opportunity to manufacturing sectors in terms of access to finance, market opportunity, land, and other basic services. Therefore SMEs should consider the industry where their businesses are making investment decision to get the advantage government incentives.

4.1.3 Organizational structure

Responses from sample business enterprises showed that 27(14%) of them did not have organization structure and these firms handled their financial tasks by external accountants on retention basis. On the other hand, 165 (86%) of respondents indicated that their businesses have organization structure. One hundred percent of these business enterprises have finance department with different number of employees.

Table 2 below shows the distribution the sample response in terms of number of employees in finance department.

Table: 2 – Number of sample SMEs finance department employees

Number of employees	**Frequencies**	**Percentage**
One	18	10
Two	33	20
Three	96	58
Four	9	6
More than four	9	6
Total	**165**	**100**

Sources: primary data

Those SMEs have number of employees with one person 11%, two persons a 20%, three persons 58%, four persons 6%, and more than four persons 5%. These indicate majority of the SMEs have finance department with more than three employees. Among these sample respondents, manufacturing firms have more than three finance employees in their operation.

Table 3 below shows the distribution the sample response in terms of number of employees in finance department by position.

Table: 3 – Sample Finance department employees by position

Position	**Frequencies**	**Percentage**

Finance Head	123	64
Accountants (both internal and external)	162	84
Cashier	102	53
Cashier Accountants	30	16
Cashier Secretary	39	20

Sources: primary data

Out of the total 192 respondents, 123 (64%) have finance head, 162(84%) have accountants (both internal and external), 102(53%) have cashiers, 30(16%) have cashier accountants, and 39(20%) have cashier secretaries. This shows that most SMEs have finance head, accountants, and cashier. Those who have a position of cashier accountants are theoretically highly exposed for risk of weak internal control system.

Firms operating without organization structure decisions, like the 14% of the sample respondents firms operating minimum of birr 20 million annual sales transaction, face with confusion within roles, a lack of co-ordination among functions, failure to share ideas, and slow decision-making which bring managers unnecessary complexity, stress, and conflict, subsequently exposed to fall of business. On the other hand 86% of the sample organizations have an organization structure. Respondents of sample SMEs indicated that organizations structure helps to simplify decision-making, give employees more clarity, help to manage expectations, enable better decision-making and provide consistency.

4.2 Financial decision making process

192 respondents were asked to answer the statement “what is/are the main inhabiting factors for your firm growth, profitability, and performance?” As table 4 indicated below, the responses indicated that massive respondents answered that the factors are weak decision making due to inefficient financial knowledge of SME managers/owners, inefficient financial planning, inadequate keeping of financial records, weak working capital management, inadequate accounting information, and low government support in terms of policy. Moderate numbers of the responses (18%) were lack of feasibility analysis before making investment decision and low government support in terms of policy making.

Table 4: Factors inhabiting firms’ financial decision making

Inhabiting factors	Frequency	Percentage
Inefficient financial knowledge of SME managers/owner	168	88
In efficient financial management practices(planning, record keeping, working capital management, accounting information)	171	89
Lack of feasibility analysis before making investment decision	126	67
Low government support in terms of policy	138	72

Source: primary data

This study identified and studied on three broad principal factors that are a cause for inefficiencies in financial decisions making process. The factors which are identified and studied were decision maker behavior and capacity, financial Management practice of SMEs, and Non financial information consideration.

4.2.1 Decision makers' information

4.2.1.1 Biographical information of the respondents

Table 5 below depicts the biographical information of the respondents. The typical respondents of this study who were mainly involved in the financial decisions in businesses were composed of owners 84%, hired managers 11%, and finance head 5%. The vast majority of respondent were therefore categorized as owner managers (84%). They were self-employed and working full time in businesses.

The respondents were also constituted of male (75%) and female (25%) with the large majority completed first degree and above (52%). Majority of the typical respondents were between the age group of 35-60 (59%) and 36% of the respondents completed the financial management training courses. The sample businesses under study were in operation for 10 to 20 years accounted for 57% which are massive number in terms of experience.

Table 5 – Biographic in formation of sample SMEs decision maker

Variables	Description	Frequency	Percentage
Gender	Male	144	75
	Female	48	25
	Total	**192**	**100**
	18 – 24	6	3
	25 – 34	66	35

Age group (in years)	35 – 60	114	59
	Above 60	6	3
	Total	**192**	**100**
Respondents' position in the company	Owner manager	161	84
	Hired manager	21	11
	Finance head	10	5
	Total	**192**	**100**
Qualification obtained	Elementary school	24	12
	High school	27	14
	Diploma /COC	42	22
	Degree and above	99	52
	Total	**192**	**100**
Years of experience in the business (in years)	Below five	6	3
	Five to ten	45	23
	Ten to fifteen	57	30
	Fifteen to twenty	51	27
	Above twenty	33	17
	Total	**192**	**100**
Financial management	Yes	69	36
	No	123	64

training course completed	**Total**	**192**	**100**

Sources: primary data

4.2.1.2 Decision maker financial literacy

The statistical data collected and analyzed helps to identify the principal factors that influence strategic financial management decisions in terms of the methods used. The methods used for the purpose of this study were broken down into four ways of different competencies. These are experience (learned competency), inherent (intuition) technique, acquired from financial management training, and expert advice (net working).

The study result indicated that financial decisions are fully the responsibility of owner managers or hired managers; this is suggesting that they applied directive decision-making style.

Table 6 below reported response of 192 respondents how they developed competency of the financial management decision making. The respondents were asked to answer the statement "How did you develop the competency of financial decision making "? The responses indicated that a massive 60% of respondents were relied on learned competencies to make strategic decisions. As might have been expected, those with 10 or more years of experience tended to rely on that experience (learned competencies) rather than other methods of developing competency.

The respondents were also asked to answer "yes" or "no" to the statement "Have you completed any financial management training course?" The 23% respondents indicated that their financial decision making competency gained from financial management training. By examining their answers, it is possible to infer financial management training is helpful in developing financial decision making competency. However SMEs owners or managers seem to lack knowledge and application of financial management practices, even though 36% of the respondents indicated that they attended financial management training.

The 17% of the respondents indicated that their decision making action were based on their internal or external expert support and Inherent (intuition) technique. The study show that to improve growth and competitiveness their business, most business owner manger who face more concerns but have less confidence in their capabilities seek information and advice from formal sources, including public and private providers governments and informal sources capable person from family, friends or internal employees.

Table 6: Respondents response how they developed competency in financial decision making

Method of competency acquired	**Frequency**	**Percentage**
Experience (learned)	115	60
Financial management training	44	23
Inherent (intuition) technique and Expert advice (net working)	33	17
Total	192	100

Sources: primary data

The respondents were also asked to indicate their impact on financial decision making using “yes” or “no” statement “Do you have a significant impact on financial decision-making?” Their respond indicated that they were fully involved (100%) on the financial decision making of their firm financial matters whether they were attended management training or not, they based on experience or used expert advice or intuition technique..

The study analyzed responses of respondents on the four functions of financial management, i.e. planning, organizing, leading and controlling. Table 7 below reported responses of 192 respondents' who impact on financial decision-making of their SMEs from the aspects of four functions of management. The analysis indicated that business owners and managers have a significant impact on financial decision on planning (18%), organizing (22%), leading (23%), controlling (29%) and all financial management functions (8%). The response of the respondents showed that their engagement in performing the whole four functions of financial management is insignificant despite they are responsible on all function. How well mangers perform these tasks determines how efficient and effective their organizations are. The analysis depicted the greatest impact lies on controlling function (29%). This indicates that much of the time of top management of SMEs allocated to controlling functions of the firm in contrary with theory (much of time of top management allocated to planning and organizing). Though the relative importance of planning, organizing, leading, and controlling (the four principal managerial tasks) to any particular manager depends on the manager's position in the managerial hierarchy, the amount of time that managers spend in planning and organizing resources to maintain improved organizational growth and success as they ascend the hierarchy. Top managers devote most of their time to planning and organizing, the task so crucial to determine an organization's long term performance. The lower the managers' positions are in the hierarchy, the more time spending in leading and controlling of first line managers or non managerial employees.

Table 7: Respondents impact on financial decision making on four financial management functions

Financial management Function	Frequency	Percentage
Planning	34	18
Organizing	42	22
Leading	45	23
Controlling	55	29
All managerial function	16	8
Total	192	100

Source: primary data

In explaining this section of the study, decision makers are at the starting point of the decision making process and the principal driver of the businesses. However the study indicated that there is an apparent lack of theoretical knowledge of owner or managers relating to the gathering and analyzing of information; practicing financial management methods, principles, and system; making choice from number of alternatives; risk and return analysis of investment projects; and considering innovation, growth, and future actions which are a perquisite for effective financial decisions. This position is suggested on their part to rely on intuition and experience alone.

The results of the study were also unexpected, given the high-level educational background of the owners. SMEs owners or managers seem to lack knowledge and application of financial management practices, even though 36% of the respondents indicated that they had attended financial management training. We can infer that perhaps the particular training they had undertaken was not effective, or that the SMEs owners or managers had not applied the knowledge gained from the training to their businesses. Secondary data analysis indicated that many higher educational institutions or training institutions in Ethiopia focus on financial management for academicians (focus on theories). There is no training arrangement in financial management for non finance persons or managers. Because of these, there is observed knowledge gap of financial management knowledge in most business organization including SMEs.

4.2.2 Financial Management Practice

The study reported that the main purpose of SMEs businesses was to prepare financial information mainly required by tax office and does not reflect the real situation of the organization of financial management decision making.

The study was focused on whether SMEs business managers understand financial management principles (techniques) and apply them to make financial. Therefore the study paying attention on five financial management practices that the researcher believed the most important in respect to financial decision making of SMEs business. These are accounting information and recording system, financial reporting, working capital management, and financing and investing activities.

4.2.2.1 Accounting information and recording system

The respondents were asked to answer the statement “Does your firm maintain books of accounts for its financial operation “? The response indicated that a massive 186 (97%) of respondents maintained books of account and 6 (3%) didn’t maintain books of accounts. The main reasons as the respondents indicated for not maintain books of accounts were high cost of maintaining books of accounts, maintained books of accounts are not the requirement of regulatory body, and their firms are presumptive tax payer and didn’t need to maintained books of account.

The respondents indicated reasons for decision of maintaining for books of accounts are indicated in table 8 below. As per the analysis of the responses the favoring factors for maintaining books of accounts were 23% due to availability of qualified expert in their firm, 26% of the respondents indicated that the need for bank and other sources of funds requirement, 11% due to regulatory body requirement, 23% tax office requirement, and 17% due to internal policy of the firms.

Table: 8 – Favoring factors to use books of Accounts

Fevering factors	**Frequency**	**Percentage**
Availability of qualified expert	44	23
Bank requirement to be eligible for loan	50	26
Regulatory body requirement	21	11
Tax office requirement	44	23
Internal policy of my firm	33	17
Total	192	100

Source: primary data

From sample study of 192 respondents, 120 (63%) respondents were indicated that their firms have written financial policy and procedure manual and 72 (37%) of the respondents didn’t have written financial policy and procedure manual for reasons indicted under table 9 below. The 37% of the sample which is representing the population didn’t have the general and specific guidelines as well as the list of ledger accounts which would be useful reference for effective management and reporting of financial operations of the firms. Existence of financial policies and procedures can help an organization for efficient financial decision in line with efficient financial management, risk mitigation, and the alignment of financial operations with the overall mission of the organization

Table 9 - Reasons for not to have written financial policy and procedure manual

Influencing factors	Frequency	Percentage
Not required by regulatory body	14	19
Not required by tax office	31	43
Not important for my firm	5	7
Cost of the manual is high	22	31
Total	72	100

Source: primary data

In examining the application of bases of accounting of 192 respondents of sample SMEs, table 10 below shows 3% did not have accounting information system, 8% used cash bases of accounting system, 43% used accrual bases of accounting, and 46% used modified basis of accounting. All SMEs engaged in manufacturing industry used accrual bases of accounting. If firms do not have accounting information system, they lack structure that their businesses uses to collect, store, manage, process, retrieve, and report their financial data so that they cannot be used by accountants, consultants, business analysts, managers, auditors, regulators, and tax agencies.

Table 10: Bases of accounting information system of sample SMEs

Information system	Frequency	Percentage
None	6	3
Cash basis of accounting	16	8
Accrual basis of accounting	82	43

Modified cash basis of accounting	88	46
Total	192	100

Sources: primary data

In investigating the application of accounting information system practice of SMEs, 97% of the sample SMEs used accounting computer software, which is dominantly Peachtree. The 3% did not maintain books of account and did not use any accounting system. The firms used the accounting software for recording of business transaction, preparing accounting special reports, production of financial statements, and controlling the budget.

Regarding the responsibility recording business transactions, table 11 reveals that 61% of SMEs in the sample used an employed or in-house accountant to record business transactions. 23% of respondents answered that they used external (or outside) accountants to record business transactions. 10% of the respondents firm used cashier accountant to record financial transaction. Whereas finance heads handled 6% of SMEs financial transaction record. Recording of transaction by finance head and cashier accountant are a sign of weak internal control system of the firms, which is conflicting the principle of segregation of duties and responsibilities.

Table 11: Responsibility – Recording business transaction

Responsibility	**Frequency**	**Percentage**
Finance Head	11	6
Employed Accountant(s)	114	61
External Accountant	42	23
Cashier Accountants	19	10
Total	186	100

Source: primary data

To conclude this section of the study, small and medium businesses did not have specialized personnel with expertise in financial administration and financial decision-making, and the owner or managers are making financial decisions without a solid foundation (analysis of number influencing factors, understanding them and evaluating their effects). The inability of small and medium firms to pay attractive salaries to experienced and capable employees made them very difficult to attract qualified accounting staff. Lack of well experienced and educated accounting staffs that were able to provide full time effort to the firms were one of the inhibiting factors for the practice of sound financial management system in SMEs. 23% of sample firms used external accountants with limited effort on retention basis and low reward. Ethiopian Revenue and Customs Authority (ERCA) is carrying out an assessment process to estimate the income earned and determine tax liability of small informal sector firms using presumptive tax system . The main goal of introducing the presumptive tax system are to simplify the rules for businesses and individuals small informal sector firms of that frequently escape taxation and to provide tax payers with equitable, efficient, quality services and bringing more firms to the tax net by promoting tax payers to voluntarily discharge their tax obligations. ERCA defined as ‘Category C’ taxpayers - those with an estimated annual turnover less than 500,000 birr are subject to a ‘turnover-based’ or ‘indicator-based’ presumptive assessment. Annual tax bills are then levied on the assessed income of Category C taxpayers. However, this study identified that 21 SMEs whose annual transaction of birr 20-300 million used presumptive tax system which is in contradictory with the regulation defined for category C tax payers. Out of 21 SMEs, 15 SMEs maintained books of account and produce financial statements. But they did not file the financial statements to reduce tax liability by using presumptive tax system. Based on secondary data analysis finding, tax payer whose tax liability with presumptive tax system reduced by two-third. This practice considered by tax payer as an opportunity to avoid tax liability using tax loophole. If SMEs have not maintained the accounting records which they should have maintained as per the law and regulation, SMEs would be liable for a penalty of 6% of taxable income, which is much lesser than lost tax liability. Analysis and reviewing of data (both primary and secondary) indicated that there are many problems in the internal control of small and medium enterprises, such as deficiency in understanding of internal control, inadequate segregation of duties, Inadequate documentation and implementation of internal control review policies, increased potential for fraudulent activities due to involvement of family members in business operations, weak risk identification ability, erroneous management decisions based on erroneous, inadequate or misleading information, low effectiveness and efficiency of operations, lack of reliability of financial reporting by users including financing instructions, and weak in compliance with applicable laws and regulations.

4.2.2.2 Financial Reporting

This study provided insight into financial reporting, analysis, and interpreting practices of SMEs in the sample presented in this section.

From total sample study of 192 respondents, 186(97%) sample SMEs maintained books of accounts and 6 SMEs did not maintain books of accounts. All SMEs maintained books of accounts prepared, analyzed, and interpreting financial information. As mentioned in table 12 below, financial report of sample SMEs that maintained books of accounts were prepared by finance head, employed accountants and external accountants were 30 (16%), 114(61%) , and 42(23%) respectively. The analysis of the study indicated that 84% of the report prepared by accountants (both employed and external). This is a good financial management practice. On the other hand majority of these financial reports were analyzed and interpreted by finance heads except for those SMEs that did not have position finance head. Table 12 present 66% of SMEs used the finance head in analyzing and interpreting the accounting information for decision-making. The remaining 44% analyzed and interpreted by accountants (internal and external). These practice are grey area (gaps in financial decision making) in terms of the same person recorded, prepared, analyzed and interpreted the accounting information.

Table 12: Responsibility for preparing and interpreting financial reports

Charge	**Responsibility**	**Frequency**	**Percentage**
Preparing accounting report	Finance Head	30	16
	Employed Accountants	114	61
	External Accountants	42	23
	Total	186	100
Analysis and interpreting the accounting information	Finance Head	123	66
	Employed Accountants	21	11
	External Accountants	42	23
	Total	186	100

Source: primary data

The analysis of the study indicated 186(100%) of sample SMEs that maintained books of account produced the two basic financial statements (balance sheet and income statement) to help owner/managers control financial position and performance of the business. Only 16% of sample SMEs prepared cash flow statements for following to be provided a detailed picture of what happened to a business's cash during a specified period.

The analysis also reported 82% and 18% of sample SMEs produce financial statements annually and semi annually respectively. 98% of the firm analyzed (ratio and trend) their financial statements annually or semiannually and the remaining 2% had never analyzed their financial statements.

The study further indicated that 186(100%) of those sample firms maintained books of accounts audited by independent auditors with 95% of them with qualified opinion and 5% with clean report. However only 171(92%) of them filed their financial statements to tax office. The rest of 15 SMEs which represent 8% did not filed to tax office to take the advantage of saving tax liability using presumptive tax system.

To wrap up this section of the study, the research finding indicated that the information's generated from financial management system are used for the purpose of taxation which does not reflect the real situation of the financial management system of SMEs. Most of respondents of sample population exhibited that the reason their firms for maintaining books of account were to meet the requirement of tax offices. The same is thru for existence of financial and procedure manual in their firms. This situation leads to infer that tax office requirements are the enforcement mechanism to practice the existing financial management in Ethiopia.

4.2.2.3 Working capital management

With reference to working capital management practices of SMEs, the study showed that, 52% response of the respondents indicated that their firms prepared a cash budget or a statement of planned inflows and outflows monthly or quarterly. The decision of firms to prepare cash budget were to assess whether the entities have sufficient cash to continue operating over the given time frame and to insight into their cash needs (and any surplus) and helps to determine an efficient allocation of cash.

The 48% of the response of decision makers reported that their firm did not prepare cash budget for main reasons of lack of experienced and capable employee, feeling that it is not important for the firm, not required by tax office, and not required by regulatory body.

The study result also revealed that 13% of the respondents did not keep their money in a bank on a daily basis. As the respondents indicated, the main reason for not deposited to bank on daily bases were used cash collection for daily business transaction, invested in to other business opportunity, used for traditional saving mechanism, or/and used for personal use. This reveals that theories of cash management have not been popularly implemented in SMEs.

In regard to determining available target cash balance, almost all respondents indicated that their firm did not determine and give attention to target cash balance. The owner/manger's used their prior experience in determining the target cash balance. Occurrence of any cash shortage filled with short term loan from relatives and business collogues. Regarding cash surplus investment, 85% of sample respondent firms deposited surplus cash in to bank and 15% respondents indicated that surplus cash deposited to other non business profitable purpose. This can be explained, because the money market in Ethiopia has not developed, therefore, firms could not use temporarily cash surplus to purchase short-term investment instruments for profit purposes.

4.2.2.4 Receivables and payables management

In reviewing receivable management practices, respondents were asked questions concerned with credit sales and policies. Based on analysis of response of sample SMEs respondents of 192 decision makers, 126 (66%) sold their products or services on credit and 66(34%) had never credit sales. All sample respondents of SMEs indicated that never had credit policies but majority of them tended to sell on credit to anyone who wishes to buy. Respondents mentioned that their firms were interested to sell on credit on the basis of available cash position in the firm and level of solvency and credit worthiness of the customer. On the other side those sample firms respondents that were reluctant to sell goods and services on credit indicated that their firms are not interested due to fear of shortage of cash due to delay of collection, fear of risk of default of collection and none security of credit sales, and weak or in insufficient law enforcement of the country.

When analyzing the percentage of bad debts to sales, 97% of responding firms indicated that their bad debts have not exceeded 5% of sales (Table 13). However, a few SMEs answered that they did not know their percentage of bad debts to sales.

Table 13: Analysis of bad debts to sales

Bad debts to sales	Frequency	Percentage
Less than 5%	186	97
5 -10% of sales	3	2
10 -20% of sales	1	0

Don't know	2	1
Total	192	100

Source: Primary data

The analysis of payables management practice, respondents were asked to answer question related to purchase of product or services on account, accordingly 145(76%) of sample response indicated that their firms did not purchase products and services on credit. The respondents indicated that they were reluctant to purchase on credit for reasons of taking advantage of discount facilities by paying creditors promptly, habit of inclined towards purchasing on cash or paying promptly when they purchase on credit, and suppliers are not interested to sale on credit without guarantee.

The remaining 47(24%) of the response of respondents pointed out that firms were experienced purchase of products and services on credit. As the respondents indicated, the decision to purchase on credit was to get the advantage of cash flow, strengthen business relationship with suppliers, establish credit history, and securing source of interest free short term financing for their firms.

To conclude this section of the study, the results of the research confirmed that business firms were not interested to sell their goods and services on credit partly with the issue of weak law enforcement of the country. The study indicated that 8% of sample firms indicated that inefficient or weak law enforcement of the country influencing the payment discipline of debtors due to inadequate legal system, little legal enforceability, and slowly court action and over all legal environment.

4.2.2.5 Financial Planning

To investigate financial planning practices, respondents were asked questions related to preparing of financial budgets, kinds of financial budgets prepared and comparing budgeted and actual results. The analysis of sample response of the respondents 150(78%) decision makers indicated that their firm prepare financial budget and 42(22%) of the response reported that their firm did not prepare financial budget. The main reasons the respondents mentioned why their firms didn't practice financial budget were lack of expertise, feeling of not important for the firm, perception of not required by the regulatory body, and not required by tax office.

Table 14 below reports of kind of financial budget prepared by sample of 150 SMEs. 147 (98%) had prepared sales budgets, 144(96%) had prepared purchase, labor, and overhead budget, 150 (100%) had prepared selling and administrative budget, and none of sample firms prepared balance sheets and Income statement budget.

Table 14: Financial budget of SMEs

Kind of financial budget	Frequency	Percentage
Sales budget	147	98
Purchase, labor, and overhead budget	144	96
Selling and Administrative budget	150	100
Income statement and balance sheet budget	0	0

Source: primary data

In addition to preparing financial budgets, 180(94%) of SMEs in the sample firm did not compared between budget and actual results, only 12(6%) conducted the comparison. As indicted by the respondents, the main reasons for not compared budget and actual results were the perception of not important for the firm and hence no systems were in place, lack of capable staffs internally, not requirement of the regulatory body, and not requirement of tax office. Those sample SMEs respondents who had practices the comparison indicated that the comparison benefited them in terms of understand and improve the way money spend and managed, improve the allocation of scarce resources in future budget, and enable them to take remedial action to be taken as variance emerge.

Furthermore, respondents of sample SMEs indicated that they carried out the comparisons of budget with actual results in quarterly and semi annually periods of time.

Therefore, the finding showed that majority of small and medium businesses do not compare their budget with performance. They don't have a system in placed to practice. Some of the respondents of sample firms don't know the importance as it is not the requirement of tax office. The SMEs mangers forgone the benefit in terms of understand and improve the way money spend and managed, improve the allocation of scarce resources in future budget, and enable them to monitor and take remedial action to be taken as variance emerge.

To conclude this section of the study, the most influential roles of business owners and managers in the process of financial decision-making were the controlling function of management. The analysis depicted that the greatest impact lies on controlling function (29%). This indicates that much of the time of top management of SMEs allocated to controlling functions of the firm in contrary with theory (much of time of top management allocated to planning and organizing).

4.2.2.6 Financing, investing, and withdrawals decisions

In this section the three financial management decisions considered for analysis of responses of SMEs respondents are investment decisions, financing decisions, and withdrawals decisions which are mainly encountered in SMEs financial operation.

Respondents of sample SMEs of 192 decision makers were asked to answer "yes" or "no" to the statement "Does your business evaluate the visibility of the business before establishment?" Accordingly, from these respondents of 192 sample firms, 189(98%) were evaluated the visibility of the projects by external consultants and the remaining 2(2%) did not evaluate. Among sample SMEs did the evaluation of the feasibility of the project 180 (95%) use the payback period methods; while, the remaining 9(5%) used post payback profitability. This implies that, payback period is more convenient and dominant method in SMEs as compared to other methods such as, accounting rate of return, net present value, and discounted cash flows.

Related to sources of financing, table 15 below reported that 64% of respondents financed their capital investment projects from owner sources, 31% from bank loan, and 5% from individual and families.

Table 15: Sources of finance

Source	Frequency	Percentage
Owner investments	123	64
Bank loan	60	31
Loan from individuals and families	9	5

Total	192	100

Source: primary data

Table 16 below presented factors that influencing the financing decision (bank financing) of owners of SMEs. 51% of the respondents indicated that high collateral requirement of the bank influenced their business to borrow from the bank. Similarly, 20% of the respondents indicated that their firm reluctant to financing from bank due to higher interest rates, 19% of the respondents indicated that their firm fear of business fail and confiscation of the collateral by the bank, and the remaining response of the respondents faced challenges of low credibility of the firm by the bank for not fulfillment of the requirements. This indicates that, the most pressing problems that facing with small businesses are the fact that higher collaterals are imposed by banks.

Table 16: Factors affecting bank loan

Factors	Frequency	Percentage
High collateral	99	51
High interest rate	38	20
Fear of business fail and confiscation of the collateral by the bank	36	19
Low credibility of the firm by the bank for not fulfillment of the requirements	19	10
Total	192	100

Source: primary data

The respondents were asked to answer the statement “What is/are withdrawals decision(s) in your firm “? 71(37%) of the respondents indicated that their withdrawals decision of money from the firm were based on availability of cash, 60(31%) based on organization plan, 44(23%) of respondents basis on internal policy, 15(8%) of respondents bases on personal need, and 2(1%) of the respondents bases on business profitability. The withdrawal decision of money without the support of internal policy of the business is violation of business entity concept. In accounting, a business or an organization and its owners are treated as two separately identifiable parties. A business holds separate entity and distinct from its owners.

Related to costing decisions, 94(49%) of respondents based their information search on competitors' prices. These findings are in agreement with results presented by Pineda et al. (1998:2), who argued that most small business owner managers used external sources of information (such as competitors' prices) to make costing decisions in their businesses. They observed that most small business owner managers collected information about competitors indirectly from a number of sources, including customers, suppliers and newspapers. 71 (37%) of the respondents indicated that their firm base their pricing decision based on demand and supply position of goods and service in the market. This practice is dominantly practiced in Ethiopia business context. 27(14%) of respondents firms follow internal analysis of to determine the price of goods and services.

The respondents were also asked to answer the statement "What is/are the foundation(s) of your financial decision in the firm? 73% of the respondents of sample firms indicated that their bases of their decision were profit maximization, market orientation, daily operation, and increasing market share. These respondents mainly focus on short term earnings and characteristics of ordinary business whose objectives are short term gain and profit maximization. Whereas the 27% of respondents indicated that their bases are considering risk and return of the firms, innovation, growth, and future actions (long term investment). Empirical study shows such types of responses are characteristics' of entrepreneur managers that their objectives are wealth maximization and business growth.

To summarize this section of the study, the finding showed that SMEs financial decision making in cash management practice is weak. 48% of the response reported that their firm did not prepare cash budget for main reasons of lack of experienced and capable employee, feeling that it is not important for the firm, and not required by tax office and regulatory body. The study indicated that SMEs missed the primary tool for cash flow management that helps them to estimate their business' short-term cash requirements, mainly to determine plan for surplus or cash shortage. In addition, the study result revealed that 13% of the respondents did not keep their money in a bank on a daily basis. In regard to determining available cash balance, almost all respondents indicated that their firm did not determine and give attention to target cash balance. The owner/manger's used their prior experience or intuition in determining the target cash balance. All these reveal that theories of cash management have not been commonly implemented in SMEs. Anny occurrence of cash shortage filled with short term loan from relatives and business collogues. Cash surplus either used for personal affairs or used for other non SMEs' business related profitable activities. This is mainly because the money market in Ethiopia has not developed, therefore, firms could not use temporarily cash surplus to purchase short-term investment instruments for profitable business purposes. Under capital structure decisions, the result shown that the majority (64%) of small and medium businesses use owner financing as a major source to finance their investments;

whereas, 36% of them have used other alternatives from external sources such as loan from banks and relatives. The highest preference to owner managers were to use internal financing which includes retained profits before resorting to any form of external funds. This was because internal funds incur no flotation costs and require no additional disclosure of proprietary financial information that could lead to more severe external financing discipline and a possible loss of competitive advantage. When firms were forced to use external financing sources, owner or managers selected the least risky and demanding source first. The study pointed out that, around 51% of sample small and medium businesses had challenges of financing from bank due to the fact that higher collateral, 20% faced challenges with high interest rate, 19% were fear of business fail and confiscation of the collateral by the bank, and 10% were low credibility of the firm by the bank for not fulfillment of the requirements. High collateral requirement by lending institutions and high interest rates charge were obstacles that some of SMEs could not access to external sources mainly from banks. On the other side, the formal financial institutions in Ethiopia structure their products to serve the needs of large businesses. This argument is similar to the previous studies by Fetene, (2010) that found 46% of the small firms in Ethiopia facing with financing problems because of insufficient collateral requirements.

4.2.3 Non financial information consideration

Non financial issues in line with this study are issues that have been considered by the owner managers when making financial decisions. This section deals with the extent to which SMEs mangers deal with business goal and objectives as well as the feedback received from various stakeholders when making financial decision making.

4.2.3.1 Business goal and objectives

With reference to the goal of the firms, table 17 reported that most of the respondents 140 (73%) decision makers revealed that goal of their firms were profit maximization and increase market share. 35 (18%) of the respondents indicated that their firm objective were wealth maximization and business growth, and 17(9%) of the respondent indicted that their business goal are increase firm value, customer satisfactions, employment opportunity, and solve community & environment problem.

Table 17: Goal of the firm

Business objectives	Frequency	Percentage
Profit maximization and increase market share	140	73
Wealth maximization and business growth	35	18
Increase firm value, customer satisfactions, employment opportunity, and solve community & environment problem	17	9
Total	192	100

Source: primary data

The respondents were asked to answer the statement "Does your firm develop short term objectives"? 189(98%) of respondents indicated that their firms have short term objectives. 3(2%) of the respondents answered that they don't know what is short term objectives and did not have any. Table 18 reported the short term objectives of those sample firms of 189 respondents. Most sample SMEs short term objectives were increase sales for more profit and cash making, optimize product/service price for more profit and margin, and decrease expenses and cost of product/service for more profit and margin.

The most important but less attention were given to liquidity and comparative advantage analysis of short objectives. Despite 49% setting price based on competitors prices, the study prevailed that less attention were given to liquidity and comparative advantage analysis.

Table 18: Selected short term objectives of sample SMEs

Short term objectives	**Frequency**	**Percentage**
Increase sales for more profit and cash making	189	100
Optimize product/service price for more profit and margin	180	95
Decrease expenses and cost of product/service for more profit and margin.	171	90
Increase liquidity and solvency(maintaining adequate level of working capital)	128	68
Create comparative advantage analysis in terms of pricing and quality of service/product delivery.	106	56

Sources: primary data

Regarding long term of objectives of the sample SMEs, 189(98%) of the respondents (similar respondents of short term objectives above) developed long term objectives and similar to short term objectives 3(2%) of respondents did not know what is long term objectives. Table 19 reported the long term objectives of those sample firms of 189 respondents' below. Massive respondents firm focused on wealth maximization and growth of firm and efficiency of the business. Despite high challenge of access to finance, the response rate regard to increase credit worthiness were less compare to the two objectives.

Table 19: Selected long term objectives of sample SMEs

Long term objectives	Frequency	Percentage
Wealth maximization (increase firm value) and growth (increase market share)	189	100
Efficiency - maximizing return while minimizing inputs	144	76
Increase credit worthiness - Increase access to finance from bank and other financial institution.	57	30

Sources: primary data

To make summarize the discussion of this section, the study attempted to distinguish small and medium business owner managers or managers in two business characteristics - entrepreneurs and ordinary business owner managers or hired mangers from theoretical point of view. Based on analysis of both primary and secondary data, the study identified that majority of sample business (73%) categorized under ordinary business. The 27% of sample business are categorized as entrepreneurs and majority of them are from manufacturing business. Ordinary business managers are generally characterized as those who have planning and market orientation as principal characteristics and are not engaged in any innovative and risk taking actions. They do not provide for the future and focus on the daily decisions, mostly involving survival activities. Whereas, entrepreneurs are characterized by an orientation to risk and innovation and have profitability and growth set as principal objectives. Entrepreneur managers go beyond survival, profit and sales targets, and involved in customer satisfactions, creation of employment opportunities and solve problems that occur in business community. Therefore, the finding of the study showed most owner or managers under the study are not entrepreneurs and experienced in difficulties with sound strategic financial management decisions making. The study indicated that SMEs under the study categorized them based on their goal is either as profit maximization or wealth maximization. The study investigated that 73% of small and medium businesses were pursuing that profit maximization and increasing market share are the main reason for their existence as compared to those wealth maximization (27%). The most commonly observed aims of majority of sample SMEs are making a profit (short term earnings). Accordingly, these business firms positioned their prices and cost structure to achieve the highest possible profit. The study showed that these SMEs are from service and trade industry. The study finding as well indicated that massive number of the respondents from manufacturing industry indicated that their firms' objectives are wealth maximization. Five respondents from manufacturing firms in the sample population indicated that their business goal are increase firm value, customer satisfactions, employment opportunity, and solve community & environment problem. The study showed that 29% sample respondents have organizational structure with three and more key business functions departments including finance, human resources, marketing, and research and development. All respondents of sample SMEs of manufacturing departments included here. This shows manufacturing industry involve in additional investments in intellectual property and strategic positioning, as well as attention to managing the risk profile of a business.

4.2.3.2 Feedback system of the firms

Table 19 reported the incorporation of stakeholder feed back in decision making. Feedback may be gathered from recorded information in the monitoring and evaluation processes. Table 20 indicated sources of financial information from stakeholders and indicated that 34% of financial information obtained from customers, suppliers, financer, and creditors, 29% from tax office, 20% from external auditors, and 17% from wider communities.

Table 20: Sources of feed back

Stakeholders	Frequency	Percentage
Customers, suppliers, financer, and creditors	65	34
Tax offices	56	29
External auditor	38	20
Wider community and staffs	33	17
Total	192	100

Source: Primary data

Chapter Five – Conclusion and Recommendation

5.1 Conclusion

The business environment continuously influences the activities in firms and the decisions of their managers. It is essential that to ensure the stability, competitiveness and long-term sustainability of the firms, managers should make effective decisions, especially in the field of finance. The goal of the study was to propose a concept, the essence of which is to determine the key systematically-occurring errors in the financial decision-making process of managers rising from the effects of the human factors as a basis for the prevention of incorrect finance decisions which could have a negative impact on the financial health, profitability, growth and sustainability and competitiveness of SMEs.

This study describes the factors inhibiting efficient and effective financial management decisions in small and medium businesses at Addis Ababa city administration. The results indicated that the important inhibiting factors are related to owner/hired managers themselves. There were an apparent lack of theoretical knowledge relating to the gathering, analyzing, recording, summarizing, and reporting of accounting information requisite for effective financial decisions and a tendency is suggested on their part to rely on intuition and experience.

The findings revealed that, the fact that owners of small businesses have no adequate financial management skills and some (36%) had been exposed to some financial management training but lacked the expertise or willingness to apply it to their business. 64% did not exposed to financial management training and need further working out. Most small businesses engaged in financial management functions (planning, organizing, controlling, and leading) and the analysis showed that the greatest impact lies on controlling function. This indicates that much of the time of top management of SMEs allocated to controlling functions of the firm in contrary with empirical evidence (much of time of top management allocated to planning and organizing). Though majority of small and medium businesses have plan most of them unable to compare their financial plan with their financial performances. This indicated that SMEs mangers forgone the benefit in terms of understand and improve the way money spend and managed, improve the allocation of scarce resources in future budget, and enable them to monitor and take remedial action to be taken as variance emerge.

The result under accounting records and financial statement preparation indicated that, a significant majority of small and medium businesses maintained books accounts and financial statements and hence managers could able to easily determine their financial successes and failures periodically, get access to timely and adequate financial information for financial decision makings. 97% of MSEs have systems of accounting information organized formally. Employed accountants 61%) played an important role in carried out most accounting responsibilities whereas external accountants (23%) have been somewhat engaged in finance operation. Most SMEs have applied computers in their accounting information systems and the dominantly used application software

(Peachtree) was used for recording and preparing accounting reports. Out of those maintained books of accounts, 100% of them have prepared balance sheets and income (profit and loss), and 16% of them prepared cash flow statements annually or semi annually. Most SMEs (98%) prepared and analyzed their financial statements (both trend and ratio analyses) on semiannually or annually. Nevertheless, about 2% of MSEs have never analyzed financial statements.

The results under working capital management, small and medium businesses appears poor at managing their working capital as a result of lack of awareness and enough knowledge in working capital management's areas. Close to half of sample respondents indicated that they firm did not prepare cash budget, some of the firms did not deposit their collection on a daily bases, firm did not determine and give attention to target cash balance, and almost all firms never had credit policies.

The study indicated that owners have entered in to business field with prior assessment of the validity of their investment before starting up the business dominantly (95%) using payback period. So they had experience of deciding whether or not the investment project should be accepted or rejected. The dominance of the payback period method over other methods can be attributed to its simplicity. In fact, other methods(net present value and accounting rate of return) could be difficult for small and medium businesses because, many of them have limited knowledge in financial management and accounting; as a result, these firms may not be able to make use of reliable estimates of future cash flows.

The results under capital structure decision revealed that, small businesses use owner investment as a major source of financing for their investment and looking for additional alternatives if they need additional fund. To access funding from external sources especially from bank , small and medium businesses felt with challenges mainly because of high collateral requirement by lending institutions and high interest rates charges for which some of the small businesses un able to pay. The majority of the small and medium firms have make use of competition based pricing strategies to price their products due it simplicity and convenience as compared to other pricing strategy namely, target rate of return, cost plus based, and demand and supply position of goods and service in the market. In theory, various objectives are possible in business environments; however, for most small and medium businesses in sample studied firms, the main reason conducting the business is profit motive, not wealth maximization

The problem with financial management decision making in SMEs is significant, but surprisingly largely ignored in current strategic literature. Much of the literature has tended to focus on describing how small businesses function. Limited attention has been given to this special problem, compounded by a scarcity of empirical data on how these small and medium businesses arrive at decisions. So the study contributes to the academic field and small and medium business management through a suggestion as to the reasons for unsound decisions in SMEs.

5.2 Recommendation

Based on the descriptive findings of financial management decision making of SMEs in the survey, this study recommends the following input to be considered by all concerned stakeholders and government policymakers:

1. Financial literacy is vital as one of the critical management competencies that contribute to SMEs financial performance, draw out firm profitability, success and growth. A possible solution to descriptive finding of the study in line with financial

literacy of managers' problem lies in mentorship, law enforcement, coaching, and possibly a provision of financial literacy education to small and medium business owner or hired managers.

2. Training institutions offering entrepreneurship or business-related modules should place more emphasis on financial management topics for non finance persons (managers) specifically targeted at SMEs level.
3. Owner/managers of small firms should avail themselves with the various training programmes organized by business and financial training institutions in the country or abroad to polish their knowledge in financial management and other management topics.
4. The regulatory body for financial administration in Ethiopia is not known its presence by most SMEs. It is not also active and weak in enforcement in regulating the financial laws and regulation of the country, the accounting system, ethical behavior, and other enforcement mechanism. As it has an impact on financial administration of the country, the government of Ethiopia should consider the issues of why financial law, regulation, system and standard are not laid down on the ground and do not practice by business organization including SMEs.
5. For future research, it would be useful to extend the number of SMEs involved in this study and broadening the scope of the study, to obtain a sample more representative of the population of small and medium business in Ethiopia.
6. The researcher suggest that future studies should include more cases and other factors closely associated with financial management decision making, including information search and analysis, risk and option consideration, financial management attitude of

owners, use of information technology, legal form of organization, pattern of ownership, liquidity position, asset structure, state of economy, government regulation, tax policy and size and age of enterprise. This would then enable results to be generalized, to provide a better and more detailed picture of which practices are followed by SMEs.

7. Internal controls are the processes, regulations, and procedures that a firm puts in place to assure the accuracy of financial and accounting data, encourage accountability, and prevent fraud. Poor internal controls result in increased bureaucracy, reduced productivity, increased complexity, and increased time to process transactions, and increased non-value activities. By performing risk assessment and setting up internal controls can help SMEs business become more efficient. Lack of employee knowledge and training is also one of the leading causes of internal control failure. Due to insufficient knowledge management theory, most of SMEs owner managers or hired managers cannot identify potential risks inherent in business by standing in the overall and strategic perspective. By training employees, and involving them in the process, can help the firm in identifying and rectifying control weaknesses. So SMEs need to strengthen the moral training and the education of internal control system of all staff, establish an effective internal control system and strengthen supervision. SME's should also conduct internal control reviews through an independent audit firm to monitor implementation and proper functioning. In addition, SMEs require that different individuals be assigned responsibility for different elements of related activities, particularly those involving authorization, custody, or record keeping.

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Annex – Structured Questionnaires

This questionnaire is prepared to obtain information from key informants. The information is required for the academic research entitled “financial management decision making challenges - the case of small and medium Enterprises (SMEs) - in Addis Ababa city, Ethiopia” is being conducted for Partial fulfillment of the requirement for Master of Business Leadership. The main objective of the research is to investigate and describe the main inhibiting factors that detract from effective and efficient financial management decision making in Small and Medium Size Enterprise (SMEs) and make recommendations based on the findings. The questionnaire consists of two sections. Section A includes general information. Section B contains specific information to financial decision making. Your response, in this regard, is highly valuable and contributory to the outcome of the research. All information will be kept strictly confidential, and utilized for this academic research only.

A. General Information

1. What is the forms of your business
    a. Sole proprietorship
    b. Private limited company
    c. Partnership
    d. Joint venture
2. What is the type of the Industry your firm is classified?
    a. Service
    b. Trading
    c. Manufacturing
    d. Other

3. Does your firm use cash register machine?
    a. Yes
    b. No
4. Is your firm a VAT registered?
    a. Yes
    b. No
5. What is/are the main in habiting factors for your firm growth, profitability, and performance?
    a. Weak financial management decision making due to inefficient financial knowledge of SME owner/manager
    b. In efficient financial practices (inefficient financial planning, inadequate keeping of financial records, weak working capital management, and inadequate accounting information).
    c. Shortage of finance and no access to finance.
    d. Lack of feasibility analysis before making investment decision.
    e. Low government support in terms of policy
6. Does your firm have organizational structure?
    a. Yes
    b. No
7. If the response for the above question is no, who handle the finance task?
    a. One of family member
    b. External accountant on retention basis
    c. Owner/hired manager
    d. Office attendant
    e. Non as my company is practicing presumptive tax system
8. If the response for the above question is yes, how many department(s) exists?
    a. One
    b. Two
    c. Three
    d. More than three
9. Based on the above question, what is/are the department(s)?
    a. Finance department
    b. Human resource department
    c. Finance and administration and finance department
    d. Marketing department
    e. Research and Development department
10. If there is a finance department, how many employees exist?
    a. One
    b. Two
    c. Three

    d. Four
    e. Above four

11. Based on the above question, what is (are) the position(s)?
    a. Finance head
    b. Accountant(s)
    c. Cashier(s)
    d. Cashier accountant
    e. Cashier Secretary
12. What is/are the sources of information(s) your firm using in financial decision making process?
    a. Financial statements (balance sheet, income statement, cash flow statement)
    b. Financing information
    c. Government investment and economic policy
    d. Tax implication on making investment
    e. Customer, supplier, and creditors' information

B. Specific to financial decision making Information

1. Decision maker capacity

1. Gender
    a. Male
    b. Female
2. Age group (years)
    a. Below 18
    b. 18 – 24
    c. 25 – 34
    d. 35 – 60
    e. Above 60
3. Role in the firm
    a. Owner manager
    b. Hired manager
    c. Finance Head
    d. Owner manager and finance Head
    e. Hired manager and finance head
4. Qualification obtained
    a. None
    b. Up to elementary school
    c. High school
    d. Certificate of Competency (COC)/Diploma
    e. First degree and above

5. Years of experience in the business
    a. Below five years
    b. Five to ten years
    c. Ten to fifteen years
    d. Fifteen to twenty years
    e. Above twenty years
6. Did you complete the financial management training course?
    a. Yes
    b. No
7. If you attended financial management training course and understand financial management principles (techniques), do you use them to make financial decisions?
    a. Yes
    b. No
8. If your answer for above question is no, why you don't have the interest to apply them?
    a. Not important for the firm
    b. No enforcement mechanism by the regulatory body to maintain books of account
    c. Not enforcement mechanism by tax office to maintain books of accounts
    d. Tax liability with presumptive tax system is much lower than that of maintaining books of accounts.
    e. Avoiding cost of maintaining books of accounts including accountant cost
9. If you involve in financial decision making, how did you develop the competency?
    a. I don't know
    b. Experience (learned competency)
    c. Inherent techniques (intuition and long term thinking)
    d. Acquired from financial management training
    e. Expert advice
10. Do you have a significant impact on financial decision-making in your firm?
    a. Yes
    b. No
11. If your response yes, which area of financial management function you are engaged in?
    a. I don't know
    b. Planning
    c. Organizing
    d. Controlling

e. Monitoring

12. If you are involved in financial decision making process of your firm, what is/are your reference(s) of compliance requirements to do so?
    a. Doing the decision inconformity with applicable laws
    b. Doing the decision in spirit of accountability to all stakeholders
    c. Doing the decision on the bases of vision, objectives and values of the firm
    d. Doing the decision in line with established internal financial policies, procedures, and system
    e. Doing the decision morally and ethically

2. Financial Management practices

2.1. Financial accounting information and recording system

1. Are there written financial policy and procedure manual in your firm?
    a. Yes
    b. No
2. If your response no, what is/are the reason(s) for not having?
    a. I don't know
    b. Not required by regulatory body
    c. Not required by tax office
    d. Not important for my firm
    e. Cost of the manual is high
3. Does your firm maintain books of accounts for its financial operation?
    a. Yes
    b. No
4. If the response for the above is no, what is/are the reason(s)?
    a. Lack of experts because of high cost of accountant
    b. My firm is presumptive tax payer
    c. Accounting information does not add any value to the business
    d. Maintaining books of accounts is not mandatory by tax office
    e. Not regulatory body requirement
5. If your firm maintains books of accounts, what is/are the influencing factors for use of books of accounts?
    a. Availability of qualified expert
    b. Bank requirement to be eligible for loan
    c. Regulatory body requirement
    d. Tax office requirement
    e. Internal policy of my firm
6. What type of accounting information system your firm is using?
    a. None

b. Manual system
c. Semi computerized system
d. Accounting software
e. Fully computerized system

7. If your firm is used computerized accounting system, what is the software?
    a. I don’t know
    b. Peachtree
    c. Quick book
    d. Internally developed accounting software
    e. Integrated computerized information system
8. What are the components of your computerized accounting system?
    a. General Ledger
    b. Trial Balance
    c. Balance sheet
    d. Income statement
    e. Cash flow statement
9. For what purpose your firm is used the computer application?
    a. Recording business transaction
    b. Preparing accounting reports
    c. Preparing payroll
    d. Preparing financial statements
    e. Controlling the budget
10. Who is recording the transaction?
    a. Owner manager
    b. Manager
    c. Finance Head
    d. Employed Accountant(s)
    e. External Accountant
11. What is the basis of accounting your firm is using?
    a. None
    b. I don’t know
    c. Cash basis of accounting
    d. Accrual basis of accounting
    e. Modified cash basis of accounting

2.2. Financial reporting

12. Who is preparing accounting report?
    a. Owner manager
    b. Hired Manager
    c. Finance Head

d. Employed Accountants
e. External Accountants

13. Who is interpreting the accounting information?
    a. Owner manager
    b. Hired Manager
    c. Finance Head
    d. Employed Accountants
    e. External Accountants
14. What is/are the source(s) of financial information of the firm?
    a. I don't know
    b. Bank Information including bank statement
    c. Competitors
    d. Compliance requirements
    e. Financial statements(Balance sheet, Income statement, cash flow statement)
15. Does your firm analyze the trend of sales, cost, and profit?
    a. Yes
    b. No
16. If the response for the above is no, what is/are the reason(s)?
    a. I don't know
    b. Lack of expertise
    c. Not important for the firm
    d. Not required by the regulatory body
    e. Not required by tax office.
17. Does your firm file financial statements to tax office?
    a. Yes
    b. No
18. If no, what is/are the reason(s)?
    a. I don't know
    b. Lack of qualified staffs to maintain books of account
    c. Not required by tax offices
    d. No enforcement by the tax offices
    e. My firm is using presumptive tax system
19. If yes, what financial statements file to tax offices?
    a. I don't know
    b. Balance sheet
    c. Income statement
    d. Cash flow statement
    e. Statement of changes in equity
20. How frequently your firm is producing the financial statements?

a. I don’t know
b. Not produce
c. Quarterly
d. Semi annually
e. Annually

21. How frequently your firm is analyzing the financial statements?
    a. I don’t know
    b. Don’t analyze
    c. Quarterly
    d. Semi annually
    e. Annually
22. What kinds of financial analysis your business is doing?
    a. I don’t know
    b. Don’t prepare
    c. Ratio Analysis
    d. Trend Analysis
23. Are the financial statements audited periodically by external audit firm?
    a. Yes
    b. No
24. If your response is yes, what was the result of the most recent audit?
    a. I don’t know
    b. Unqualified opinion-clean report.
    c. Qualified opinion-qualified report.
    d. Disclaimer opinion-disclaimer report.
    e. Adverse opinion-adverse audit report.
25. If your response is no, what is/are the reason(s)?
    a. Not mandatory by tax office
    b. Not mandatory by regulatory body
    c. No enforcement mechanism by tax office
    d. No enforcement mechanism by regulatory body
    e. My firm is presumptive tax payer

2.3. Working capital management

2.3.1. Cash management

26. Does your firm prepare cash budget?
    a. Yes
    b. No
27. If your response is no, what is/are the reason(s)
    a. I don’t know
    b. Lack of competent person

c. Not important for the firm
d. Not required by tax office
e. Not required by regulating body

28. If you prepare cash budget, how frequently preparing cash budget?
    a. I don’t know
    b. Monthly
    c. Quarterly
    d. Semiannually
    e. Annually
29. Does your firm make daily deposit of cash collection?
    a. Yes
    b. No
30. If the response for the above is no, what is/are the reason(s)?
    a. Use the cash collection for daily business transaction
    b. Use the collection to invest in other business opportunity
    c. Use the collection for traditional saving mechanism (equb)
    d. Use the collection for other non business purpose
    e. Use collection for loan repayment to lender
31. What is/are the reason(s) for making cash flow projection in the firm?
    a. I don’t know
    b. Not done
    c. Past experiences
    d. Operation (transaction) motives of the firm
    e. Credit, inventory, and receivable policy of the firm

2.3.2. Account receivable and Account payable management

32. Does your firm sells products or services on credit.
    a. Yes
    b. No
33. If the response above is yes, what is/are the bases for credit sales?
    a. Available cash position in the firm
    b. Level of solvency and financial position of customers/credit worthiness of the customers
    c. Internal policy of the firm
    d. Available guarantee
    e. Cash conversion cycle and the time of receivables turnover
34. If the response above is no, what is/are the reason(s)?
    a. Fear of shortage of cash due to delay of collection
    b. Fear of risk of default of collection
    c. High cost of receivable management

d. In insufficient or none security of receivables
e. In insufficient law enforcement,

35. Does your firm purchase products or services on credit?
    a. Yes
    b. No
36. If the response above is no, what is/are the reason(s)?
    a. I don't know
    b. Take advantage of discount facilities by paying creditors promptly
    c. Doesn't know the advantage of purchase on credit
    d. Habit of inclined towards purchasing on cash or paying promptly when they purchase on credit
    e. Suppliers are not interested to sale on credit without guarantee
37. If the response above is yes, what is/are the bases for purchase on credit?
    a. I don't know
    b. Helps to improving cash flow
    c. Building supplier relationship
    d. Establish credit history
    e. Source of securing an interest-free short-term financing for businesses

2.3.3. Financial planning

38. Does your company practice financial plan?
    a. Yes
    b. No
39. If the response for the above is no, what is/are the reason(s)?
    a. I don't know
    b. Lack of expertise
    c. Not important for the firm
    d. Not required by the regulatory body
    e. Not required by tax office
40. If the response for question 39 above is yes, what kind of budget that your firm prepared?
    a. Sales budget
    b. Purchase, labor, and overhead budget
    c. Selling and Administrative budget
    d. Cash budget
    e. Budgeted balance sheet ,income statement, and income statement
41. Does your firm compare financial plan with actual performance?
    a. Yes
    b. No
42. If the response for the above is no, what is/are the reason(s)?

a. I don’t know
b. Not important for the firm and hence no system in place to do the comparison
c. Lack of competent staffs
d. Not required by regulatory body
e. Not required by tax office

43. If the response for the above is yes, what is/are the reason(s)?
    a. I don’t know
    b. Understand and improve the way money spend and managed
    c. Improve the allocation of scarce resource into future budget
    d. Enables remedial action to be taken as variance emerge
44. If you do the comparison, how frequently your firm is doing?
    a. I don’t know
    b. Monthly
    c. Quarterly
    d. Semiannually
    e. Annually

2.4. Financing and Investing activities

45. What is (are) the sources of your firm financing?
    a. Owner(s) investment
    b. Loan from bank
    c. Loan from microfinance
    d. Loan from Individuals and families
    e. Other
46. What is/are the factor(s) that influencing the financing decision of loan from bank or micro finance fto your businesses?
    a. High collateral
    b. High interest rate
    c. Fear of business fail and confiscation of the collateral by the bank
    d. Weak financial accounting record by the firm
    e. Low credibility of the firm by the bank for not fulfillment of the requirements
47. If your financing source is bank or micro finance, what is/are pledge collateral to guarantee later payment?
    a. Land, building under ownership of establishment
    b. Machinery and equipment
    c. Personal assets of owner (house)
    d. Moveable asset (vehicle)
    e. Personal assets of families/relatives(house)

48. What is/are withdrawal pattern(s) in your firm?
    a. Personal need
    b. Organization plan
    c. Business profitability
    d. Availability of cash
    e. Internal policy
49. What are the bases of costing and pricing decision of your firm?
    a. I don't know
    b. Internal analysis
    c. Competitor's prices
    d. Intuition
    e. Demand and supply position
50. What is/are the base(s) of financial decision in the firm?
    a. I don't know
    b. Making a choice from a number of alternatives
    c. Focus on profit maximization, market orientation, daily operation and survival activities of the firm market orientation.
    d. Considering risk and return of the firm
    e. Considering innovative, growth, and future actions
51. Does your business evaluate the visibility of the business before establishment?
    a. Yes
    b. No
52. If the response for the above is yes, what technique is used to evaluate?
    a. Payback period
    b. Accounting rate of return
    c. Net present value
    d. Post Pay-back Profitability
    e. Not known
53. If the response for question 51 above is no, what is/are the reason(s)?
    a. I don't know
    b. Lack of expertise
    c. Not important for the firm
    d. Not required by the regulatory body
    e. Not required by tax office

3. Non Financial information consideration

3.1. Financial objectives and strategies of SME

1. What is/are the goal of your firm?
    a. Profit maximization
    b. Customer satisfaction

    c. Providing employment
    d. Business growth
    e. Solve problems that occur in business community or environment.
2. Does your firm set short-term financial objectives?
    a. Yes
    b. No
3. If the response for the above is no, what is/are the reason(s)?
    a. I don't know
    b. Lack of expertise
    c. Not important for the firm
    d. Not required by the regulatory body
    e. Not required by tax office
4. If the response for question 3 above is yes, what is/are your firm short term financial objective(s)?
    a. Increase sales for more profit and cash making
    b. Optimize product/service price for more profit and margin
    c. Decrease expenses and cost of product/service for more profit and margin
    d. Increase liquidity and solvency(maintaining adequate level of working capital)
    e. Create comparative advantage analysis in terms of pricing and quality of service/product delivery.
5. Does your firm set long-term financial objectives?
    a. Yes
    b. No
6. If the response for the above is no, what is/are the reason(s)?
    a. I don't know
    b. Lack of expertise
    c. Not important for the firm
    d. Not required by the regulatory body
    e. Not required by tax office
7. If the response for question 6 above is yes, what is/are your firm long term financial objective(s)?
    a. Wealth maximization – Increase firm value
    b. Growth - increasing size and value of business in long term.
    c. Efficiency - maximizing return while minimizing inputs.
    d. Profitability - maximizing profits and making a financial return from business activities.
    e. Increase credit worthiness - Increase access to finance from bank and other financial institution.

3.2. Feedback system of the firm

8. Does your firm maintain feedback information recording system?
    a. Yes
    b. No
9. If the response for the above is no, what is/are the reason(s)?
    a. I don't know
    b. Lack of expertise
    c. Not important for the firm
    d. Not required by the regulatory body
    e. Not required by tax office
10. If the response for the above is yes, which stakeholder(s) is/are providing feedback about your operation(s)?
    a. Customers, suppliers, financer, and creditors
    b. Tax offices
    c. Regulatory body
    d. External auditor
    e. Wider community and staffs
11. In what area(s) the above mentioned stakeholders provide feedback to your firm?
    a. Internal control system and Internal financial practice and policy
    b. Pricing of product/service
    c. Solvency and liquidity
    d. Compliance requirement
    e. Social responsibility