A Profitability-Focused Assessment of Financial Literacy Level of Southeastern Nigeria SMEs

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ABSTRACT
Presently, unavailability of funds is no longer the major obstacle for Small and Medium Enterprise (“SME”) start-up and or survival as there are increasing sources of funds for new or existing SMEs. Recently, there are indications of a consensus among scholars that financial literacy, or the lack thereof, is a better indicator of the long-run enterprise survival chance. This study used four components of financial literacy – cash management, budgeting, financial record-keeping, and savings to establish the level of financial literacy of SMEs in the Southeastern region of Nigeria as well as to understand the effects of determined levels of financial literacy on enterprise profitability. Results show that majority of SMEs in the South-East Nigeria are not only financially literate but that their levels of financial literacy affected their profitability. The study also showed that the not-financially literate SME managers had significant inability with cash management and saving.

Keywords: Financial, Literacy, SMEs, Nigeria, South-East, Profitability

1.0. INTRODUCTION
Currently, Nigeria is a unique economic situation that is prime for significant contribution by SMEs for national structural transformation. According to (Fatoki, 2014), scholarly evidences indicate that with adequate resources and favorable environment, SMEs have potential to contribute to alleviation of various social problems including economic instability, unequal income distribution in addition to contribution to job creation in their respective societies. Because they assist to improve social quality of life, it can be argued that SMEs are a necessary component for a developed private sector. In the particular case of Nigeria, it is imperative for government to create an enabling environment for SME development. The 2012 enterprise baseline survey of Nigeria indicates that the national SME population of 17,000,000 provides about 32.4 million jobs which represents up to 46.5% of Nigeria’s Gross Development Product (GDP). It is therefore unquestionable that the SMEs are important, more so to a country like Nigeria, in the struggle for economic and structural transformation.

However, SMEs, irrespective of their nationality, but particularly in Africa and other developing economies, experience a number of difficulties (Kalekya & Memba, 2015). In Nigeria, SME development difficulty include inadequate or unavailability of financing, poor management skills and an almost non-existent administrative planning skill for efficient and effective deployment of available resources. Because of its sometimes visible effects of unavailability of capital and due to ease of attribution of failures to financing problems, scholarly attention focused on the effect of inaccessibility of capital and financial services on SMEs operations and profitability. Consequently, financial institutions, relying on the findings of these reports, consider SMEs as costly, high-risk loan beneficiaries and difficult clients for loan services.

With growing availability of information, improving technological infrastructure and reasonable governmental support, the cost of providing loan services to SMEs continues to decrease, leading to
improved financial assistance from financial institutions, thus making SMEs economic rising potentials. If SMEs are now able to access financial support from lending institutions, what then explains the low profitability, early death of most SMEs, as well as their inability to serve as enabling components for national structural transformation? It is not only arguable that earlier scholar-identified problems of SMEs are not exhaustive, but the focus on inability to access capital may be exaggerated. Studies like (Cole, Sampson, & Zia, 2008) affirm that there is a solid relationship between financial literacy and SME owner capacity to make sound financial decisions, improved profitability and business survival. A key objective of most business organizations is owner profit-maximization which is not attainable in the absence of profit. It can be argued that one unique, and almost universal, measure of organizational performance is profitability which is also a strong indicator of organizational operational dynamics. SMEs operational reality, particularly in Nigeria, is that there are still varied, and almost daily, decisions, often with financial implications, to be made; and the propriety or lack thereof of these financial decisions may be more critical to the survival of an enterprise than a mere shortage of capital. Relevant daily SME management decision include those focusing on savings, investments and retirement (Adomako & Danso, 2014). Consequently, financial literacy is an intrinsic component of SMEs survival, demanding of significant scholarship if developing economies like Nigeria must have any chance to enjoy significant contributions from this sector in their struggle for transformation. It is only from the combined contributions of all sectors of the economy that an entire society may be revived or even transformed. From improved performance and enhanced profitability that flows from sound financial literacy, Nigeria SMEs promises substantial contribution towards national poverty alleviation, reduction of income inequality, and increased job creation.

2.0. LITERATURE REVIEW

2.0.1. Financial literacy defined

Interests in financial literacy permeates all economies – developed, developing, and under-developed; and aided by global economic crises of recent times, financial literacy has generated substantial scholarly interests. It is, therefore, not surprising that the term has been defined in many ways including: a specific form of knowledge (OECD, 2005); the ability or skills to apply that knowledge, perceived knowledge, good financial behavior, and even financial experiences (Hung, Parker, & Yoong, 2009). Financial literacy has been thought to be a measure of the degree to which one understands key financial concepts; possess the ability and confidence to manage personal finances through appropriate short-term decision-making and sound long-range financial planning; while maintaining consciousness of life events and changing economic conditions (Redmund, 2010). Just like the Organization for Economic Co-operation and Development (OECD), the National Financial Educators Council (NFEC) defines financial literacy as the possession of requisite skills and knowledge on financial matters that enables one to confidently take effective actions that best fulfills personal, family or global community goals.

For the objective of this study, our position in agreement with (CBN, 2013) definition of financial literacy, is that a person is financially literate when he or she possess the combined sense of consciousness, understanding, and ability to conduct affairs timely and in relevant manner to facilitate his or her financial wellbeing. This position on financial literacy embodies the ability of the financially literate to make effective financial decision including Cash Management (CM), Budgeting (BU), Financial Record-Keeping (FRK) and Saving (SV). In this study, we hold that these components constitute the major variables of financial literacy. Following the CBN definition of financial literacy and our proposed major explanatory variables of the concept, we present the following questions on South-East Nigeria SMEs managers:

Q. 1. What is the level of financial literacy amongst managers of SMEs in South-East Nigeria?
Q. 2. Does the financial literacy status of a South-East Nigeria SME manager affect the enterprise cash management ability?
Q. 3. What is the relationship between the financial literacy status of a South-East Nigeria SME and the enterprise ability to budget?
Q. 4. Does the financial literacy status of a South-East Nigeria SME manager affect the enterprise financial record-keeping ability?

Q. 5. What is the relationship between the financial literacy status of a South-East Nigeria SME and the enterprise ability to save?

2.0.2. Implications of financial literacy

There are far-reaching implications for financial literacy including the enhanced readiness, and greater potential for success in periods of economic uncertainties. It is arguable that a financially literate business professional has greater tendency to improved allocation of resources thereby increasing the potential gains of diversified asset portfolio, adequate savings mechanisms, and proper assessment and procurement of increased insurance protection. Financial literacy increases one’s control over his or her financial future and provides avenues for the effective use of financial products and services as well as leads to decreased susceptibility to over-zealous financial misrepresentations. According to (Siekei, Wagoki, & Aquilars, 2013), when regulators are faced with a large educated population, the need for improved quality and efficiency of products and services is urgent and more likely to be considered. As (Siekei, Wagoki, & Aquilars, 2013) indicated, this is primarily because financial literate consumers have increased tendency to demand better financial products at reasonable prices, hence exerting pressure for health competition among providers of financial products. This study seeks to answer the following questions relative to financial literacy amongst owners and managers of SMEs in the South-East geo-political zone of Nigerian:

The longevity objective of business enterprises in likely unachievable in the absence of profit. While it is important to measure past and current profitability of business operations, the predictability of future profitability may not be ignored. Profit, here simply defined as the excess of an entity’s revenues over the expenses for a given period of time, create conditions for enhanced investing and financing activities of a business entity. In a broad sense, true enterprise profitability is the capacity to make generate excess revenues over expenses from all of an entity’s operating activities. If they must survive in the long run, SMEs must devise mechanism to achieve satisfactory levels of profitability in ever-changing, competitive, and rapidly globalizing market. Until, the managers and owners of SMEs comprehend the major aspects of profit determination beyond mere ignorant ideas of simply hauling in more money, continued business survival remain threatened. In the particular case of South-East Nigeria SMEs, the question is:

Q. 6. Does the level of financial literacy of SME managers in South-East Nigeria affect their business profitability?

The increased interest in financial literacy leads to our study on the relationship between the concept and business profitability. Scholars have assessed financial literacy through varied prisms including the correspondence between the concept and personal and business decision-making (Adomako & Danso, 2014); business performance and financial outcomes (Bruhn & Zia, 2011); as well as to profitability of women-owned enterprises (Kalekya & Mamba, 2015). Our study provides a critical assessment of the relationship between financial literacy and business profitability among SMEs of the very important South Eastern region of Nigeria.

South-eastern Nigeria was one of the initial 12 states created during the Nigerian Civil War, which later broke into the present Akwa Ibom State and Cross River State (Destination Nigeria, 2017). Subsequent to further states creation in Nigeria, South-east is now the name of one of Nigeria’s geo-political zones. The states in Nigeria’s South-east geo-political zone are Abia, Anambra, Ebonyi, Enugu and Imo, and their language is Igbo. South-east geo-political zone, which is the home of Nigeria’s oil wealth, borders the Atlantic Ocean and Cameroon to the south and east, respectively. What implications, if any, does financial literacy have for entrepreneurial profitability or survival? In their study on the impact of business and Financial literacy for young entrepreneurs, (Bruhn & Zia, 2011) discovered that the effects of training on individuals with below and above medium financial literacy at baseline differentiated their business outcomes and practices. Although entrepreneurs with below and above average financial literacy improved few aspects of their business practices, only those with above-
average financial literacy experienced rises in sales and profits consequent to their training (Bruhn & Zia, 2011). Similarly, (Simeyo, Lumumba, Nyabwanga, & Odondo, 2011) studied the effect of provision of micro-finance on the performance of youth micro-enterprises under Kenya Rural Enterprise program in Kisii county.

Financial literacy plays a vital role in the profitability of women-owned businesses (Kalekya & Memba, 2015), and because one’s level of financial literacy is positively correlated to his or her business management ability, the profitability of a business entity is subject to the influences from financial literacy of the owner and or management. Financially literate individuals properly and efficiently managed their business’ cash, prepared accurate and timely budgets and regularly saved surplus profits (Kalekya & Memba, 2015). In their presentation on sustaining SMEs through financial service utilization, (Nunoo & Andoh, 2012) indicated that financial literacy of Ghanaian SME owners is an essential factor in determining their utilization of financial services. Further, the modest state of financial literacy among Ghana SME owners creates an urgency for improved financial education.

Similarly, (Fatoki, 2014) suggests that financial literacy impacts positively on the capability of micro-entrepreneurs thereby increasing the prospects of financial inclusion into the social economic mainstream. However, (Fatoki, 2014) noted that most South African micro-entrepreneurs lack formal financial planning ability, proper record-keeping, control and budgeting, hence increasing the possibility of stunted profits and decreased operational capability and performance.

In order to get better insights into the Nigeria perspective of the influence of financial literacy on SMEs operation, we propose the following hypothesis:

**H1. Managers of South-East Nigeria SMEs are financially literate?**

**H2. There is a positive significant relationship between the financial literacy status of a South-East SME manager and the enterprise cash management ability.**

**H3. There is a positive significant relationship between the financial literacy status of a South-East SME manager and the enterprise ability to keep financial records.**

**H4. There is a positive significant relationship between the financial literacy status of a South-East SME manager and the enterprise ability to save.**

**H5. Financial literacy status of a South-East SME manager is significantly related to the SME’s profitability.**

### 3.0. RESEARCH DESIGN

In order to get further insights towards our research questions and hypotheses, we formulated a questionnaire to assess respondents’ proficiency in cash management, financial record-keeping, budgeting, and saving. The questionnaire also comprise questions on the entity’s average monthly profit; length of time of operation; number of employees and the length of time of their employment; as well as the weekly average sales of the entity. We conducted a pilot test of the questionnaire with 80 South-east SME managers and based on responses, further modifications were made to the questionnaire. Following their completion of the questionnaire, face-to-face interviews were also conducted. The personal interviews enabled us to elicit further explanation from the respondents’ relative to the responses provided on the questionnaire. Further, the interviews provided opportunity for in-depth explanation and examples aimed to further explain the terms and concepts in the questionnaires. The target population were selected SMEs in South-eastern geopolitical zone of Nigeria comprised of Abia, Anambra, Ebonyi, Enugu, and Imo states. From an approximate 550 questionnaires that were distributed, we received about 505. A total sample of four hundred ninety-eight (498) valid responses were analyzed.

### 4.0. FINDINGS

Out of the 498 respondents, 180 (36%) were from Abia, 100 (20%) were from Anambra, while 100 (20%), 70 (14%) and 73 (17%) were from Imo, Enugu, and Ebonyi States, respectively. We assessed
respondents’ financial literacy based on knowledge and skill of cash management, record-keeping, budgeting, and savings. An overall financial literacy score was computed for each respondent by combining responses across a range of questions measuring respondents’ knowledge and skill of cash management, budgeting, financial record-keeping and savings. The scores ranged from “financial literacy” (≤ 20) to “not financial literacy” (> 20). The histogram of financial literacy scores is shown in figure 1 below.

![Histogram of financial literacy scores](image)

**Figure 1**: Frequency distribution of financial literacy scores.

From the tables in Figure 1 above, we observe that 337 (67.67%) of the respondents are financially literate while 161 (32.33%) are not financially literate.

Crosstab analysis, figure 2, revealed that there is a statistically significant relationship between financial literacy and average monthly profit at the 95% confidence level (i.e. the calculated p-value < 0.05). About 89% of respondents who are financially literate reported average monthly profit > ₦100,000 with approximately 24% of them reporting average monthly profit of ₦1m above. Also, no financially illiterate respondent reported an average monthly profit of > ₦5m as compared to the 1.5% of the financially literate respondents that reported average monthly profit of ₦5m. On the other hand, a significant proportion (41%) of the not financially literate respondents reported average monthly income of < ₦100,000.

A further crosstab analysis revealed, as in Figure 3 below, that there was a statistically significant relationship between financial literacy and start-up capital (p-value <.05). The table in figure 3 shows that 301 of the 337 financially literate respondents had start-up capital of at least ₦2m while more than 20% of the not-financially-literate respondents reported start-up capital of less than ₦2m. Whether, and to what level, financial literacy affects availability of start-up capital may very well be a function of the budgeting and record-keeping ability of the manager; and only to the extent that such abilities may affect knowledge of where and how to source start-up resources as well to satisfy the conditions to enable receipt of the resources.
We then proceeded to assess the relationships between financial literacy and the component variables: CM, BU, FRK, and SV. In essence, our investigation was aimed at determining how much of a South-East SME manager’s financial literacy is explained by the combined influence of the variables.

Figure 4 above indicates a strong positive relationship between financial literacy and the component variables of CM, BU, FRK, and SV (Pearson R = .82). Similarly, we deduce that the component variables of the study explains an approximate 67% of the change in financial literacy status of a South-East Nigeria SME manager.
We now proceed to assess the relationship between financial literacy status of the SME managers with respect to the components of each variable – knowledge of a variable and skill to perform tasks relative to that variable.

A respondent has ability of any of the component variables of financial literacy if he or she has knowledge and requisite skills of that component variable. The tables in figure 4 indicate that there are statistically significant relationships between financial literacy and each of the component variables. From the tables, of the 337 financially literate respondents, 307, 306, 321, and 311 respondents were found to
have CM, BU, FRK, and SV abilities. The tables below indicate that the not-financially literate respondents have significant inabilities with respect to cash management and savings.

5.0. CONCLUSION
This study set out to assess the financial literacy level status of managers of South-East Nigeria SMEs; the relationship between their financial literacy status and the enterprise abilities to manage cash, budget, keep proper and adequate financial records, and save. Also, this study aimed at assessing the relationship between the financial literacy status of managers of South-East Nigeria SMEs and their enterprise profitability. The investigation was necessitated by findings by scholars in other countries that financial literacy is important and of paramount need for strong SME development and growth towards national economic transformations. With Nigeria’s current economic situation, SMEs are primed for significant contribution to national structural transformation. Fatoki (2014) suggests that there is evidence that with adequate resources and favorable environment, SMEs have potential to contribute towards increased economic stability, decreased income disparity, as well as job creation.

We set out to investigate what the evidences from Nigeria may suggest. We sampled, conveniently, SME managers from the five states of the South-East geopolitical zone of Nigeria. Our findings is that the high level of financial literacy among the responding SME managers. We also found that the financial literacy status of a South-East Nigeria SME manager is statistically significant relative to the enterprise ability to manage cash, budget, keep financial records as well as save. Further, we found that the financial literacy status of a South-East Nigeria SME manager is significantly related to the enterprise profitability.

We recommend increased government and financial institutions’ participation in financial literacy campaign among SMEs. Also, the financial literacy services should be delivered on a timely basis if the SMEs are to experience maximum benefits from the services. Our recommendation is based on the strength of our findings that SMEs with financially literate managers are more likely to be profitable, hence make positive and relevant contribution to the country’s development and structural advancement.

6.0. LIMITATIONS AND RECOMMENDATIONS FOR FURTHER STUDIES
The findings of this study, as is with most studies involving convenient sampling, may not readily lend themselves for generalization. The study was conducted among selected SMEs from chosen cities in the states. We do not doubt that the small sample size of 498 SMEs from five states that rank among the most commercial in Nigeria may have some impact on our findings. Notwithstanding the above-indicated limitations, we believe, that our findings will, generally, be consistent with any other study that conducted across more SMEs and across more geo-political zones.

Considering that Nigeria is made up of several tribes and cultures, in addition to its multi-religious and language composition, it will be interesting to see what, if any, is the relationships between financial literacy and personal characteristics including religion and culture. Finally, we suggest studies on methods that will lead to effective delivery of financial literacy services as well as determination of the impact of provided services on SME profitability.

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