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The financial management practices of small to medium enterprises

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Abstract:

This paper examines financial management practices in small to medium enterprises (SMEs) from a study of 289 small business owner-managers across 30 industry sectors in Australia and Singapore. The data was collected using a case study survey by MBA students and analysed via three stages: (1) examination of the quantitative survey data; (2) NVivo analysis of the interview data; and (3) Leximancer analysis of the selected coded transcripts. The findings show that SMEs have largely informal and ad hoc financial management practices. Differences by size and financial literacy levels were found. As the firm grows in size and complexity the owner-manager is required to adopt more sophisticated and systematic approaches to financial management. SMEs with higher financial literacy have greater capacity to monitor and control the financial performance of their businesses. Challenges for SMEs negotiating with more powerful players were also identified and approaches to address this issue briefly discussed.

Keywords SME, financial management, owner-manager, case studies.

INTRODUCTION

The success or failure of small to medium enterprises (SMEs) is contingent on their financial viability and one of the most common problems facing such firms is their ability to secure sufficient cash flow and working capital to remain profitable. It was noted as one of the top problems facing SMEs as long ago as the Bolton Report in the early 1970s (Bolton, 1971). This has been a recurring theme in the small business literature since that time (Carrington and Aurelio, 1976; Carland and White, 1980; Kennedy, Tennent and Gibson, 2006). This was highlighted in the 2014 *Sensis Business Index* report where the most important prime concerns of Australian SME owner-managers were lack of sales and cash flow, bad debts and profitability (Sensis, 2014).

Financial management in SMEs is often different to that found in large firms due to the more dynamic nature of their cash flow cycle, general paucity of working capital, and their ability to raise finance through debt or equity (Welsh and White, 1981). SMEs also lack the financial management and accounting systems available to large firms, as well as the professional staff who manage such systems. Typically the owner-manager is required to perform these tasks, often, but not always, with support from a bookkeeper and an accountant. This is a pattern found throughout the world, both within the advanced economies that comprise the Organisation for Economic Co-operation and Development (OECD) group of nations, and the developing economies (OECD, 2010; Abanis et al., 2013; Amoako, 2013; Uwonda, et al., 2013).

In Australia SMEs are defined as firms with less than 200 employees (ABS, 2002). They comprise around 99.7 per cent of the 2.1 million firms operating in the country (DIISR, 2011), and most (approx. 60%) are non-employing micro-firms with only the owner-manager as employee. This paper examines the financial management practices of SMEs drawing on a case study survey of 289 owner-managers from 30 industry sectors. It explores three research questions:

(1) How do the owner-managers of SMEs undertake financial management?

(2) Why owner-managers of SMEs manage their firms' finances in the way they do?

(3) How does this financial management behaviour impact the performance of SMEs?

This paper is organised as follows. First we review the literature relating to the financial management of SMEs. Then we overview the case study survey methodology used in this study before outlining the findings. A discussion of the findings is then undertaken before drawing conclusions, stating limitations and outlining future directions for research as well as implications for policy and practice. The paper's overall finding is that despite their relative lack of accounting and financial management systems and concerns over their profitability, most owner-managers surveyed for this study were profitable and not dependent on debt.

LITERATURE REVIEW

Whilst all firms can encounter problems of financial management the challenges facing SMEs are more significant due to their small size and vulnerability to fluctuations in cash flow. As Welsh and White (1981) wrote in their famous article "A small business is not a little big business", large firms tend to operate in relatively benign environments where rates of growth are small and an "approximate equilibrium" exists where "cash flow equals net profit plus depreciation and amortization" (p. 23). By contrast SMEs are seldom in equilibrium, impacted by seasonal sales cycle fluctuations and at the risk of losing major clients (Colot and Michel, 1996; Lavigne, 2002). Under such conditions they consume cash and require working capital to help them remain solvent as income dries up. Even in periods of growth the SME can experience financial problems as growth typically demands the firm has more working capital to help maintain its liquidity. As Welsh and White (1981) conclude:

> "Owner-management of a small business is a distinct discipline characterized by severe constraints on financial resources, a lack of trained personnel, and a short-range management perspective imposed by a volatile competitive environment. Liquidity must be a prime objective. The analytical models applicable to big business are of limited use in this arena. (p.32)

This unique nature of financial management in SMEs was acknowledged by the Beddall Report (1990) that examined the state of small businesses in Australia as well as by the OECD (2000) review of the role played by SMEs in job creation and economic growth. Both reports identified the challenges facing owner-managers seeking to raise either debt or equity capital in order to fund their businesses. As well as the heavy dependence SMEs have on the owner's collateral as security for loans, plus the critical importance of cash flow and retained profits.

Sources of financing

There are three primary sources of financing for SMEs: equity, debt and retained profits (OECD, 2004). The first of these is typically provided by the owner-manager who invests their private savings into the firm in order to launch it and/or leaves any accumulated earnings in the business to help fund future growth rather than drawing it out as dividends. Equity from third parties can take the form of informal investors (e.g. family, friends), semi-formal investors such as business angels, or formal venture capital funds managers (ABS, 2010; OECD, 2006). The second is comprised of borrowings (both secured and unsecured) that are typically provided by banks or other financial services firms. This debt can be short (e.g. credit card debt, accounts payable), or long term (e.g. mortgages) in nature (OECD, 2012). Banks are the most common provider of debt financing for SMEs, although this usually requires the owner-manager to supply collateral such as the family home or similar asset (Cowling and Westhead, 1996). Accessing credit is major challenge for SMEs and their access to short-term debt became more difficult and expensive in the period following the Global Financial Crisis (GFC) of 2008/2009 when compared to large firms (OECD, 2012).

In a review of the literature relating to the financing of SMEs, Abdulsaleh and Worthington (2013) note that the size and age of the firm, its ownership type and legal form, location, industry sector and assets structure all influence its funding decisions. Differences appear to exist between owner-managers based on their age, gender, education and experience in relation their preferences for financing. This is consistent with earlier research that suggests that owner-managers from SMEs prefer to fund their companies from their personal savings and retain profits rather than from bank loans or third-party equity (whether formal or informal) (Hamilton and Fox, 1998; Adair and Adaskou, 2011). Many SME owner-managers view debt financing as an "excessive" risk due to the bank's requirements for collateral, and therefore something to avoid if it is possible to do so

(Hankinson, 2000). They have also been found critical of banks that are viewed as offering poor service and charging too much for these services (Hankinson et al., 1997; Nakamura, 1999).

However, while banks have improved their services to SMEs in the past 25 years a major challenge facing owner-managers in securing bank financing is their firm’s structure and governance (Baudret and Allegret, 1996; Brau, 2002). This is typically centred on the owner-manager who is generally unwilling or unable to develop a long-term relationship with the banker. In general the SME owner-manager should seek to maintain a close working relationship with their bank, take the advice that is given, and have fees and charges explained and justified, and then be prepared to shop around if they cannot find satisfaction (Gammie, 1995).

Cash flow and working capital management

Two of the most important areas of financial management in SMEs are cash flow cycle and working capital management. Without cash or the liquid assets (working capital) that are necessary to operate on a daily basis, the company risks becoming insolvent and failing (Grondin and Cieply, 1999). Cash is generated from sales revenues (accounts receivable) and if this cash flow slows due to falling sales, or slow recovery of the accounts receivable, the business will need a cash injection or become insolvent. Under these circumstances the owner-manager will need to either inject more money from borrowing debt, or lower costs through cutting expenses (Carrington and Aurelio, 1976). For this reason the management of the cash flow cycle has been viewed as one of the most critical aspects of management in SMEs (Rowan, 1994).

Research has shown a positive relationship between the efficient management of cash flow (the cash conversion cycle) and working capital, and the firm’s profitability (Yazdanfar and Ohman, 2014). The more efficiently a firm manages its working capital the more it can boost its profitability. This emphasizes speeding up the recovery of accounts receivable while carefully managing inventory turnover (Enqvist, Graham and Nikkinen, 2014; Gul, et al., 2013). The owner-manager needs to ensure that they monitor their accounts payable (money the firm owes to creditors), and accounts receivable (money owed to the firm from debtors) closely. As many SMEs have fairly limited working capital the more efficiency they can develop in their management of the cash conversion cycle the more profitable they will be (Tauringana and Afrifa, 2013). SMEs that can shorten their cash conversion cycles (i.e. collect accounts receivable faster) are more likely to have high liquidity levels and greater working capital (Ebben and Johnson, 2011).

The management of working capital within the SME is therefore important to the firm’s success. There is also some suggestion that SMEs may have an “optimal level of working capital” beyond which their profitability might decline (Banos-Caballero, Garcia-Teruel and Martinez-Solano, 2012). However, the amount of liquidity an SME requires may depend on its age, size, industry, availability of owner-manager’s collateral, and whether it has access to bank overdraught facilities (Drever and Hutchinson, 2007). Access to finance by SMEs differs from large and public companies as the SME owner and his/her social networks are an integral part of their financial behaviour decision (including applications for loans) (Vos, Yeh, Carter and Tagg, 2007; Wincent, 2005).

Accounting systems and management practices

It is unsurprising to find a strong relationship between efficient cash flow and working capital management and profitability in SMEs. However, the main reasons many owner-managers get into difficulty are the poor financial control systems and management practices in their firms (Chapellier, 1997). Owner-managers need to be actively engaged in the monitoring of their firm's cash flow cycle, break-even and profitability (Vos and Roulston, 2008).

A study by Ekanem (2010) of SME owner-managers in the printing and clothing manufacturing sectors found that managerial practices differed by sector. For example, the average collection period for accounts receivable within the clothing industry was 30 to 90 days, while that in the printing industry was 14 days. Where clothing manufacturers employed "closed loop" learning with a resort to standard industry conventions, the printers were more likely to apply "open loop" learning, relying on advice from accountants and their own experience when setting their practices in debtor collection and credit management.

Many owner-managers do monitor their cash flow and financial positions closely with a keen eye on debtors and creditors (Kubickova and Soucek, 2013). In fact there is often a high focus by owner-managers on financial performance measures at the expense of non-financial ones, although such financial management is frequently ad-hoc and less systematic or formal than it should be (Perera and Baker, 2007). However, in many developing economies the use of formal accounting systems, credit management and cash flow monitoring is largely ad hoc and informal in nature (Orobia et al., 2013; Mungal and Garbharran, 2014).

This type of poor practice in financial management is typically due to owner-managers having insufficient skills and knowledge of financial accounting controls to know what to do (Uwonda et al., 2013). This typically results in these SMEs experiencing cash flow and liquidity problems with high levels of bad and doubtful debts (Abanis et al., 2013). In many developing economies it is not mandatory for SMEs to keep financial records and as a result the owner-managers fail to do so, often avoiding the need to pay taxes at the same time (Amoako, 2013).

In most advanced economies the requirement for SMEs to keep good financial records, and the obligation to do so for taxation compliance establishes their relationship with professional accountants and bookkeepers (Sian and Roberts, 2009). As the size and complexity of the business grows so too does the level of formality and sophistication in the financial management practices (Stafanitisis, Fafaliou and Hassid, 2013). Where owner-managers have greater skills and knowledge of the accounting and financial management processes they are more likely to generate financial reports and use them to make informed decisions (Van Auken and Carraher, 2013).

Given the significance of financial management decision making in SMEs, this study examines the financial management practices in SMEs, the perceptions of their owner-managers on this particular area of their role, and the impacts of their behaviour on the performance of SMEs.

METHODOLOGY

This research draws on a case study survey undertaken in Australia and Singapore over an 11 year period from 2003 to 2014. It was conducted as part of an MBA program focusing on small business management run within an Australian university. Student investigators worked in teams to undertake in-depth interviews with owner-managers representative of selected industries. Yin (2014) suggests that case study design is a preferred method when the main research questions deal with ‘how’ or ‘why’ issues, where the researcher cannot control the events they are studying, and where the phenomena they are investigating is contemporary. For this reason the case study survey methodology was chosen (Yin, 1982). A mixed-method approach involving the collection of both quantitative and qualitative data from owner-managers of SMEs was used as it offered greater opportunities for triangulation and complementarity (Molina-Azorin, 2007). It also allowed the study to be used as a teaching tool for the MBA program, while providing multiple cases that offer a deeper understanding of the phenomena and better “picture of locally grounded causation” (Miles, Huberman and Salandra, 2014)

Case study selection

The selection of cases was driven by the ability of the student investigators to identify, recruit and interview the owner-managers of the SMEs. Selection took a theoretical rather than a random sampling approach (Eisenhardt, 1989), with cases chosen for their ability to offer a good illustration of the key units of analysis (Garson, 2013). All firms had to meet the definition of being SMEs as provided by the Australian Bureau of Statistics (ABS, 2002), and within one of a selected industry sector. The program ran on an annual basis and so the data was collected each year. This provided a total of 289 interviews with the owner-managers of SMEs representing 30 industry sectors.

The majority (59%) of the firms had been in operation for more than 10 years with 41 per cent aged less than 5 years. This compares to the true population of SMEs in Australia were 44 per cent are less than 5 years old (ABS, 2008; 2013). All the firms had fewer than 200 employees with 49 per cent having less than 5 employees (micro-firms), 44 per cent between 5 and 20 employees (small firms), and 7 per cent over 20 staff (medium firms). This compares to micro-firms (84.2%), small firms (11.4%) and medium firms (4.1%) in the true population of Australian businesses (DIISR, 2011).

Crafting the instruments and protocols

The case study protocol was built on the conceptual framework proposed by D’Amboise and Muldowney (1988) that examines the SMEs’ task environment, organisational configuration, managerial characteristics, success/failure and stage of evolution/growth. This was combined with a framework developed by Hankinson et al. (1997) and Hankinson (2000) that examines the owner-managers’ lifestyle, skills and capabilities, management methods, motivation and sense of “identity” as a business owner, plus their relationships with banks and strategic vision for their firm. This protocol was used in conjunction with a diagnostic assessment tool developed by the authors. This comprised 124 questions grouped into 12 categories that examined a wide range of units of analysis at the level of the firm.

In this paper we explore the financial management and performance of these SMEs and the skills and capabilities of the owner-managers who operate them. The SME diagnostic assessment tool comprised questions on the firm’s actual financial performance. This included total sales, variable and fixed costs, gross profit, break even sales and net profit. It also contained 16 questions relating to the owner-managers’ views on sales trends, pricing, break-even and profitability management, cash flow forecasting and monitoring, sources of financing and financial management skills.

Data collection

Data collection involved having MBA students use the case study protocol and diagnostic survey tool to interview two small business owner-managers from selected industry sectors. The diagnostic tool was set up within an EXCEL spreadsheet with macros to produce a questionnaire that could generate a diagnostic report for the small business owner. The questionnaire used to collect the diagnostic information used a simple three-point scale for the various items coded 'Yes', 'Partially' or 'No' to each item, which asked specific questions about the owner-manager's operation of the business. It also collected data on owner-manager's past use of and attitudes towards outside assistance (e.g. sources of advice, use of consultants, mentors, business round tables and networking). The diagnostic tool was aimed at helping an SME owner-manager develop a well-constructed management operating system (Fassoula and Rogerson, 2003). Student investigators conducted in-depth interviews typically lasting over an hour with the owner-managers. They then provided the owner-manager with a copy of their diagnostic report as a reward for the interview. The students were then placed into groups and prepared an industry benchmarking report focusing on the industry sector from which the cases were drawn, and aggregating the findings from the individual cases.

DATA ANALYSIS AND FINDINGS

The total amount of data collected for this project was substantial. It included interview reports with the owner-managers, diagnostic reports and industry benchmarking reports numbering in the hundreds of which each were between 20 and 50 pages in length. This included both quantitative data from the diagnostic survey and qualitative data from the interviews with the owner-managers. It was analysed via three stages: (1) examination of the quantitative survey data; (2) NVivo analysis of the interview data; and (3) Leximancer analysis of the selected coded transcripts.

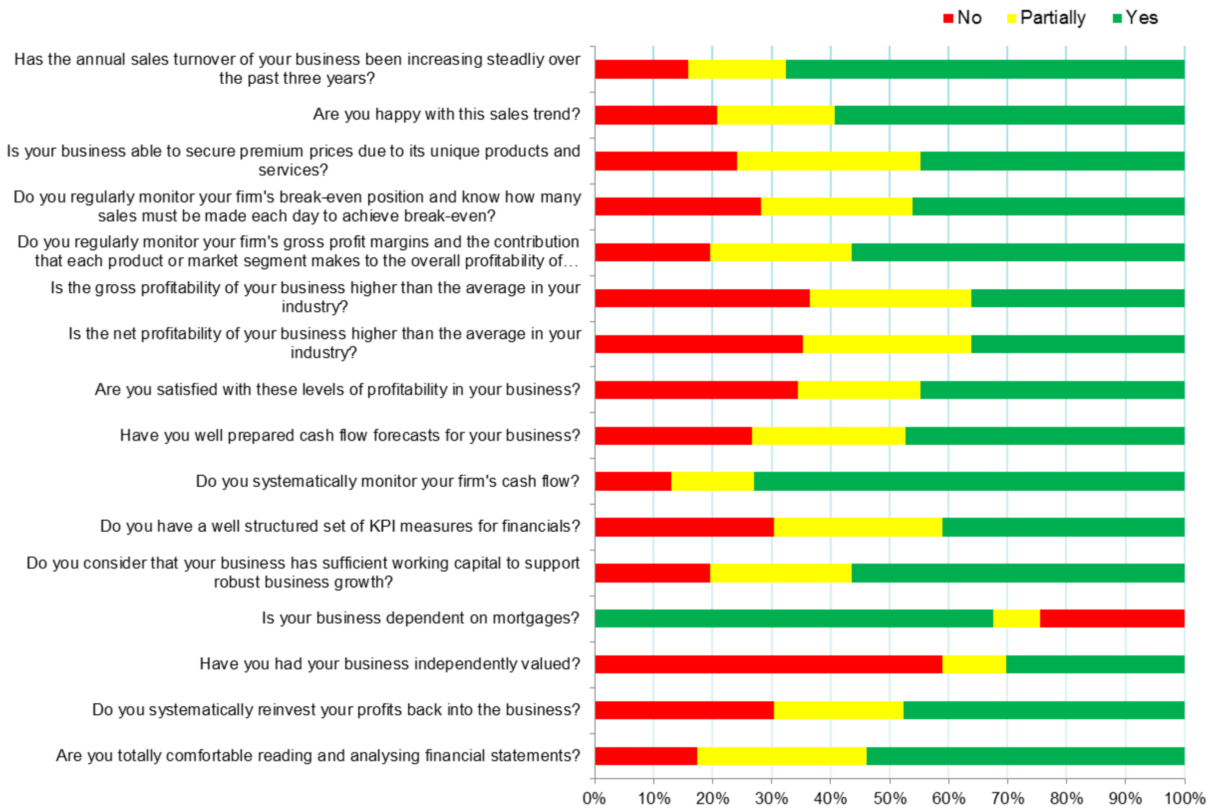
Quantitative analysis of the diagnostic assessment tool

The quantitative analysis of the data from the diagnostic assessment tool was undertaken using the SPSS statistical software package. This examined the financial performance data provided within the diagnostic survey as well as the 16 items relating to the owner-manager's financial management within the firm. A total of 187 firms (64.7%) of the total cases survey provided financial data. This revealed that total sales ranged from a mere $5,000 to $27 million with a median of $1 million. Gross profit margins (the amount of money left over once the variable costs are deducted from the firm's total sales revenue – the 'margin' is calculated as gross profit as a % of sales) varied by firm size with micro-firms showing an average of 47.4 per cent, small firms 51.6 per cent and medium firms 65.4 per cent. The gross profit of the firms also ranged from a loss of $500,000 to a profit of $27 million, with a median of $420,000. The median gross profit margin across these firms was 43.4 per cent. Net profit margins were an average of 25.5 per cent (median 20.6%), which was quite high considering that the net profit margin of Australian firms is around 11 per cent (ABS, 2014).

The break-even margin (the break-even sales figure calculated as a % of sales) for these firms was an average of 49 per cent. However, it varied by size of firm. For example, the average break-even margins were: micro-firms (47.4%); small firms (51.6%) and medium firms (54.2%), which suggest that the break-even increases with firm size as might be expected.

Overall the observations from this analysis of the firms' actual financial performance data suggests that these firms had similar performance data to that found in the broader business community (ABS, 2014). In relation to the 16 items relating to the owner-managers' financial management the findings are illustrated in figure 1.

Figure 1: Financial Management and Performance – Diagnostic Report Findings



It can be seen that most owner-managers reported they were generally on top of most of these issues. Only 16 per cent were negative about sales trends. However, only 45 per cent of these owner-managers indicated that they were totally happy with their firm's gross and net profit margins. Yet it was encouraging to see that 73 per cent of the owner-managers indicated that they systematically monitored their cash flow. Despite this less than half (47%) were positive that they had well-prepared cash flow forecasts in place, while a similar number (46%) said that they regularly monitored their firm's break-even position. Also of concern was the low number (41%) who expressed total confidence that they had a well-structured set of financial key performance indicators (KPIs) in place. Although more than half (56%) indicated that they regularly monitored their firm's gross profit across product line or market segment.

An analysis of those owner-managers who indicated they were comfortable reading and analysing financial statements, compared with those who were not, was undertaken using a chi-square test. Just over half (54%) of the owner-managers indicated that they were what we might describe as "financially literate" in relation to their understanding of the financial statements. When compared to their counterparts who did not claim such financial literacy some significant findings emerged (significant at the 0.05 level). The majority (60%) of the financially illiterate business owners did not maintain financial KPIs, compared to 51.5 per cent of the financially literature owners. The majority

(88.5%) of the financially literature owner-managers also reported monitoring their cash flow, compared to only 45 per cent of their financially illiterate counterparts. We found similar patterns with respect to cash flow forecasts (i.e. 62% of financially literature owners had them compared to 19% of financially illiterate owners), and regular monitoring of gross profit margins (71% versus 31%). It is also worth noting that the majority (68%) of owner-managers were not dependent on mortgages for the operation of their firms, but relatively few (30%) had had their business independently valued.

A principal component analysis (PCA) was also undertaken with the 16 items to help reduce the data and examine any underlying constructs. The Kaiser-Meyer-Olkin (KMO) measure of sampling adequacy (MSO) was 0.717 and the Bartlett's Test of Sphericity was significant at the 0.000 level suggesting that the data was suitable for factor analysis (Kaiser, 1974). The PCA was undertaken with a varimax rotation with Kaiser Normalization to provide a simplified structure. It generated an initial factor structure after eight iterations with six components accounting for 65.8 per cent of variance. Factor loadings for the items ranged between 0.506 and 0.911 suggesting that the items comprising these components were strongly associated (Stewart, 1981). However, subsequent examination of the scale reliability using Cronbach's alpha (Cronbach, 1951). This found strong alpha scores for only four of the initial six factors, one factor was a single item, resulting in a final structure of 5 components or 'factors' that were labelled: 'cash flow', 'profitability', 'sales turnover', 'monitoring' and 'mortgage financing'. The remaining items were left as independents. Table 1 lists these results.

An examination of these factors and the independent variables was undertaken. One-way Analysis of Variance (ANOVA) tests were used to examine differences between the firms of different sizes in relation to these variables. Scheffe's tests were used in the SPSS statistical package. Not surprisingly this found significant differences (at the 0.05 level) between micro, small and medium sized firms in relation to 'cash flow', with larger firms more likely to be positive in relation to the items that comprise that factor. This suggests that the larger firms are more likely to have owner-managers who use cash flow forecasts and KPIs to monitor their firm's performance, and who feel comfortable reading and using financial statements.

In relation to 'profitability' significant differences were found. Perhaps unsurprisingly the micros were found less likely to feel that their gross and net profitability were higher than the industry average than did their larger counterparts. This pattern was found for 'monitoring' and in relation to the reinvestment of profits, having the business independently valued the setting of premium prices and working capital. In general it suggests a divide between the micro firms and the large ones, with the owner-managers of these micro-businesses being less able to control and monitor their finances or set premium prices. They also appear to have less working capital available for growth.

Table 1: Principal Component (Factor) Analysis of Financial Management Measures

	Component				
	1	2	3	4	5
Factor 1: Cash-flow					
Do you have well prepared cash flow forecasts for your business?	.833				
Do you systematically monitor your firm's cash flow?	.775				
Do you have a well-structured set of key performance indicators (KPI) measuring such things as stock turnover, debtors and creditors, creditor strain and breakeven sales?	.682				
Are you totally comfortable reading and analysing financial statements (e.g. balance sheet, profit and loss, cash flow forecasts) to allow you to feel in control of your business?	.506				
Factor 2: Profitability					
Is the gross profitability of your business higher than the average in your industry?		.911			
Is the net profitability of your business higher than the average in your industry?		.899			
Factor 2: Sales Turnover					
Are you happy with this sales trend?			.852		
Are you satisfied with these levels of profitability in your business?			.667		
Factor 4: Monitoring					
Do you regularly monitor your firm's breakeven position and know how many sales must be made each day to achieve breakeven?				.876	
Do you regularly monitor your firm's gross profit margins and the contribution that each product or market segment makes to the overall profitability of your business?				.523	
Factor 5: Mortgage financing					
Is your business dependent on mortgaged property (e.g. your personal home) to secure its financial solvency?					.849
Independents					
Do you systematically reinvest your profits to build up the equity in your firm's balance sheet?					
Have you had your business independently valued particularly the amount of goodwill that might lie in the balance sheet?					
Has the annual sales turnover of your business been increasing steadily over the past three years?					
Is your business able to secure premium prices due to its unique products and services?					
Do you consider that your business has sufficient working capital to support robust business growth?					
Eigenvalues	3.772	1.899	1.573	1.060	1.015
Percentage of variance explained (total for 5 factors 59.4%)	23.57	11.87	9.83	6.62	6.35
Cronbach's alpha	.729	.886	.758	.619	

Case identification and coding

The conceptual frameworks used to shape the case study protocol provided the initial 'parent' nodes in the NVivo analysis, with 'child' nodes emerging to form sub-sets of the original framework. The coding continued with a process of removing any redundant nodes or nesting nodes within tree nodes to reduce the total number of overall themes to a reasonable level (Bazeley and Jackson, 2013). It is suggested that the coding continue until there are around 5-7 main themes interconnected via layering (Rovai, Baker and Ponton, 2013). This process was followed until seven themes emerged around: (1) financing (e.g. equity/debt); (2) break-even analysis; (3) cost control; (4) accounting systems; (5) the management of working capital; (6) the management of cash flow; and (7) pricing and profit. The coding process was also guided by the three research questions (Miles, Huberman and Salandra, 2014). Data was of two kinds, 'emic' or that derived from the owner-managers as direct comments during the interviews and from the diagnostic survey tool, and 'etic', which comprised the analysis from the MBA students who had undertaken the interviews and produced the industry benchmark reports. Both types of data are important in order to provide a comprehensive view of the phenomena being examined (Rovai, Baker and Ponton, 2013).

Table 2: Units of Analysis

Units of Analysis	Examples of transcript
Financing (debt/equity)	"In terms of financing the business, the most common, and yet the majority opted for personal savings, borrowings from friends and trust money as their means of capital funding. Bank loans were cited by two of the respondents and both admitted that approving bank loans was not a problem." (field note, cafe restaurant sector) "Those who borrowed money would have preferred not to and those who didn't borrow wished that they had had more funds to do things better." (field note, hosted accommodation sector) "Owner 'L' had strong ties with an investment banker who was part owner in the business, so financing seemed to be a lot easier. Owner 'JM'' had a loan from the bank to buy the business and said it was difficult to get, and he had to use his father as guarantor. His father was a part owner of the business and 'JM' was slowly buying him out as the business made profit." (field note, independent liquor store sector)
Break-even analysis	"The owner-manager has not worked out the break-even point but thinks it is around $30,000 a week." (field note, newsagencies sector) "All pharmacies reported regularly monitoring either the break-even position or gross profit margin and product contribution. However, notably 'I3', 'I5', 'F3' and 'F1' all reported regularly monitoring both parameters." (field note, pharmacy sector) "I am not sure how to calculate this; I usually just focus on weekly sales amounts." (owner-manager, newsagency)
Cost control	"The major credit suppliers of companies in General Aviation are banks, insurance companies, airports and air gas. The owners' ability to negotiate on administration fees, parking fees, fuel costs and insurance is limited." (field note, general aviation sector) "Both businesses interviewed were consistent with the above fixed costs most strongly impacted by staff wages. In 'JM' staff wages were actually over 60% of expenses which the owner is aware is higher than the industry norm. 'CC' and 'TR' have fewer building costs as the premises are owned outright with no current mortgage costs outstanding." (field note, travel agencies sector)
Accounting systems	"The majority of owner-managers interviewed showed a weakness with respect to financial management skills. Despite the fact that they generally were making a profit, few recognised that by having systems or better systems in place could potentially increase their profits substantially." (field note, graphic design industry) "Next, the implementation of the MYOB program for the businesses is an example of good practice, as it allows the owner-manager to closely monitor and control the business condition." (field note,

	florist industry sector) "Very few firms demonstrated evidence of management accounting systems. One firm did not appear to be aware of their break-even and a number of firms only reviewed their financial position on a yearly basis with their accountant." (field note, general aviation sector)
Working capital management	"Sufficient working capital to facilitate growth is available to 90% of the survey respondents, with a number of small business owners constrained by the general state of the economy. Seven of the ten respondents systematically reinvest profits to build up equity in the business, reducing the need for external funding." (field note, real estate industry) "The owner believes that his firm doesn't really need more financing in future, as they have a cash buffer." (field note, travel agencies sector) "Both of them are closely monitoring their financial performance. They claimed that their business is able to secure premium prices due to their unique services, and has sufficient working capital to support the robust business growth." (field note, independent consultants) "All owners reported a high capital investment requirement and three reported they had underestimated this requirement by some half." (field note, florist industry sector)
Cash flow management	"Budgeting and cash flow forecasts are a waste of time in my business because it is project based work and project duration alters constantly...Cash flow forecasts are difficult as month-to-month sales can vary enormously..." (owner-managers, graphic design industry) "Payments from customers in the B&B business are generally at time of sale; therefore cash flow is not generally a problem, though one owner reported that corporate customers were slow in paying bills. Occupancy rate and realisation of forward bookings was of much greater concern." (field note, hosted accommodation sector) "All interviewees kept daily, weekly, and monthly figures on both department and total store turnover, which was compared to previous years and months data. Of the KPIs in a volume driven industry, this was the most readily monitored. Turnover by area is also used as a guide for analysing the health of a store." (field note, independent supermarkets sector)
Pricing and profit	"Designers can be guilty of under-pricing themselves to keep clients. Stick to core business and keep up with the times. Position yourself accordingly by trying to keep out of areas that will disappear or where you have to lower your prices e.g. print with respect to annual reports and prospectus..." (owner-manager, graphic design) "Most B&B's stated that their pricing was based on 'what others were charging'. Using this strategy, several owners found they were undercharging and not making a profit and have gradually pushed prices up. One reported that it had found a point above which occupancy decreases and another pushed prices up, in line with the established market leaders in their region." (field note, hosted accommodation sector)

Table 2 lists the main units of analysis identified from the NVivo analysis and provides some examples of the 'emic' and 'etic' data taken from the transcripts. The general pattern that emerged from this was the absence of excessive bank borrowing or even equity financing, other than from family or friends. Most owner-managers preferred to finance their firms from initial owner savings and then retained profits. In terms of break-even analysis most firms had not formally calculated this, although they did possess a crude benchmark based on sales volume. For cost control the owner-managers were generally able to quickly identify their main costs of operations. However, they typically lacked much power to negotiate these costs which were usually imposed by more powerful suppliers, landlords or regulators.

Most owner-managers were relatively weak in their financial management skills and their firms' lacked sophisticated systems to monitor finances. While the majority had accounting software packages, these were used for financial accounting for tax purposes rather than for the more critical management accounting tasks. This translated into informal ad hoc methods of tracking working capital, cash flow, pricing and profit. As most firms were not seeking to grow, or to only undertake modest growth, the requirement for working capital was modest and could generally be funded from cash flow. However, in some cases where there was a need for more capital intensity, the working capital requirement rose.

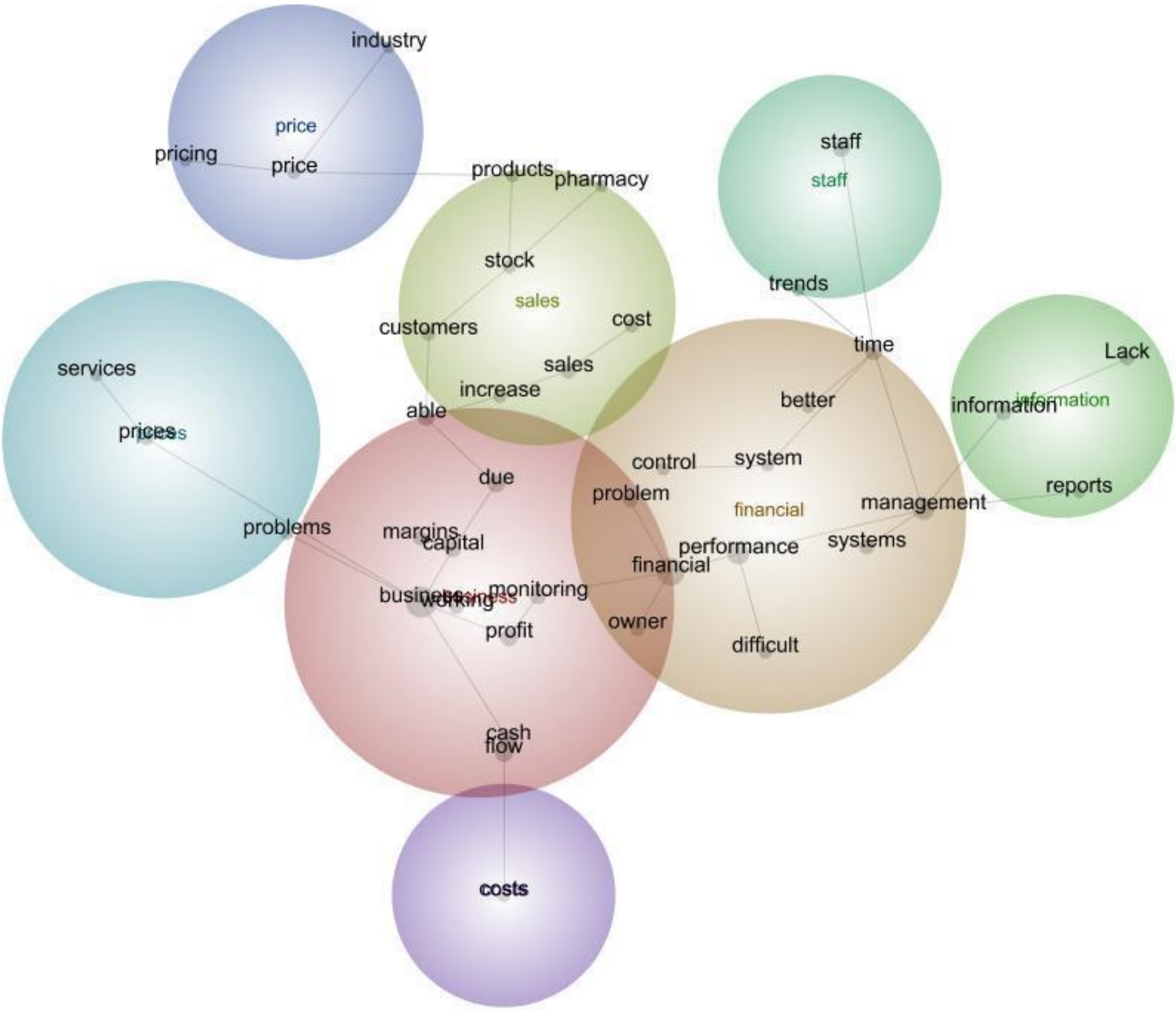
Although most owner-managers kept a close eye on their cash flow few had prepared cash flow forecasts. Many complained that it was not possible to generate reliable cash flow forecasts due to volatility in their sales, this was particularly the case for those firms that had seasonal or project based work. Finally, the pattern of setting prices was largely based on following the trend within the industry. However, this often resulted in the business under pricing and this squeezed profitability.

Leximancer analysis

Once the NVivo analysis had been completed we undertook further analysis of the relevant data relating to financial management using the text analytic software tool "Leximancer". This provides a both conceptual (thematic) analysis and relational (semantic) analysis, identifying concepts in the corpus and how they interrelate. Leximancer uses word frequency and co-occurrence counts as its basic data (Smith and Humphreys, 2006). It identifies how frequently words occur, and also tags them as containing a 'concept' if sufficient accumulated evidence is found to suggest that they represent a distinct concept (Leximancer, 2011). Terms found in the text are weighted so that the presence of each word in a sentence contributes to the body of evidence to support the existence of a concept. The Leximancer analysis generated a concept map (see Figure 2) that provides a visual representation of the data and the relationships between key concepts and themes located therein. A 'concept' is a collection of words that are associated within the text with each other. The bubbles are *themes* that contain concepts, with themes overlapping and clustering around concepts that are associated with each other in the same sequences of text.

As shown in Figure 2 the Leximancer analysis generated eight major themes: (1) *business*; (2) *financial*; (3) *sales*; (4) *prices*; (5) *price*; (6) *costs*; (7) *information*; (8) *staff*. The size of each theme "bubble" reflects their relative importance as they contain a greater number of related 'concepts'. Table 3 lists these themes and their related concepts as well as examples from the interview transcripts and field notes reflecting the nature of this data.

Figure 2: Financial Management and Performance – Leximancer Concept Map



As shown in Figure 2 and described in Table 3 the first theme *business* reflects the owner-managers' focus on the key tasks associated with financial management and a recognition of the importance of cash flow and working capital (particularly in the early years or during periods of growth). The *business* theme relates closely to the second theme *financial*, which is overlapped around the owner-managers' abilities to understand and use their financial management reporting systems for control. As reported in the quantitative analysis many owner-managers lacked financial management skills and those who did were generally happy with their financial accounting but not their management accounting capability. This issue became more prominent as the firms grew requiring more sophisticated systems.

Table 3: Leximancer Themes and 'Concepts'

Themes	Concepts	Examples
Business	'business' 'cash flow' 'profit' 'due' 'working' 'monitoring' 'margins' 'capital' 'owner'	"The present moment it is the cash flow of the business and securing capital to ensure that we have the right cash flow to increase sales to target. New business opportunities are arising and ensuring that we have the cash flow to finance these with ever tightening margins is the challenge, current restructuring of debt is the key to this." (owner-manager SME) "I found premises that would allow me to start the business on a small scale with little initial outlay, and on a very part-time basis. I have a lot of experience in music and teaching music, therefore good product knowledge and good knowledge of my customers' requirements, but no

	'able'	experience of financial planning, monitoring business performance and business cash flow". (owner-manager SME) "Some of the procedures such as cash flow forecasts were informally monitored. Due to the accounting and family background of the owner, it was clearly stated that the importance of monitoring financial performance of the business was of utmost importance, but the need for formal and/or documented procedures regarding these felt redundant." (field note)
Financial	'owner' 'financial' 'performance' 'difficult' 'problem' 'control' 'system' 'systems' 'better' 'management' 'time'	"I am not very good at handling financial matters in a systematic way, so I need help with people such as accountants and bookkeepers." (owner-manager SME) "Financial reporting mechanisms are good. However, we need more advice on how to manage the financial resources effectively. This needs to be done in the form of monthly KPIs that reflect the performance of the business, and is in addition to the quarterly covenant reporting provided by our financier." (owner-manager SME) "As the company grows I need to move to more sophisticated financial management systems and have somebody else take on the day to day financial operations – I will find this difficult to delegate!" (owner-manager SME)
Costs	'costs'	"You can pay someone to value it properly, but it costs $8,000 to $10,000 and after you pay that bill, that figure you are looking at will be even lower!" (owner-manager SME) "No real issues in particular. However, we could engage in more formal ways of tracking wastage rates and costs more systematically."
Sales	*'increase'* *'sales'* *'cost'* *'customers'* *'stock'* *'pharmacy'* *'products'*	"The monthly sales turnover does not meet the target every month". (owner-manager SME) "There are not enough sales to break-even the daily costs." (owner-manager SME) "The mark up on beer and spirits is minimal and profit margins on these products are low. To stay viable the owner-manager is always in the field, visiting suppliers to become the main distributor so that he can stock them in the store and ask a premium." (field note)
Prices	*'prices'* *'services'* *'problems'*	"Originally we looked at what other people were charging but then realised we weren't making a profit – so we gradually put up our prices." (owner-manager SME) "Both of them are closely monitoring their financial performance. They claimed that their business has sufficient working capital to support the robust business growth". (field note) "We don't experience any substantial problems with this currently, but we had massive problems with GST when it was first introduced. There are very few deductions in hairdressing, so it was essentially just adding 10% to our prices for the government without being able to claim this back anywhere." (owner-manager SME)
Information	*'information'* *'lack'* *'reports'*	"I feel that I haven't managed information effectively. But I haven't really thought about how to improve it." (owner-manager SME) "One of my main problems is a lack of timely information, and lack of tracking and reporting of information." (owner-manager SME) "I use my reports (both KPIs and financial) by the 20th of the following month and generally these are late. Unacceptable!" (owner-manager, SME)
Staff	*'staff'* *'trends'*	"My problem is a lack of communication between some of the senior staff members with the junior staff. It doesn't occur often but when it does occur it can be bothersome." (owner-manager SME) "We need to better utilise our sales figures so that we can analyse trends and respond quickly and efficiently." (owner-manager SME)
Price	*'price'* *'pricing'* *'industry'*	"Most of the respondents mentioned that they could not compete on price with larger firms. However, a majority of the interviewees stated that they had developed a model where they could charge a premium price for the goods they provided." (field note) "In terms of pricing their offerings, the majority of the owner-managers opted for an average pricing attitude." (field note) "Market insecurity is a concern, we (firm and industry) are very busy at the moment but some business units are not reflecting the return from demand that should be expected. There are some delegation and decision making issues relating to additional resources that we do not have a clear decision making process for." (owner-manager SME)

Associated with *business* are the themes *costs*, *sales* and *prices*. The first of these is linked to 'cash flow' and is concerned with the costs of operating the business including ways of tracking such hidden costs as wastage. The theme *sales* encompasses concepts relating to the owner-managers' recognition that insufficient sales will reduce cash flow, make it harder to break-even and place pressure on the working capital requirement of the business. The theme *prices* reflect the problems that poor pricing strategy can create for the business. This seems to be a particular issue for services firms and many owner-managers reported initially under-pricing or attempting to follow the market average or industry leader rather than setting their own price benchmark.

Other minor themes were *information*, *staff*, and *price*. The first of these reflects the owners' abilities in extracting information on their firms' finances. As reflected in the comments listed in Table 3, many owner-managers felt that they were not getting financial information in a timely manner. The second theme *staff* relates to the ability of the owner-manager to link the activities of their employees to the firm's activities and financial performance. Most SMEs have limited working capital and must keep a close eye on sales trends, cash flow, stock turnover and operating costs. This requires a range of monitoring systems and staff must understand the consequences, although most SMEs don't have such systems in place. Finally, the theme *price* was associated with how the owner-manager viewed their pricing within their wider industry context. A common pattern emerging from the data was the sense by the owner-managers that they could not compete on price with larger firms and what they should do strategically to address this threat.

DISCUSSION AND CONCLUSIONS

Our study collected data from a large sample of SME owner-managers across a wide range of industries over a period of more than a decade. It provides a picture of a small business community in which most firms are making do with largely informal and ad hoc financial management practices. Whilst some minor differences existed between firms and across industries, the overall pattern emerging from this analysis is that there is a division between the micro-business and their small and mid-sized counterparts. As the firm grows in size and complexity the owner-manager is required to adopt more sophisticated and systematic approaches to financial management.

Different patterns of monitoring financial data were found between those SMEs with financial literacy and those with limited financial knowledge or skills. Monitoring of financial data and performance appeared to be more systematic and comprehensive for financially literate SMEs. Hence, SME policy makers, advisors and educators/trainers have a major challenge to increase financial literacy across the SME sector and in particular within the micro firms which are the dominant business form. Providing access to financial education programs to develop financial skills and literacy will help SMEs to monitor and control their finances and increase their chances of survival. Gaining expertise with accounting systems, software and other financial tools will improve their ability to monitor the performance of their business, and move beyond routine tax reporting.

Our data confirms prior research on the funding preferences of SME owner-managers in general, as we found most owner-managers preferred to finance their firms from personal sources and to avoid excessive bank borrowing or even equity financing, other than from family or friends. The study shows that the key issues for SME owner-managers regarding financial management include controlling cash flow, monitoring costs and working capital requirements, and seeking to find the most appropriate pricing strategy to retain sales while also ensuring profitability. Most of the owner-managers from micro-firms were not confident in their ability to read and use financial statements. Further, most firms found that their accounting and reporting systems were adequate for financial accounting and tax compliance purposes, but inadequate for the more important task of monitoring their firm's financial performance on a daily, weekly basis.

While small size can increase agility, the difficulty of negotiating costs or contracts with more powerful suppliers, landlords or regulators was noted. This highlights another challenge for SMEs competing in a dynamic environment controlled by others. There are approaches SMEs can take to improve their bargaining power and to avoid direct competition such as focusing in a niche with a specialised product or service. However, it is also important to have a national system which includes some advocates for SMEs - such as the Australian Small Business Commissioners who assist SMEs with information, advocacy services, lobbying for regulatory changes, and dispute resolution.

Future research should be undertaken using in-depth case studies of different SME owner-managers across more industries. While this is time consuming it offers the opportunity to explore in-depth the actual task environment of the owner-manager. For the majority of SME owner-managers the effectiveness of their financial management is a make or break issue. Yet far too little attention is given to it. In a review of research into the financial management of SMEs Jindrichovska (2013) made the following observations:

> "There is a school of thought that believes that 'a well-run business enterprise should be as conscious of its finances as healthy a fit person is of his or her breathing'. It must be possible to undertake production, marketing, distribution and the like, without repeatedly causing financial pressures and strains. It does not mean, however, that financial management can be ignored by a small enterprise owner-manager; or as is often done, given to an accountant to take care of. Whether it is obvious or not to the casual observer, in prosperous small enterprises the owner-managers themselves have a firm grasp of the principles of financial management and are actively involved in applying them to their own situation." (p. 93)

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