Volume:6 Issues: 34 [June, 2021] pp. 43 - 49]
International Journal of Accounting, Finance and Business (IJAFB)
eISSN: 0128-1844
Journal website: www.ijafb.com

IMPACT OF FINANCIAL LITERACY AMONG SMALL MEDIUM ENTERPRISE OWNERS ON ENTERPRISE PERFORMANCE: A CONCEPTUAL FRAMEWORK DEVELOPMENT

Nur Farhana Sudarmoyo @ Suffari[1]*
Putri Rozita Tahir[2]

[1] Faculty of Business & Management, DRB-HICOM University of Automotive Malaysia, Malaysia
Email: nfarhana@dhu.edu.my
[2] Faculty of Business & Management, DRB-HICOM University of Automotive Malaysia, Malaysia
Email: putri@dhu.edu.my

Article history
Received date : 24-4-2021
Revised date : 25-4-2021
Accepted date : 15-6-2021
Published date : 13-7-2021

To cite this document:
Sudarmoyo @ Suffari, N. F., & Tahir, P. R. (2021). Impact Of Financial Literacy Among Small Medium Enterprise Owners on Enterprise Performance: A Conceptual Framework Development. *International Journal of Accounting, Finance and Business (IJAFB), 6 (34), 43 - 49.*

Abstract: *Small Medium Enterprises (SMEs) play a vital role and across all sectors of economy. Malaysia, like many other countries depend on SMEs in generating income, represent source of entrepreneurship abilities, creating job opportunities and expanding local and global market. The important aspect to be addressed is the ability of the SME owners to manage their financial matters effectively. One of the key success factors of the business is in financial management and it lies on the financial literacy of the company owners. Thus, the SMEs performance depends heavily on the financial literacy of the owners. In order to be financially literate, the owners must have financial knowledge, a well-defined attitude towards financial issues and a sense of financial awareness. Therefore, this paper has proposed a conceptual framework that consists of three variables namely, financial knowledge, financial attitude and financial awareness that would have impact on the performance of SMEs.*

Keywords: *Financial literacy, Financial performance, Small Medium Enterprise*

Volume:6 Issues: 34 [June, 2021] pp. 43 - 49]
International Journal of Accounting, Finance and Business (IJAFB)
eISSN: 0128-1844
Journal website: www.ijafb.com

Introduction

In today's globalized world, financial literacy has gained special attention of a wide range of private companies, government agencies, consumers, community and public as a whole. Financial literacy deficiencies affect an individual's day to day money management and the ability to make saving for their long-term goal such as investing and buying a home, upgrading standard of living and planning for financing retirement and many more. Ineffective money management make consumers vulnerable to serve financial crises. People are interested in learning the importance of financial literacy especially after the Asian financial crisis in 1998, the global financial crisis of 2008 and the European Sovereign debt crisis of 2012 (Yong & Tan, 2017). The concept of financial literacy is differently understood by different people based on the stage of life they are in, occupation, the level of income, etc. (Remund, 2010).

Existing literature shows numerous definitions of financial literacy. These definitions serve as guidelines for individuals to make decisions regarding their financial wellbeing. Financial literacy has also become a concern for governments, banks, employees, community groups, financial markets and other organizations, especially in developing countries (Hassan Al-Tamimi Al Anood Bin Kalli et al., 2009). This proves that financial literacy is not only important for individuals but also important at the business level (Firli, 2017). Most countries consider Small Medium Enterprises (SMEs) as the main actors for national and regional development primarily in the economic field (Rashid & Shami, 2018). This is recognized by the world because SMEs have a significant contribution in the field of socio-economics such as creating jobs, promoting exports, producing output, and encouraging people to become entrepreneurs (Keskin et al., 2010). Data from the World Bank shows that SMEs contribute 45% of total workers and 33% of total national income in developing countries (Okello Candiya Bongomin et al., 2017)

There is a significant obstacle to the performance and sustainability of SMEs. Lack of knowledge, skills, experiences, attitude and awareness will give impact on their business. According to Joo & Grable (2004), business people tend to make inappropriate, inadequate and in effective financial decisions because they lack personal financial knowledge, they do not spend time to learn personal financial management, they face complexities in financial transactions and variety of choices in financial products and services. Lack of business management skills can also lead to them having financial problems. These phenomena may also be the same to SME owners as SME owners are also business people. Thus, if owners want to expand the business, they should improve on their financial literacy so that they can keep their business finances in order. In addition, the owners should know how to stay out of debt and take responsibility of the money they are managing to ensure healthy enterprise performance. Therefore, this paper focused on developing the framework for financial literacy among SMEs owners by looking at three variables namely financial knowledge, financial attitude and financial awareness that have impact on performance of the SMEs.

Literature Review

Financial Literacy

Financial literacy is a major factor in determining the economic and financial stability of SMEs. Specifically, financial literacy has been variably defined as knowledge, ability or skills, perceived knowledge, good financial behavior, and financial experiences (Hung et al., 2011). Financial literacy is also about facts on personal finances and key to personal financial management (Garman & Forgue, 2002). In addition, the critical managerial competencies includes financing literacy in SMEs (J. A. Timmons, St. Spinelli, 2008).

In order to be effective entrepreneurs that constantly have financial issues, they must be financially literate (Kojo Oseifuah, 2010). Financially literate SME owners and managers make suitable financing decisions on the business performance at various growth stages of the business. Lusardi and Tufano (2009) also emphasized the ability to make decisions as a representation of financial literacy of managers. Moore (2003) stated that practical experience provides the basis for knowledge and other faces of financial literacy. Because of the varying definition of financial literacy, there is a need to look at how financial literacy is defined for SMEs.

Financial Knowledge

According to Peters (2010), education is the development of knowledge, character and skills of individuals. The literature reported that individuals with lower education levels have lower financial literacy or lack the numeracy skills (Lusardi and Mitchell, 2007a, 2013). From previous studies, the factors such as parent's education levels and the children's financial literacy are significantly correlated (Lusardi et al. 2010; Mahdavi, 2012). Wagner (2016), financial education studied in three ways. Firstly, how financial education affects the financial literacy scores of individuals. Secondly, how financial education affects short-term financial behaviors differently, and thirdly, by way of examining the effects of financial education on financial behaviors. Based on past research by (Gale & Levine, 2013), there the four approaches to financial education. The four approaches stated are employer-based, school-based, credit counseling and community-based. Besides that, Beverly et al. (2003) stated that financial behaviors might be hierarchal and that some behaviors may affected by financial knowledge.

Remund (2010) further added that being financially literate should not be just focused on understanding financial concepts but also include the ability to manage personal finances. However, past research by Lusardi and Mitchell (2014) showed that there is limited evidence showing the effectiveness of financial education. Therefore, more research is needed to address the gap that exists in existing literature. In addition, Potrich et al. (2016) posit that financial education is used as a development process to facilitate people's personal finance management. Most individuals cite their personal experience as the most important source of their financial learning (Beverly et al., 2003). One of the most important roles of financial education is to act as a preventive measure to manage debt (Anderloni & Vandone, 2011)

Financial attitude

Attitude refers to the way one feels towards certain financial problem that are measured by responses to a statement or opinion (Marsh, 2007). A person's behavior, which is determined by attitude, norm and the perceived control, is backed by his behavioral intention (Ajzen, 1991). Attitude consists of three components: cognitive, affective and behavioral (Alexandra et al., 2017). Financial attitude is a state of mind, opinions and judgments about finance (Pankow, 2003).

In terms of attitude related to risk-taking, it is defined as the firm conscious commitment of resources to projects with a chance of higher returns but may also entail a possibility of high failure (Lumpkin & Dess, 1996). This is further evidenced by a study that shows risk-taking as the link between entrepreneurial behavior and success where successful entrepreneurs are risktakers (Kuratko & Hodgetts, 2001). Moore (2003) goes as far as incorporating handy experience in the argument that provides the basis of knowledge and different perspectives of financial related proficiency. Cude (2010) examined effective factors of people's financial literacy. He observed that more work experience, higher levels of education, risk appetite, parental occupation, higher age, family income, and training attending classes will boost financial literacy. Bond & Meghir (1994) opined that credit terms also determined the extent to which SMEs access finance. Financial literacy has been reported to have a negative relationship to financial constraints (Sabri & MacDonald, 2010).

Financial awareness

Awareness is one sector of the managerial skills, where the owners and managers must look after the well-being of the business. The ability to read, analyze, manage and discuss various financial conditions that eventually lead to individuals' economic well-being (Lusardi & Tufano, 2009; Rahmandoust et al., 2011; Vitt & Ward, 2000). Deakins, Logan, and Steele (2001) found that owners-managers have different approaches concerning business planning. Lusardi & Tufano, (2009) Mandell (2007), emphasized the ability to make financial decision shows awareness of financial literacy. Berman and Knight (2008) stated that financial literacy needs to become part of every business culture. Audet & St-Jean (2007) discovered that the SME owner and managers, who perceived more and aware about the external service providers, make use of those services more than the SME owner and managers who did not hold any information about these services.

Lusardi and Mitchell (2007) examined how financial literacy affects people's preparedness for their retirement and established that financial literacy increases the planning for retirement and that people who plan for retirement have higher levels of wealth compared to people who do not plan. This show that financial literacy has indirect impact towards household saving behavior. Many researches have also shown that people with higher financial awareness and knowledge of finance are more capable of preparing themselves for retirement through better saving and insurance plans for future.

Performance of SMEs

The performance and growth of Small and Medium Sized Enterprises (SMEs) have throughout the nations, been of great concern to, among others, development economists, entrepreneurs, governments, venture capital firms, financial institutions and non-governmental organizations (A. Eniola & Ektebang, 2014).

In business, planning and decision-making needs to be rational based on available information. This implies that owners and managers of business should have a reasonable degree of knowledge related to make good decisions. Remund (2010) opined that financial literacy is the degree to which one understands important financial concepts and possesses the capacity and confidence to handle personal funds of appropriate, brief period decision-making and solid for long-term financial.

In the management field, firm performance can be interpreted as measures of good or indifferent management (Jennings & Beaver, 1997; Sefiani & Bown, 2013). The effects of a firm's performance depend on whether the firm has attained its goals or not (Davidsson et al., 2010). The general performance of the organization depends on the correct management at the three levels of management: the firm's ability to create acceptable outcomes, decision and actions.

Performance is also commonly employed as an index of a firm's health over a dedicated period. (A. A. Eniola & Entebang, 2015). Thus, the business performance is one of the key issues to be studied to see the relationship with enterprise performance.

Based on discussion of the above literatures, this paper posits three variables that can be included in the conceptual framework that would influence enterprise performance. They are financial knowledge, financial attitude and financial awareness.

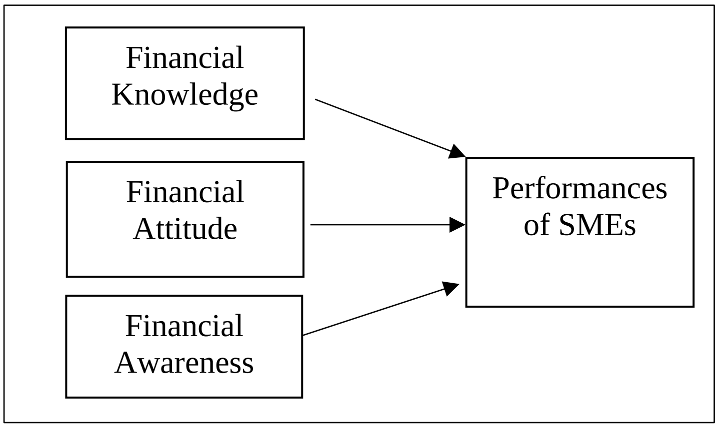

Figure 1: Framework

Conclusion

This paper contributes to literature on financial literacy among SMEs. The conceptual framework incorporates the three variables as factors that may have impact on financial performance, which would provide direction for future research. A suitable research approach and design will be chosen to determine the causality of the variables shown in the framework once finalized. More literatures will be reviewed to determine if there exist other factors that mediate or moderate the relationship. It is hoped that the result will provide indicators of financial literacy among the SME owners and add significant values to researches on performance of the SMEs.

References

Ajzen, I. (1991). The theory of planned behavior. Organizational Behavior and Human Decision Processes, 50(2), 179–211. *Organizational Behavior and Human Decision Processes*, *50*(2).

Alexandra, L., Erzsébet, N., & Boglárka, Z. (2017). Financial Personality Types and Attitudes that Affect Financial Indebtedness. *International Journal of Social Science and Economic Research*, *02*(09).

Anderloni, L., & Vandone, D. (2011). Risk of Over-Indebtedness and Behavioural Factors. In *Risk Tolerance in Financial Decision Making*. https://doi.org/10.1057/9780230303829_5.

Audet, J., & St-Jean, E. (2007). Factors affecting the use of public support services by SME owners: Evidence from a periphery region of Canada. *Journal of Developmental Entrepreneurship*, *12*(02). https://doi.org/10.1142/s1084946707000629

Beverly, S., Hilgert, M. A., & Hogarth, J. M. (2003). Household financial management: the connection between knowledge and behavior. *Federal Reserve Bulletin*, *59*(Jul).

Bond, S., & Meghir, C. (1994). Financial constraints and company investment. *Fiscal Studies*,

15(2). https://doi.org/10.1111/j.1475-5890.1994.tb00194.x
Cude, B. J. (2010). Financial Literacy 501. *Journal of Consumer Affairs*, *44*(2). https://doi.org/10.1111/j.1745-6606.2010.01168.x
Davidsson, P., Achtenhagen, L., & Naldi, L. (2010). Small firm growth. *Foundations and Trends in Entrepreneurship*, *6*(2). https://doi.org/10.1561/0300000029
Eniola, A. A., & Entebang, H. (2015). Government Policy and Performance of Small and Medium Business Management. *International Journal of Academic Research in Business and Social Sciences*, *5*(2). https://doi.org/10.6007/ijarbss/v5-i2/1481
Eniola, A., & Ektebang, H. (2014). SME firms performance in Nigeria: Competitive advantage and its impact. *International Journal of Research Studies in Management*, *3*(2). https://doi.org/10.5861/ijrsm.2014.854
Firli, A. (2017). Factors that influence financial literacy: A conceptual framework. *IOP Conference Series: Materials Science and Engineering*, *180*(1). https://doi.org/10.1088/1757-899X/180/1/012254
Gale, W. G., & Levine, R. (2013). Financial Literacy: What Works? How Could it Be More Effective? *SSRN Electronic Journal*. https://doi.org/10.2139/ssrn.2316933
Hassan Al-Tamimi Al Anood Bin Kalli, H. A., Hassan Al-Tamimi, H. A., & Anood Bin Kalli, A. (2009). Financial literacy and investment decisions of UAE investors Financial literacy and investment decisions of UAE investors. *The Journal of Risk Finance African Journal of Economic and Management Studies International Journal of Social Economics International Journal of Bank Marketing*, *10*(6).
Hung, A., Parker, A. M., & Yoong, J. (2011). Defining and Measuring Financial Literacy. *SSRN Electronic Journal*. https://doi.org/10.2139/ssrn.1498674
J. A. Timmons, St. Spinelli. (2008). Chapter 3: The Entrepreneurial Process. *New Venture Creation: Entrepreneurship for the 21st Century*, *100–118*.
Joo, S. H., & Grable, J. E. (2004). An exploratory framework of the determinants of financial satisfaction. *Journal of Family and Economic Issues*, *25*(1). https://doi.org/10.1023/B:JEEI.0000016722.37994.9f
Keskin, H., Senturk, C., Sungurt, O., & Kiris, H. (2010). The Importance of SMEs in Developing Economies Definition of Small and Medium-Sized Enterprises (SMEs). *2nd International Symposium on Sustainable Developement*.
Kojo Oseifuah, E. (2010). Financial literacy and youth entrepreneurship in South Africa. *African Journal of Economic and Management Studies*, *1*(2), 164–182. https://doi.org/10.1108/20400701011073473
Marsh, B. A. (2007). Examining The Personal Finance Attitudes, Behaviors, And Knowledge Levels Of First-Year And Senior Students At Baptist Universities In The State Of Texas. *Christian Higher Education*, *6*(3).
Okello Candiya Bongomin, G., Mpeera Ntayi, J., Munene, J. C., & Akol Malinga, C. (2017). The relationship between access to finance and growth of SMEs in developing economies: Financial literacy as a moderator. *Review of International Business and Strategy*, *27*(4). https://doi.org/10.1108/RIBS-04-2017-0037
Pankow, D. (2003). Financial Values, Attitudes and Goals. *North Dakota State University Fargo, North Dakota 58105.*, *2018*(16/07/2018).
Potrich, A. C. G., Vieira, K. M., & Mendes-Da-Silva, W. (2016). Development of a financial literacy model for university students. *Management Research Review*, *39*(3), 356–376. https://doi.org/10.1108/MRR-06-2014-0143
Rashid, N., & Shami, S. A. (2018). *Business Model for Sustainable Development: An Insight from Malaysian Automotive Industry*. *2*(1), 2600–8122.

Remund, D. L. (2010). Financial literacy explicated: The case for a clearer definition in an increasingly complex economy. *Journal of Consumer Affairs*, *44*(2). https://doi.org/10.1111/j.1745-6606.2010.01169.x

Sabri, M. F., & MacDonald, M. (2010). Savings Behavior and Financial Problems among College Students: The Role of Financial Literacy in Malaysia | Sabri | Cross-cultural Communication. *Crosscultural Communication*, *6*(3).

Wagner, J. F. (2016). An analysis of the effects of financial education on financial literacy and financial behaviors. *Journal of Behavioral Decision Making*, *11*(7).

Yong, H. N. A., & Tan, K. L. (2017). The influence of financial literacy towards risk tolerance. *International Journal of Business and Society*, *18*(3).