ST. MARY'S UNIVERSITY

SCHOOL OF GRADUATE STUDIES MBA PROGRAM

"FINANCIAL MANAGEMENT AND REPORTING PRACTICE IN MICRO AND SMALL ENTERPRISES THE CASE OFADDIS ABABA LEDETA SUB-CITY"

BY

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Financial Management and Reporting Practice in Micro and Small Enterprises the Case of Addis Ababa Lideta subcity

BY

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Declaration

I, Esubalew Takele, undersigned, declare that this thesis is my original work, prepared under the guidance of Abebaw Kassie (PhD). All sources of materials used for the thesis have been duly acknowledged, the researcher further confirm that the thesis has not been submitted either in part or in full to any other higher learning institution for the purpose of earning any degree.

Esubalew Takele ________________

St. Mary's University, Addis Ababa **July, 2020**

ENDORSEMENT

This thesis has been submitted to St. Mary's university, school of Graduate Studies for examination with my approval as a university advisor.

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Advisor Signature

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Abstract

Financial management is indispensable for all companies because having, reaching and analyzing financial information is a vital issue for all successful businesses. This study was conducted with an objective of identifying practices of financial management and reporting at MSE in Lideta Subcity in Addis Ababa. From this broad objective the study has assessed practices of financial management, reporting and bookkeeping, and methods and basis of account recording in the enterprises. To meet these objectives the study has targeted employees with role of financial management and reporting. There are 1,475 MSE in the Subcity and thus 1,475 target population. Sample size for the study was determined by using Carvalho (1984) and set to be 200 samples. Respondents for the study were randomly selected by using list of MSE as sampling frame. From the employees, data for the study was collected by using questionnaires and interview and then analyzed by using descriptive statistics. Based on the findings the study concludes that financial management and reporting practice of most of micro and small scale enterprises found very poor and needs many improving activities.

Key Words: Financial management and reporting, Micro and Small Enterprises, Finance Mangers

CHAPTER ONE
INTRDUCTION

1.1 Background of the Study

Financial management is one of several functional areas of management but it is central to the success of any small business (Meredith, 2006). Financial management is the management of finances of a business in order to achieve the financial objectives of the business. McMahon et al. (2013) defines financial management based on mobilizing and using sources of funds: Financial management is concerned with raising the funds needed to finance the enterprise's assets and activities, the allocation of theses scare funds between competing uses, and with ensuring that the funds are used effectively and efficiently in achieving the enterprise's goal.

McMenamin (2009), stated that financial management may simply be defined as 'the ways and means of managing money' but more formally; it is the determination, acquisition, allocation, and utilization of financial resources, usually with the aim of achieving some particular goals or objectives. In support, Van Horn and Wachowicz, Jr. (2008) observed that financial management is concerned with the acquisition, financing, and management of assets with some goal in mind. According to a study by Nguyen (2001) on the financial management practices and profitability of small and medium-sized enterprises (SMEs) in Australia. SMEs apply financial planning practices such as financial, operational, sales and cash budgets; whilst 83% frequently ·compare budgeted and actual results. SMEs use accounting information systems to monitor and execute their accounting operations. According to Maseko and Manyani (2011), accounting systems is source of information to owners and managers of small businesses operating in any industry for use in the measurement of financial performance in areas such as costing, expenditure and cash flow, by providing information to support monitoring and control.

Ismail and Zin (2009) investigated the practice of financial management among Malaysian small and medium-sized non-manufacturing firms. They found that half the

SMEs that prepared accounting information used computerized accounting systems and just over half sought financial advice from accounting firms. In addition, they found that 40% of the SMEs did not prepare a balance sheet. Maseko and Manyani (2011) investigated the record-keeping practices for performance measurement and improving the financial management practices of SMEs in Zimbabwe. They found that due to a lack of accounting knowledge the majority of SMEs did not keep complete accounting records and concluded that there was inefficient use of accounting information. An earlier study by McMahon (1999) found that most SMEs did not prepare a complete set of financial statements; and some did not prepare any financial statements.

The need to prepare a complete set of financial statements increases as an entity progresses from small to medium size. It is at the medium-size stage that financial performance reporting will be useful to internal and external users. External users include lenders and suppliers of raw material or finished goods. In most cases owner managers prepare financial statements in MSEs and many are not financially literate: it is possible that they resort to this practice to avoid the cost of hiring accountants (Everaert et al, 2006). Although, an efficient financial management involves several activities either carried out step by step or simultaneously. At best, each of these activities may be described as a financial management function and therefore individually, they do not represent the full functions of financial management.

1.2 Background of MSES development in Ethiopia

Ethiopia has scored double-digit growth in the past 10 consecutive years. Recognizing the role of Micro and Small Enterprises (MSEs) in the socio-Economic development of the country and giving special attention to the sector, MSES policy and strategy is prepared and imprinted in the past 17 years. MSE are designed to ensure the sustainability of the development achieved in all economic sectors of the country, the main focus of the government is creating Job opportunities through MSEs development, to reducing unemployment and alleviate poverty and enhancing MSEs to be base for industrial development in the country. The sector is crucially important to the economic and social development of the country in the sense that it generates broader job opportunities and assist to alleviate poverty and facilitates rural and urban economic linkage and boost the economy as well as promotes Entrepreneurship culture and enhance self-employment and serves as fertile ground for the emerging of Medium and Large Industries, etc.

According to Federal Micro and Small Enterprise development agency (FeMSEDA), (2017) in order to achieve these goals and objectives, the Federal Micro and Small enterprises development Agency (FeMSEDA) was to support, coordinate and formulate policies and programs, for the promotion and development of MSE sector. In its commitment to the socio-economic development of the country, the Government of Ethiopia has given greater focus for the development of the MSES Sector. In order to realize this, the Government of Ethiopia has designed the first MSEs Development Strategy in 1997. This strategy was intended to create coherence with the other economic sectors and outline duties and responsibilities of all the stakeholders at all level (from Federal to Kebele level). The revised MSEs Development Strategy was designed in 2011 in order to integrate the development of the sector with the country's 5 year (2011-2015).

Growth and Transformation Plan (GTP), hoped to bring about rapid economic growth and lift up the country to middle income level. The MSES Development was integrated in the GTP as one of the pillars of the Industrial Development Plan and taken as one of the best tools to implement the country's Industrial Development Strategy. According to revised strategy MSEs are defined on the base of total capital and working labor engaged (FeMSEDA, 2019).

Small and Micro enterprises establishments both individual and as a partnership two or more individuals in lideta sub-city also more of enterprises form as a partnership this is not always by their interest rather the system push them to create partnership because of some sector are restricted to individual so, financial management and reporting practices important for the members trust and work as a team. Small and Micro enterprises are a promising to job creation, innovation and development of the country but without proper financial management it cannot be real. Therefore, this study was conducted to assess practices of financial management and reporting in the enterprises particularly by using MSE in Lideta Subcity, Addis Ababa.

1.3. Statement of Problem

Micro and small enterprises in Ethiopia provide goods and services in promoting innovation and enhancing the enterprise culture, which is necessary for private sector development and industrialization. Micro and small enterprises (MSEs) offers economic, social and educational benefits both to for themselves and the societies at large. This is because the objective of micro and small enterprises is transfer the owners' condition such a way that they make their social life riches and happier and contribute for national GDP (FeMSEDA, 2019). FeMSEDA, (2019) suggested to implement strong financial management activities to improve their overall performance and the financial performance.

Sosyal (2013) states that financial management is concerned with all areas of management, which involve finance not only the sources, and uses of finance in the enterprises but also the financial implications of investment, production, marketing or personnel decisions and the total performance of the enterprise. Financial management is indispensable for all companies because having, reaching and analyzing financial information is a vital issue for all successful businesses. When financial transactions are recorded properly based on standard principles, it is possible to know easily the position and operational activates of a micro and small enterprises and increases members and lenders confidence and accountability of each. Based on these importances, managers of companies are highly recommended to understand the meaning of financial data and follow the regulations which affect financial report of the company.

Financial management in MSE is a key to operating business that involves managing assets such as cash, account receivables, inventories and fixed assets. It includes managing liabilities such as account payable and obtaining favorable long term financing. Sufficient members or equity capital and sound financial position must be maintained that will be acceptable to creditors, supplier, or buyers of MSE. Activities carried on by an MSEs involves substantial amount of capitals which requires proper management and reporting practice as per the country law and state law or as per generally accepted accounting principle. This suggest it is important to study financial management and reporting practices in MSE.

Although the enterprises have different roles, Yared, (2018) and Assegedech (2014) indicated that there are various types of challenges that micro and small enterprises faces such as marketing problems which includes lack of product diversity, pricing problems, lack of awareness how to compete in the market, limited business management and salesmanship ability, and limited capacity to promotional activities are also hindering the development of MSE, luck of formal and informal linkage, luck of good infrastructural facilities, luck of access to finance and credit, inadequacy of credit facility, in efficiency of service delivery. In addition, Weldegbriel (2017) identified the Problems of Micro and Small Enterprises in Addis Ababa including the financial management practices. Findings from studies done earlier and government reports on the state of affairs of small scale enterprises reveals that the sector faces numerous problems and constrains that affect their performance.

While much research has been done on the small business, little has been done specifically on financial analysis and reporting practices of SMEs in Ethiopia. These studies have focused on opportunities and challenges of the enterprises. But they failed to the weakness and strengths of the enterprises regarding financial management and reporting. The overall problem therefore is that relatively little is known about the relationship between financial management and reporting practices of small and medium enterprise in Addis Ababa in general and Lideta Subcity in particular. Therefore, this study was conducted to assess financial management and reporting practices of micro and small enterprises in Lideta Subcity.

1.4 Research Questions

In line with the above purpose the following specific research questions formulated for investigation;

- What are practices of financial management in MSE in Lideta Subcity?
- How reporting and bookkeeping are practiced in MSE in Lideta Subcity? and
- What are methods and basis of account recording in MSE in Lideta Subcity?

1.5. Objective of the Study

1.5.1 General Objective of the Study

General objective of the study is to assess financial management practices in SME in Lideta Subcity.

1.5.2 Specific Objectives

This study was conducted with following specific objectives;

- To assess practices of financial management in MSE in Lideta Subcity;
- To identify reporting and bookkeeping practiced in MSE in Lideta Subcity; and
- To assess methods and basis of account recording in MSE in Lideta Subcity.

1.6. Significance of the Study

This study aims to assess the financial management and reporting practice of micro and small enterprises that create meaningful results on the economic development and help reduce poverty. Since this study was conducted with considerations of local and internationally accepted reporting standards, stakeholders of the enterprises as owners would use the research findings to revise the financial management practices. Therefore, this study is important for MSE in Lideta Subcity in particular and in Addis Ababa in general.

Therefore, the study is expected to have some practical contributions in a sense that it shares some light on the direction of micro and small enterprises financial management. In this regard the study assists the effort of Addis Ababa Lideta sub-city to combat one of country strategy in area of poverty alleviation and unemployment reduction. These in turn are expected to help Micro and small enterprises technically assisted by Addis Ababa Lideta sub-city to become productive and profitable.

1.7 Scope and Limitation of the Study

This study is delimited to Financial Management and Reporting practices of micro and small enterprises in Addis Ababa: the case of Lideta sub city. The researcher selected this Sub city from ten sub-cities which has better equitable distribution of all types of MSEs under the study by considering the essentiality of studying the financial management and Reporting Practices the of MSEs in Addis Ababa, and by supposing the selected sub city is representative enough to infer about MSEs in the City. It is known that different factors may influence performance of MSEs. However, this paper has confined only on service year, Financial management and reporting practice of micro and small Enterprises (MSEs) of Addis Ababa Lideta sub-city.

1.8. Organization of the Thesis

The rest of the paper is organized as follows: chapter two presents the theoretical and empirical related literature to the study, while chapter three provides research methodology. Chapter four outlines data presentation, analysis and interpretation and chapter five concludes and suggests some recommendations.

1.9. Operational Definitions of Terms

Enterprise: It refers to a unit of economic organization or activity whether public or private engaged into the manufacturing of goods.

Micro enterprise: means commercial enterprise whose capital is not exceeding birr 20,000 other than high technology and consultancy services.

Small enterprise: means a business engaged in commercial activities whose capital is exceeding birr 20,000 and not exceeding 50,000 birr, other than high technology and consultancy service institutions.

Partnership: involves two or more individuals who have a partnership agreement to operate a business and share the earnings and liabilities of the venture.

Respondent: respondents are those individuals who are owner managers or operators of an enterprise.

CHAPTER TWO

LITERATURE REVIEW

Introduction

The chapter looks at literature on the research topic "Assessing financial management and reporting practices of micro and small scale enterprises on Lideta Subcity". The chapter also gives a review of numerous literatures on Micro and small enterprises considering theoretical and empirical studies to the subject matter.

2.1. Definition and Concepts

2.1.1 Micro and Small Enterprises

The definition of micro and small enterprises is still controversial. There is no generally accepted definition of micro and small enterprises. Micro and small enterprises in one country may be small or medium enterprises in the other country. Many developing countries apply based on specific parameters, which include factors such as the number of employees, asset, capital, sales turnover, etc. The definition which is based on the above criterion partially focuses on specific target groups for any preferential treatment of the various actors in the MSE recognizing that, there are no standard definitions of MSE. Thus, the definition of MSE depends on the stage of economic development of the country.

According Bolton Committee (1971), first an "economic" and "statistical" definition of a small firm was formulated. Under the "economic" definition, a firm is said to be small if it meets the following three criteria: relatively small share of their market place, managed by owners or part owners in a personalized way, and not through the medium of a formalized management structure; and independent, in the sense of not forming part of a large enterprise. On the other hand, the "statistical" definition, the Committee proposed two criteria; size of the small firm sector and its contribution to GDP, employment, exports, etc.; the extent to which the small firm sector's economic contribution has changed over time (Bolton, 1971). The sectorial classification has also used as criteria to define MSEs by Bolton Committee. Accordingly firms in manufacturing, construction and mining were defined in terms of number of employees (in which case, 200 or less qualified the firm to be a small firm), those in the retail, services, wholesale, etc. were defined in terms of monetary turnover (in which case the range is 50,000-200,000 British Pounds to be classified as small firm) whereas, firms in the road transport industry are classified as small if they have 5 or fewer vehicles (Bolton, 1971).

However, there have been criticisms of the Bolton definitions. This center mainly on the apparent inconsistencies between defining characteristics based on number of employees and those based on managerial approach. In Japan, small-scale industry is defined according to the type of industry, paid-up capital and number of paid employees. Thus, small and medium- scale enterprises are defined as: those in manufacturing with 100 million yen paid-up capital and 300 employees, those in wholesale trade with 30 million yen paid-up capital and 100 employees, and those in the retail and service trades with 10 million yen paid-up capital and 50 employees (Ekpenyong, 1992).

European Union (EU) Member States, traditionally have their own definition of what constitutes an SME, for example the traditional definition in Germany had a limit of 250 employees while in Belgium it could have been 100. But now the EU has started to standardize the concept. Its current definition categorizes companies with fewer than 10 employees as "micro", those with fewer than 50 employees as "small", and those with fewer than 250 as "medium" (Carsamer, 2009).

By contrast, in the United States, when small business is defined by the number of employees, it often refers to those with fewer than 100 employees, while medium-sized business often refers to those with fewer than 500 employees. Canada also defines a small business as one that has fewer than 100 employees (if the business is a goods-producing business) or fewer than 50 employees (if the business is a service-based business), and a medium-sized business as fewer than 500 (Carsamer, 2009).

Generally, from the global experiences of the definitions of MSE entails that there is no commonly used definition of MSE across the countries of the world. However, all the definitions have taken the common criteria such as the number of employees, paid up capital, sectorial category, market share and the management entity.

Micro enterprises aim to create large-scale employment in the economy, separate from the formal sector. And they can achieve this target with very limited finances and investment. Another objective is to spread industries and trade in an economically backward area. This helps in the development of the overall economy.

The small business sector is recognized as an integral component of economic development and a crucial element in the effort to lift countries out of poverty (Wolfenson, 2001). Small-Scale businesses are driving force for economic growth, job creation, and poverty reduction in developing countries. Further, small scale business has been recognized as a feeder service to large-scale industries (Fabayo, 2009). In light of this, Micro and Small Enterprise Development Program in Ethiopia has been given due attention by government since 2004/2005. Until 2004/2005, the national strategy was implemented by Federal MSEs Development Agency organized only at national level. Because of this, it was very difficult to make the strategy practical specially in delivering business development service for MSE operators. Thus, by considering the critical role of the sector and the challenges faced by MSE operators since 2004/2005 the government of Ethiopia decided to establish MSEs coordinating body at the regional level.

2.1.2 Overview of MSE Sector in Ethiopia

According to FeMSEDA, (2011) definition of MSE in Ethiopia varies from above definitions. In the past the definition of Micro and Small Enterprises was based on paid up capital only. An enterprise is categorized as micro if it's paid up capital is less than or equal to Birr 20,000. Similarly, an enterprise is considered small when its paid up capital is less than or equal to Birr 500,000.However, this does not provide information on the size of jobs or number of employees in the MSE. It also did not tell the size of the total asset for the MSE and did not differentiate between manufacturing (industry) and services. Current definition considers human capital and asset as the main measures of micro and small enterprise to addresses the limitations of the old definition. Micro enterprises in industrial sector has paid up capital of below 100,000 and 5 human power. In the service sector micro enterprises have 5 human capital but asset is below 50,000 birr. Small enterprises have human power from 6-30 but the capital is 1.5 million and 500,000 birr in industry and service sectors respectively.

The Ethiopian government has formulated a National MSE Development and Promotion strategy in 1997, which enlightens a systematic approach to alleviate the problems and promote the growth of MSEs. The overall objective of the strategy is to create an enabling environment for MSEs, with specific objectives to facilitate economic growth; bring equitable development; create long-term jobs; strengthen cooperation between MSEs; provide the basis for medium and large-scale enterprises; promote export; balance preferential treatment between MSEs & bigger enterprises. The strategy targets support measures and beneficiaries such as small manufacturers in food, textiles, leather, clothing metal works, and crafts; self-employment (focus on school leavers, disabled and unemployed youth); start-up and expanding firms (focus on women owned); small enterprises in nomadic and disaster areas; agro-business and small scale farming and fishing; small builders/contractors; small exporters; as well as small-scale tourism operators (FDRE MoTI, 1997).

On the other hand, the Ethiopian MSE Development Agency has developed different strategic manuals and policy directives concerning capacity building, financial management, service cluster, level of transition of MSES, scaling up best practices, etc. In the year 2011/2012 for the effective implementation of MSE followed by dissemination of documents and massive training. According to research carried out by Commission on Legal Empowerment of the Poor in 2006 the private sector in Ethiopian is characterized by high domination of micro and small enterprises of low income groups accounting for the bulk of nonagricultural economic activities and particularly, concentrated in the production and consumption of textiles, food and beverage processing. Moreover, the report of the research has shown that most MSEs are characterized by ease of entry and constitute the bulk of the population at the same time most of them are located in rural areas (Commission on Legal Empowerment of the Poor, 2006).

2.1.3 Financial Management

Financial management is the management of the finances of a business in order to achieve the financial objectives of the business. McMahon and Davies (1994) define financial management as the function concerned with raising the funds needed to finance the enterprise's assets and activities, the allocation of these scarce funds between competing uses, and ensuring that the funds are used effectively and efficiently in achieving the enterprise's goals. According to Arm strong (1986), financial management is concerned with planning, budgeting and control techniques. Oduware (2011) adds that financial management entails planning for the future of a business enterprise. Brinckmann et al (20II) define financial management as including managerial activities that concern the acquisition of financial resources and the assurance of their effective and efficient use to ensure a positive cash flow. Armstrong (200 I) posits that financial management is further concerned with the activities within a business that contribute to profit maximization. According to Firer et al (2004), the goal of financial management is to maximize the wealth of the firm's owners. This notion is supported by Keown et al (2002), who argue that financial management contributes to creating and maintaining the economic value of a business.

Financial management can occupy the major part of a financial manager's time and attention (Gitman, 2003) and many business failures have been attributed to the inability of financial managers to plan and control properly the current assets and the current liabilities of their respective firms (Dodge and Robbins, 1992, Ooghe, 1998).

Financial management is composed of five constructs; working capital management which is also subdivided into cash management, receivables management and inventory management. Other constructs under financial management include; investment, financing, accounting information systems and financial reporting and analysis. Ross et al (1999) indicated three kinds of decisions the financial manager of a firm must make in business; these include the financing decision, and decisions involving short-term finance and concerned with the net working capital, investment and financial reporting. Similarly, Ang (1992) also indicated three main financial decisions including the investment decisions, financing decisions and dividend decisions. The strong points of financial management practices in the SME sector have long attracted the attention of researchers. Depending on different objectives, researchers emphasize different aspects of financial management practices.

Armstrong (2001) identified five principles of financial management: financial planning, financial accounting, financial analysis, management accounting and capital budgeting. Harif et al (2010) include working capital as a sixth financial management practice. In the same way that financial management practices are important to large and multinational enterprises, they are also important for MSEs (Fatoki, 2012). Among these practices of financial management, financial management in MSE focuses on financial planning, financial accounting and financial analysis. Therefore, this study focuses on financial planning and control, financial accounting and financial analysis.

According to Armstrong (2001) financial planning predicts the overall financial performance of a business and alerts management to the funds required, when they will be required and how much will be needed. The primary financial planning activities are: income forecasting, cash flow forecasting, determining financial resource requirements, and profit and dividend planning. The basic purpose of the financial planning is to make sure that adequate funds are raised at the minimum cost and that they are used wisely. In Micro and small Enterprises, profit is not the motive and financial plans have to deal with raising and deploying resources. Financial planning pertains only to the function of finance and includes the determination of the firm's financial objectives, formulating and promulgating financial policies and developing financial procedures (Walker and Boughn, 2014).

According to Weygandtetal (2000), financial accounting is the process of identifying, recording and communicating the economic events of a business in order to communicate this information to interested parties. Armstrong (2005) asserts that financial accounting records the financial transactions that have taken place in a business. The Information recorded is then communicated through accounting reports in the form of financial statements: financial position, profit and loss statement and a cash flow statement, deemed to be the primary data sources for financial analysis.

Financial analysis is the process of evaluating the performance of a business and other projects using tools such as ratio analysis, payback period, net present value and internal rate of return. Investment in projects requires risk analysis and sensitivity analysis. Typical tools such as cost-benefit analysis, cost-effectiveness, sales mix analysis and cost-volume analysis can be useful. Financial analysis includes ratios such as current ratio, quick ratio, return on sales, debt ratio, inventory turnover and return on equity (Nguyen, 2001).

2.1.4 Financial Reporting

Three financial reports commonly used in business are the balance sheet, income statement, and the statement of cash flows. They report the financial position of the Micro and small Enterprises, its performance over a given time period, and its ability to meet cash obligations. They are the basis for planning future operations. Each report contains different, but interrelated information that together give a complete picture of the financial operations of the Micro and small Enterprises. Managers, bookkeepers and board members should be able to understand and interpret these reports so they can make informed business decisions about the future of the Micro and small Enterprises. Financial Reports of Micro and small Enterprises Financial reports are used to evaluate past operations and are the basis for management and operating decisions on future projects. The board of directors uses the reports for feedback on the financial status of the Micro and small Enterprises to evaluate progress and to make informed decisions about future operations. Managers need accurate and timely information to run the day-to-day operations. Creditors examine the financial reports when considering loans to the Micro and small Enterprises and accountants need accurate records to prepare tax documents. Accurate and current records are also important to members of the Micro and small Enterprises Records should show the net profit, the level of each member's patronage account and the amount of equity members hold in the Micro and small Enterprises. This facilitates distribution of patronage refunds and ensures that the Micro and small Enterprises is operating according to Micro and small Enterprises principles.

2.2 Empirical Reviews

Prominent among these are limited financial management and entrepreneurial skill of the owners/managers, marketing problems due to quality of the products and poor market research, lack of adequate infrastructure and modern technology and lack of adequate access to credit. Small scale enterprises produce largely for the domestic market although there are few of their products for export markets. Those producing for export are unable to identify the specific buyers in the export trade. In the early years 1930's Senator Macmillan said that SMEs' growth showed that they were distressed with finance gap. Much pragmatic studies revealed that SME were faced with not only equity gap but also debt gap.

Aryeetey et.al (2016) indicated that most of the small business enterprises' operators have little formal education in managing their business. The background of the owners/managers, therefore, places a limitation on their managerial capabilities. This problem has affected the scope of their operation and therefore they are not able to take full Advantage of emerging opportunities (Steel, 2016). In certain situations, managerial incompetence has led to operational inefficiencies resulting in poor performance (Pappoe, 2012).

Small scale enterprises produce largely for the domestic market although there are few of their products for export markets Those producing for export are unable to identify the specific buyers in the export trade. This creates the problem of unfair competition from outside producers as well as dumping of goods from the developed countries (Aboagye et.al 2008).

With regard to the use of modern technology, the operators of the SMEs use basic locally developed technology and machinery which restrict incentives to innovation. These are limited in capacity and efficiency. The SMEs thus, experience much wastage of materials as well as frequent machine breakdown (Anderson, 2008).Technical expertise in the SMEs is also limited. Some of the small firms are not aware of the availability of modern technologies or do not have the capability to develop and apply them. Moreover, where there is such awareness, luck of funds restricts their acquisition.(Olu,2009).

Sosyal (2013) identified importance of financial management knowledge in small and medium enterprises managing by women. In this research, following important results have been found about Turkish women entrepreneurs; they mostly manage their business (89%); however, they have support from another one (77.7%).They do not face with problems arising from sexuality in women customer sectors. Most of women entrepreneurs do not know the meaning of business risk, financial analysis, financial planning, investment decision and they mostly stated that they needed education on financial management. All of the responders said they do not have information about the financial issues in the new TTC which will be affected after 2012. The results of the international studies and this study reveal that women entrepreneurs need “continuous financial management education” for well-managed SMEs. Moreover, following recommendations should be taken seriously by related institutions about women entrepreneurship and SME management. Continuous business management education including financial management and trade code should be provided to women entrepreneurs by Trade Chambers and educational institutions. Women entrepreneurs should consult to financial advisors to decide for investing, budgeting, funding and the other financial issues instead of consulting families. Women entrepreneurs should organize network on business issues to support each other on financial issues. Women related institutions like universities, trade chambers and nongovernmental organizations should organize projects and education events for women entrepreneurs to keep them accurate. “Continuous management education for women managing SMEs” is one of the way out to increase women contribution in economy. Appropriate financial decision needs advanced financial knowledge as investment decision starts with the identification of investment opportunities, often referred to as capital investment projects.

The study made by John Kwaning Mbroh (2017) which is entitled "*Financial Management Practices by Small and Micro Enterprise Owners in Ghana*" results have shown how haphazard the SMEOs have conceived and practiced the crucial function of financial management. Crucial to being efficient in cost-benefit strategies is the application of the relevant financial management skills and knowhow. It is concluded that majority (81.2%) of the respondents must have the necessary financial management knowhow (being in their long-term business management stage) with over 3 years of experience. Also, male owners (63%) are more in the small businesses and their female counterparts dominate (52%) the micro businesses.

Mbroh and Assah (2015) found more females and males in the micro and small business segments respectively in Ghana. Overall, majority (68%) of the respondents have had reasonable academic backgrounds. However, a significant proportion (13%) had not had any form of education. The results are conclusive that the SMEOs lacked basic working knowledge in financial management, with an overall majority (39%) of the respondents neither having the reasonable (or relevant) level education nor the appropriate training. Again, 31% of them have never had any business-related education. Less than a third (30%) had either business education or relevant financial management training of some sort. In his study the researcher conclude that the Government of Ghana, on its part has put in place funding some interventions and established some departments and agencies in addition to licenses issued to several of NGOs to operate in this sector of the Ghanaian economy, with the objective, among others, of building or enhancing the necessary business (financial) management capacities. However, it appears these interventions and agencies are either inadequate or not making the necessary impact for now. Again, even though external financial management challenges like: unreliably poor general economic conditions; unreliable training promises by certain agencies and NGOs; business-unfriendly loans' terms and conditions; and relatively high cost of borrowing were assigned; internally however, majority (24%) of respondents lacked the basic working knowledge in financial management and this crucial challenge was cited to have multiplier effects on both the number and types of other (associated) challenges

In Ethiopia almost all studies taken on micro and small enterprises are mostly focused on factors affect the performance of micro enterprises, the tax effect on micro enterprises, the importance of micro and small enterprises and the challenges of micro enterprises in Ethiopia. Studies From those Eshetu and Zeleke (2008) conducted a longitudinal study to assess the impact of influential factors that affect the long-term survival and viability of small 25 enterprises by using a random sample of 500 MSMEs from 5 major cities in Ethiopia. According to this research, that lasted from 1996-2001, the factors that affect the long term survival of MSMEs in Ethiopia are found to be adequacy of finance, level of education, level of managerial skills, level of technical skills, and ability to convert part of their profit to investment. This is so because the findings of the study revealed that businesses that failed, during the study period were characterized by inadequate finance (61%), low level of education (55%), poor managerial skills (54%), shortage of technical skills (49%), and inability to convert part of their profit to investment (46%).

Paul and Rahel (2010) found out that the studied enterprises registered 25% increment in the number of total employment they created since their establishment with an average annual employment rate of 11.72%. With regard to the sources of initial capital of the studied enterprises, the study indicated that, the main ones were loan from MFI (66.7%), personal savings/Iqub (17.5%), and loan from family/friends (17.1%). Moreover, the concrete problems that the targeted MSEs faced at their startup were lack of capital (52.8%), skills problem (17.9%) and lack of working space (17.1%). Moreover, Daniel (2007:49), identified that lack of raw material, stiff competition and shortage of working capital. Mainly relying on a sample survey of 557 operators and 200 MSEs chosen from four 26major cities of Ethiopia namely Adama, Hawassa, Bahirdar and Mekelle, Tegegne and Meheret's research (2010:40-72) was conducted with the intention of assessing the contribution of the MSE strategy to poverty reduction, job creation and business development. The raised causes for this gloomy prospect of business were not growing (33%), lack of finance (13%), lack of market (11%), and lack of working space (4%).

The major constraints identified by various studies on MSEs in Ethiopia are associated with market and finance problems. The causes of market-related problems of MSEs engaged in metal and wood work are shortage or absence of marketing skills, poor quality of products, absence of marketing research, shortage of market information, shortage of selling places, and absence of sub-contracting (FMSEDA, 2016). The product line of MSE activities in Ethiopia is relatively similar (Assegedech, 2014). Accordingly she states that: Lack of product diversity, however, is prevalent and as a result similar products are over-crowding the market. Some micro enterprises shift from one product to another, and in doing so, capture better market opportunities. Nevertheless, as soon as the market has established itself, a multitude of further micro enterprises start off in the same business and this causes the selling price to fall immediately.

In reality, literature on MSEs in Ethiopia is scanty and most of the available studies were not conducted in line with financial management and reporting practice aspects of micro enterprises. However, This study places emphasis on financial management and reporting practices in micro and small enterprises considering finance acquisition (sources), budgeting, business operations, investments, performance measurements and reporting by the selected enterprises in Lideta sub-city.

CHAPTER THREE
METHODOLOGY OF THE STUDY

3.1 Introduction

This chapter presents about research design and methodology followed by the study. Specifically, the chapter presents about the design of the research, approach of the study, the sampling design, sampling technique, data sources, tools used for data collection and method of data analysis.

3.2 Research Design

According to Burns & Grove (2001) designing a research helps to plan and implement the study that enables easily to obtain intended results. Thus, appropriate research design increase the chances of obtaining information that could be associated with the real situation. This study was conducted to identify financial management and reporting practices of micro and small enterprises. Consequently, ultimately this study describes the practices of finance management and reporting. Therefore, descriptive design is applied based on using descriptive statistics. Descriptive survey also enables to obtain the current information. According to Paul et al (2009) descriptive design describe the data and characteristic about what was been studied. It was also use in fact finding studies and helps to formulate certain principles and give solutions to the problems. In addition to this survey design is a research method that provides a quantitative or numeric description of trends, attitudes, or opinions of participants with the intent of generalizing from a sample to a population.

3.3 Research Approach

Creswell (2007) states that there are three commonly implemented approaches to conduct a research. These include quantitative, qualitative and mixed, where one of them is not better than the others and all of this depends on how the researcher want to do a study.

The quantitative data was collected by using structured questionnaire. To supportive information on the finding through questionnaire the study has followed qualitative approach and collected detailed data through interview. To reach at the aforementioned objectives, a mixed approach was followed by using questionnaire and interview.

3.4 Sampling Design

3.4.1 Target Population

Hair et al., (2010) states target population as a specified group of people or object for which questions can be asked or observed to collect required data structures and information. This study was conducted with an objective of identifying the financial management and reporting practices in Micro and Small Enterprises in Lideta Subcity. Based on this objective the study targets the enterprise. According to Addis Ababa Micro and Small Enterprises Development Bureau (2019), there are 1,475 Micro and Small enterprises in the subcity. Therefore, this study was conducted by targeting MSE in the subcity.

After identifying the MSE in the subcity, the study has targeted the respondents for the study. The financial management and reporting is mainly duties of finance managers in the enterprises. The preliminary survey shows the operation and management of the finance is almost totally conducted by a single person especially by the finance manager. Therefore, the study targets one person in an enterprise. Therefore, the number of target population is 1,475 finance managers of the enterprises.

3.4.2 Sample Size

Alreck & Settle (2005) suggested that there is no single and precise way to determine sample size; hence there are a number of inadequacy for deciding on sample size. Accordingly, the choice of sample size is made after considering statistical precision, practical issues and availability of resources. Malhortra& Peterson (2006) and Zikmund (2003) stated that, the larger the sampling size of a research is more accurate than the small sample size. Based on its simplicity, this study has adopted sample size determination method developed by Carvalho (1984).

Table 3.1 Sample Size Determination

Population size	**Sample size**		
	Low	Medium	High
51-90	5	13	20
91-150	8	20	32
151-280	13	32	50
281-500	20	50	80
501-1200	32	80	125
1201-3200	50	125	200
3201-10,000	80	200	315
10,001-35,000	125	315	500
35,001-150,000	200	500	800

Source: Carvalho (1984)

As mentioned in the previous section, the target population of the study is 1,475 finance managers in the enterprises that fall in the range of population 1,201 – 3,200. To increase the data accuracy and minimize non-response rate, the study has used high sample size in the range. Consequently, the sample size used for the study is 200 respondents.

3.4.3 Sampling Technique

Purposively, the study has used the finance managers in the enterprises who are responsible for managing the finance of the organizations and handling the reports. The samples of 200 respondents were selected from the population of 1,475 managers. The study has randomly selected the enterprises for the study based on the simple random sampling strategy from the list of enterprises in Lideta Subcity. Therefore, this study was conducted by implementing purposive and simple random sampling strategies.

3.5 Data Type and Sources

This study was conducted by using primary data through questionnaire and interview. The study data was collected from finance managers of the enterprises by using questionnaire and interview. The study has used questionnaire as a quantitative data collection instrument that helps to cover larger target groups than the interview, given the quality and chance of no response. Further, the study was supported by theoretical and empirical literatures.

3.6 Survey Instrument

The questionnaire has three sections; background of the respondents, profile of the enterprise and practices of financial management and reporting. The questionnaires were prepared using close-ended method questions; yes/no, multiple choices and open ended questions. The questionnaires were designed in English.

3.7 Data Collection Procedures

The respondents for the study were selected randomly by using list of enterprises in the subcity as sampling frame. Questionnaires were distributed to randomly selected enterprises physically at office hours. Five enterprises were randomly selected from the sampled enterprises and the interview was conducted at office of the managers.

3.8 Methods of Data Analysis

Analysis of data is a process of editing, cleaning, transforming, and modeling data with the goal of highlighting useful information, suggestion, conclusions, and supporting decision making (Adèr, 2008). Data from the field were edited and coded appropriately to make meaning out of them. Editing was done to correct errors, check for non-responses, accuracy and corrects answers. Coding was done to facilitate data entering and a comprehensive analysis.

The data collected through questionnaire was analyzed using quantitative data analysis techniques. Moreover, the data collected through interview was presented qualitatively. Quantitative data gathered through semi – structured questionnaire were analyzed through the use of both descriptive statistics. Descriptive analysis was used to present the data in a summary format by tabulations (frequency and percentages) and measure of central tendency (mean and standard deviation). Specifically Percentages was used to compare the significance of the response of respondents. Moreover, charts were used to describe the general characteristics of enterprises.

Besides, the interview questions were analyzed using descriptive narrations through concurrent triangulation strategy.

3.9 Ethical Consideration

Before the data collection, permission from the companies and respondents was requested. During the distribution of the questionnaire, respondents were informed about the purpose and the benefit of the study along with their full right to refuse or accept the participation. The respondents were told their response would be kept confidential and their identity shall not be exposed. Every person involved in the study was entitled to the right of privacy and dignity of treatment, and no personal harm were caused to subjects in the research. Information obtained is held in strict confidentiality by the researcher. All assistance, collaboration of others and sources from which information was drawn were acknowledged.

CHAPTER FOUR
DATA PRESENTATION AND ANALAYSIS

4.1 Introduction

In this chapter, the result of data analysis and its interpretation is presented. This study was conducted by following descriptive design that the data is analyzed by using descriptive statistics such as frequency, percentage, mean and standard deviations. The data analysis follows the phases discussed in chapter three (under research design and analysis methods). The first phase involves editing, coding and the tabulation of data. This assisted in identifying any anomalies in the responses and the assignment of numerical values to the responses in order to continue with the analysis. The data was then checked for possible erroneous entries and corrections made appropriately.

Based on the sampling strategy followed, the study has distributed 190 questionnaires to the respondents who are at the position of financial management. The study has collected 138 questionnaires that are properly filled and usable for the study. Thus this study was conducted with response rate of 71.6%. In addition, 10 respondents were selected for interview and all respondents were contracted.

4.2. General Information about Respondents

General information about the respondents is presented in Table 4.1 below. The demographic information includes age, sex and education level.

Age of the respondents is presented in 4 categories; below 26, 26-35, 36-45 and above 45 years. The largest group (47.1%) of respondents at age category of ’26-35’ years and followed by number of respondents below 26 years that include 32% of the respondents. but the smallest group of respondents are at age category above 45 years. the survey about the age of the respondents suggests that the role of financial management in the enterprises is undertaken by younger employees.

Table 4. 1 Demographic Information about Respondents

Variable	Category	Count	Percent
Age	Below 26 Years	32	23.5
	26-35 Years	64	47.1
	36 - 45 Years	24	17.6
	Above 45 Years	16	11.8
Sex	Male	76	55.9
	Females	60	44.1
Education	Primary Schools	9	6.6
	Secondary Schools	47	34.6
	College and Above	80	58.8

Source: Own Survey, 2020

Regarding the sex of the respondents; about 56% of the respondents were male and 44% of the respondents were females. In this study it was found out that in the sample of the study there were dominance of males in the leadership of the micro and small scale enterprises.

Educational level of the respondents in this study were, primary education 6.6%, secondary education 34.6% and college and above 58.8%. Indicates that the major members of micro and small scale enterprises in this study are educated enough to understand, to run and develop their enterprise in more growing and developing business through developing and preparing business plans that can lead to business growth like financial management, keeping proper books of records, taking advocacy issues to support their businesses and also look for more training programs to improve their businesses which is normally run by development organizations. Further, finding about the education level of the respondents suggest that managing finance is supported by theoretical education provided by higher education as only 58.8% of the respondents might take accounting education.

4.3 Description about the Enterprises

Description about the enterprises include number of members, type of business where the enterprises engaged, form of ownership of the enterprises, size of the enterprises as indicated by number of employees, and source of initial capital.

4.3.1 Type of business

It is about form of business that the enterprises enterprise involved. The study has identified four types of the business types. The summary of the business type is presented in figure 4.1 below by using bar chart and descriptive statistics such as frequency and percentage.

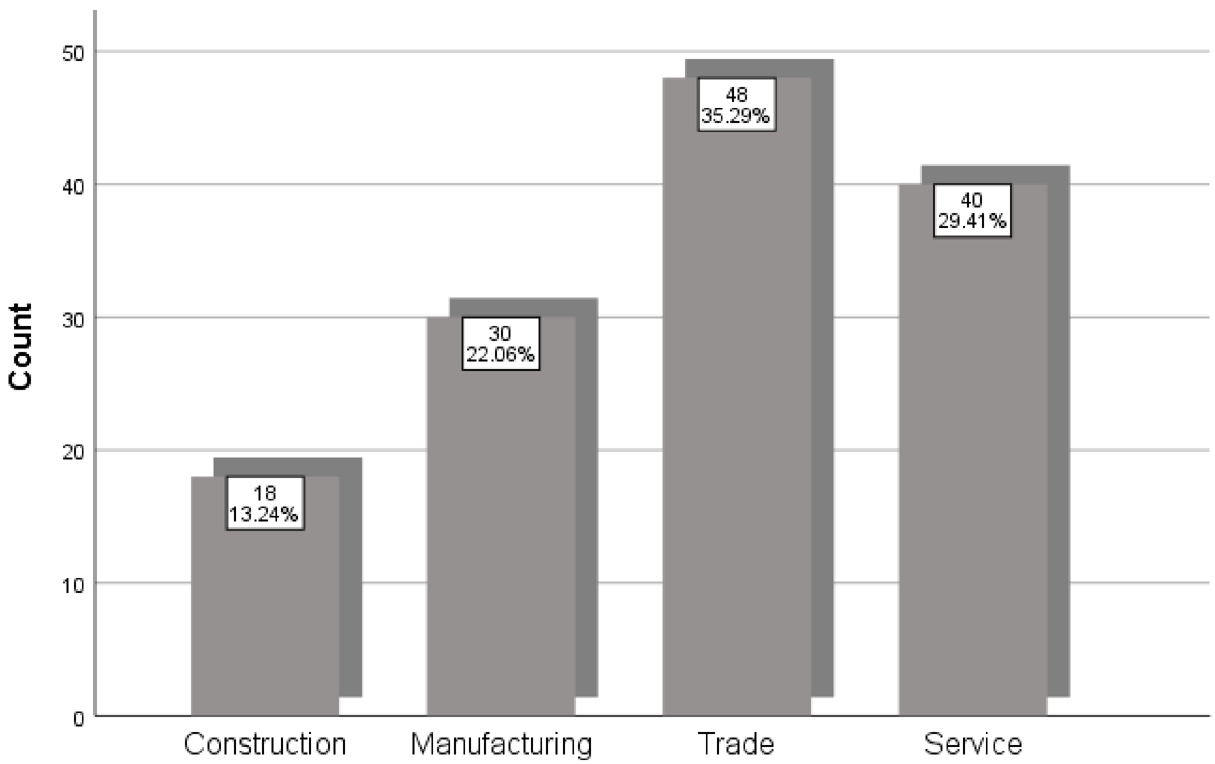

Figure 4.1: Type of business of the enterprises (*Source survey, 2020)*

As shown in the above table, the sample micro and small scale enterprises were operating in four sectors of the economy. Most of them are engaged in trade (35.3%) This is mainly due to small capital required to start such business and because the types and numbers of business transactions to trading businesses is relatively less complex than businesses in the other sectors, followed by service sector (25.7%) the manufacturing (22.1%) and construction (13.2%)these is due to of manufacturing and construction sectors which require much capital and expertise. This division of MSEs by sector type was believed to be helpful to study to understand and asses the financial management and reporting practice of micro and small enterprises found in each sector.

4.3.2 Type of Ownership

Another description about the enterprises is form of ownership. The forms of ownership of the enterprises is presented in Figure 4.2 below in pie chart. To summarize the data, frequency and percentage were used.

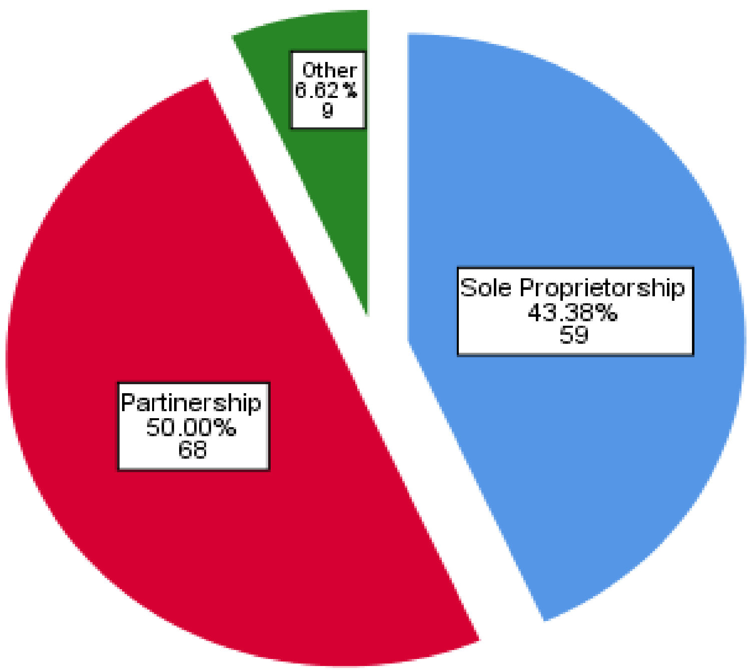

Figure 4.2 Type of ownership of the enterprises (source: Own survey, 2020)

The form of ownership has significant impact on the financial management and reporting practices of micro and small enterprises. As shown in the above in Figure 4.2, micro and small enterprises involved in this study, the major enterprises form of ownership is partnership (50%) followed by sole proprietor ship (43.38) and other forms (6.62%).

Enterprises hold by sole proprietor were most of the time run by only by sole proprietors including financial decisions and reporting procedures as result there will be luck of reliability in the financial management and reporting practice of the enterprises, in the other side micro and small enterprises were has partnership form of ownership which includes minimum of two and maximum of five members in ownership statues in the enterprise, this form of ownership is better to make financial management and reporting practice about their business affaires necessary to mutual understanding and decision making including budgeting and investment issues with in enterprise. Other forms indicated by the enterprises are venture relationship between family and relatives and distributing wholesaler's merchandise which includes insignificant financial management and reporting practices.

4.3.3 Size of Enterprise

The third description about the enterprises is size of enterprise. This description is intended as financial management varies based on size of company. As an indicator of size of company, the study has used number of employees and the survey result is presented in table 4.2 below by using summary statistics such as frequency and percentage.

Table 4. 2 Size of Enterprises

Number of Employees	Frequency	Percent	Cumulative Percent
2 - 5	84	61.8	61.8
6 - 10	28	20.6	82.4
11 - 20	24	17.6	100.0
Total	136	100.0	

Source: Own Survey, 2020

Most of micro and mall enterprises in this study hold two up to five employees including the owner (62%) followed by those who has six up to ten (21%) and the rest were holds more than ten employees. the cumulative result indicates, 82.4% of the enterprises have 2-10 employees. this suggests the enterprises are at small scale level.

This might be linked with the finding that majority of them were entities engaged in businesses that do not require a large number of employees to function. On the other hand, when we trace the definition for SMEs set by the development bank of Ethiopia in 2017, based on the number of employees 56.7% (6 to 30 employees) were small businesses and 6.0% (30 to 100 employees) were medium businesses.

4.3.4 Source of Initial Capital

Source of initial capital of the enterprises is presented in Table 4.3 below. The survey result shows, four sources were observed in the enterprises.

Table 4. 3 Source of initial capital

Sources of Capital	Frequency	Percent	Cumulative Percent
Personal Saving	40	29.4	29.4
Micro finances	62	45.6	75.0
Banks	6	4.4	79.4
Friends/Relatives	28	20.6	100.0
Total	**136**	**100.0**	

Source: Own Survey, 2020

As shown in Table 4.3 above, the initial sources of finance for the MSEs in the study. A large Proportion (45.51%) of respondents' started their business by borrowing money from microfinance institutions. This was followed by money obtained from own personal Saving (29.4%), loan from relatives (family and friends) (20.6%). And (4.4 %) of the respondents got money from bank loans. From this we can observe most of micro and small scale enterprises generate their initial capital from micro finance institutions and from their own personal saving and family, where the study revealed that most of the SMEs use internally generated funds. The access to bank loans by SMEs is low due to factors such as lack of collateral security, high costs associated with interest rates, fear of the bureaucratic tendencies that must be followed by the banks in order to access bank loans and poor record keeping.

4.4. Practices of Financial Management

The practices of financial management is summarized in Table 4.4 below based on close ended questions and triangulated by interview responses.

Table 4. 4 Financial Management Practices

	Yes		NO	
	Frequency	Percent	Frequency	Percent
Enterprise have financial policy/procedure manual	62	45.6	74	54.4
Enterprise have finance manager	38	27.9	98	72.1
Enterprise took loan	62	45.6	74	54.4
Enterprise prepare financial plan	116	85.3	20	14.7

Source: Own Survey, 2020

4.4.1 Financial Policy and Procedure

As depicted in Table 4.4 above, from micro and small scale enterprise involved in this study, 45.6% have their own financial policy and procedure that serve as guideline in order to run their business, whereas the rest (54.4%) has do not have any clear and planned financial management system. As a result most of micro and small scale enterprises run their business without clear and defined financial management policy and procedure, which results problem in future business growth of micro and small enterprises.

Sound financial management is essential to the success of a business. Successfully managing financial resources is important in new as well as expanding businesses, so time should be taken to develop and implement financial plans that will ensure the success of small firms. Financial policy and procedures is one of the necessary tools in order to make financial decisions including investment decisions and implementing financial operations of the enterprises. The main purpose of financial management and reporting practices is to operate the business in efficient and effective way through preparing budget and financial information to stake holders that improves the ability of making reliable information based decision in operational and business relationship aspect of the enterprise. It is good practice for an organization to produce a detailed set of financial procedures. Financial procedures are a set of instructions that any stakeholder, including new members of the committee or staff, can use to find out exactly: what tasks need to be done; who will do these tasks; and who will ensure the tasks are done properly.

It is important that the agreed financial procedures are written down so that there is clarity about what is required and that the management committee ensures that staff and committee members are aware from the outset of what is expected of them.

Financial management policy to be a sustainable organization, it is not enough to only monitor and evaluate your projects, strategic processes, personnel and knowledge. It is essential to also monitor and evaluate your operational and organizational budgets. Having a continuous stream of income and making the most of it is an essential element of the of the stability of your organization's work. In doing so, cost efficiency and effectiveness are important to keep in mind along with the allocation of specific financial resources to monitoring, evaluation and learning activities

In order to have an effective financial management an organization needs to establish a suitable internal environment. Such environment depends to a large extent on the size of the organization. In all situations it is essential to assign concrete responsibilities to positions/people related to the financial management at the organizational and the operational level. Most of Micro and small scale enterprises in this study do not have clear and precise financial procedures and planes.

4.4.2 Existence of Finance Managers

Financial managers are responsible for the financial health of an organization. They produce financial reports, direct investment activities, and develop strategies and plans for the long-term financial goals of their organization. Responsibility of financial manager responsibilities include financial planning, investing (spending money), and financing (raising money). Maximizing the value of the firm is the main goal of the financial manager, whose decisions often have long-term effects. Financial management the art and science of managing a firm's money so that it can meet its goals is not just the responsibility of the finance department. All business decisions have financial consequences. Managers in all departments must work closely with financial personnel.

It is important to have financial manager in order to perform duties and responsibilities described in the above, From micro and small scale enterprises involved in this study about 72.05% of them do not have financial manager which has an identified roll only in financial management of the enterprise and most of respondents who said they do not have an identified financial manager revealed that the financial management activates of enterprise have been takes place ether by owner or someone who have other roll with in the enterprise such as an accountant ,the rest have an identified personnel who took financial management role.

4.4.3 Liability Management

In finance, a loan is the lending of money by one or more individuals, organizations, or other entities to other individuals, organizations etc. The recipient incurs a debt and is usually liable to pay interest on that debt until it is repaid as well as to repay the principal amount borrowed.

As seen in the above chart, 54% of respondents in these study have said they do not took loan from other external third party due to lack of sufficient loan finance access and also they asked for collateral and excess amount of interest repayment from financial institution, which is not easy to micro and small scale enterprises with luck of sufficient collateral and financial strength.

From 46% of respondents most of them described individuals and micro financial institutions as their main source of loan in order to fulfill financial need of their enterprise and they also said this is due to low level of interest repayment expense on the loan and easy processes to have loan fund from such source.

4.4.4 Existence of Financial Plan

Financial planning is the task of determining how a business will afford to achieve its strategic goals and objectives. The Financial Plan describes each of the activities, resources, equipment and materials that are needed to achieve these objectives, as well as the timeframes involved.

Comprehensive financial plan helps you meet your current financial needs and prepare for financial stability in the future. The work involved in creating a financial plan will guide the investment plan and eventually the retirement plan. It also influences tax and estate planning.

Preservation of capital is a conservative investment strategy where the primary goal is to preserve capital and prevent loss in a portfolio. This strategy necessitates investment in the safest short-term instruments, such as Treasury bills and certificates of deposit

Financial management is the activity of management which is concerned with the planning, procuring and controlling of the firm's financial resources. Organization's future will depend upon the effective utilization of funds like growth, expanding the company, long run of the company.

Financial control may be construed as the analysis of a company's actual results, approached from different perspectives at different times, compared to its short, medium and long-term objectives and business plans.

Most of MSEs’ in this study do not have prepare financial plan and those who prepare financial plan their main purpose is efficient use of financial resource and for controlling purpose.

The study has assessed inclusion of capital budget in financial plan of the enterprises. Capital budgeting is the process that a business uses to determine which proposed fixed asset purchases it should accept, and which should be declined. This process is used to create a quantitative view of each proposed fixed asset investment, thereby giving a rational basis for making a judgment.

The importance of capital budgeting is the amount of cash involved in a fixed asset investment may be so large that it could lead to the bankruptcy of a firm if the investment fails. Consequently, capital budgeting is a mandatory activity for larger fixed asset proposals. This is less of an issue for smaller investments; in these latter cases, it is better to streamline the capital budgeting process substantially, so that the focus is more on getting the investments made as expeditiously as possible; by doing so, the operations of profit centers are not hindered by the analysis of their fixed asset proposals.

In an ordinary sense, working capital denotes the amount of funds needed for meeting day-to-day operations of a concern. ... Hence it deals with both, assets and liabilities—in the sense of managing working capital it is the excess of current assets over current liabilities. The funds invested in current assets are termed as working capital.

It is the fund that is needed to run the day-to-day operations. It circulates in the business like the blood circulates in a living body. Generally, working capital refers to the current assets of a company that are changed from one form to another in the ordinary course of business, i.e. from cash to inventory, inventory to work in progress (WIP), WIP to finished goods, finished goods to receivables and from receivables to cash.

4.5 Reporting and Accounting Practices

The accounting practices are about having formal accounting system, recording transactions, existence of accounting department, using computer software and existence of bookkeeping and financial control system. The survey result about these practices is presented in Table 4.5 below.

Table 4. 5 Reporting & Accounting practice

	Yes		NO	
	Frequency	Percent	Frequency	Percent
The enterprise has a formal accounting system	18	13.2	118	86.8
The accountant in charge of recording all transactions	22	16.2	114	83.8
The accounting department is operating efficiently	8	5.9	128	94.1
The enterprise uses computer assisted software in recording transactions	28	20.6	108	79.4
The enterprise have a record keeping and financial control system	39	28.9	96	71.1

Source: Own Survey, 2020

The study established that majority (86.8%) of the businesses do not have a formal accounting system and lack an operating accounting department.83.8% of the businesses do not have an accountant in charge of recording all transactions. Many of the businesses (79.4%) do not use computer assisted software in recording transactions.

The study revealed that most of the businesses do not have a formal accounting system, lack an operating accounting department, do not have an accountant in charge of recording all transactions and do not use computer assisted software in recording transactions. This is probably due to the fact that most of the SMEs are owned by sole traders who end up doing all the work themselves.

The findings further revealed that most of the SMEs accounting systems are informal. Some of the SMEs may fear to maintain formal systems because they come with maintenance costs. The findings showed that the accounts departments are not functional and not efficiently operated which hinders financial reporting. Few of the SMEs employ accountants and put them in charge of recording transactions due to limited resources to enable SMES afford the services of professional accountants. Failure to use computers and computer assisted software among SMEs makes timely financial reporting as well as decision making very difficult. The study findings are in agreement with the previous studies Peacock (1988) who revealed that few of the SMEs in South Africa were fully utilizing accounting information systems and that contributed to their failure. KAM (2009) argued that adoption of Technology advancement in business financial management enhances organization performance.

As can be observed from Table 4.4, only one-third of the respondents keep regular accounting record. About 70 percent of the respondents either do not totally keep accounting record or keep the record irregularly. For those that are keeping accounting record, owners or managers are responsible in the majority of the cases. The use of qualified internal or external accountant is very much limited. This implies that MSEs do not realize the inaccuracy of information based on their limited knowledge will affect the decision making process and will jeopardize their companies' performance.

This indicates that the quality of accounting information produced is quite low because owner/managers may have insufficient accounting knowledge. As opposed to this finding, almost three-quarters of Austrian MSEs keep regular accounting record and outsource the preparation of their financial statements to outside experts. As can be seen from the figure 1 above, perception that the business is too small to qualify for accounting record is the main reason for not keeping book of accounts. Even those that are keeping accounting record, owners or managers use instinctive method than the formal accounting procedures we are teaching at college or university. This is typical management behavior of even in larger enterprises conceivably due to inadequate awareness and skill of most of our business people. Other reasons for not keeping accounting record include lack of qualified accountants at appropriate pay rate and fear of high taxation as a result of honestly keeping accounting record. Another factor that discourage from keeping proper record may be; per income tax proclamation 286/2002, MSEs whose annual turnover is less than Birr 500,000 ($20,000) are not legally required to keep book of accounts for tax purpose. Therefore, record keeping by MSEs is based on the willingness of the owners themselves.

Table 4. 6 Types of Report used in the Enterprises

Report	Category	Frequency	Percent
Type	Sales report	61	44.9
	Profit and loss report	48	35.3
	Balance sheet report	12	8.8
	Purchase report	15	11.0
Frequency	Monthly	6	4.4
	Semi annually	52	38.2
	Annually	78	57.4

Source: Own Survey, 2020

A sales report, or sales analysis report, gives an overview of the state of the sales activities within a company. It shows the different trends happening in the sales volume over a certain time, but also analyzes the different steps of the sales funnel and the performance of sales executives.

The profit and loss (P&L) statement is a financial statement that summarizes the revenues, costs, and expenses incurred during a specified period, usually a fiscal quarter or year. The P&L statement is synonymous with the income statement. These records provide information about a company's ability or inability to generate profit by increasing revenue, reducing costs, or both. Some refer to the P&L statement as a statement of profit and loss, income statement, statement of operations, statement of financial results or income, earnings statement or expense statement.

A balance sheet is a financial statement that reports a company's assets, liabilities and shareholders' equity. The balance sheet is a snapshot, representing the state of a company's finances (what it owns and owes) as of the date of publication.

Purchase reports are reports exclusively generated for purchase transactions and the items that have purchase information in your organization. Currently we support six different sales reports - Purchase Order History, Receive History, Purchase by Vendor, Purchase by Item, Bill Details and Payments Made report.

A cash flow statement is a financial statement that summarizes the amount of cash and cash equivalents entering and leaving a company. The cash flow statement measures how well a company manages its cash position, meaning how well the company generates cash to pay its debt obligations and fund its operating expenses.

As can be seen from above table, the most common types of report prepared by MSEs include income statement and sales report. In addition, the majority of the respondents prepare the report on annually or semiannually. This is mainly due to absence of formal accounting system and lack of having professional accountant with its own department.

Table 4. 7 Responsible Organ for Bookkeeping

Responsible for Bookkeeping	**Frequency**	**Percentage**
Employee accountant	16	11.76%
Contract out to professional accountant	38	27.95%
Sell person	48	35.3%
Manager (Owner of the enterprise)	34	25%
Total	**138**	**100%**

Source: Own Survey, 2020

Because of their size and limited capacity, MSEs in Ethiopian are unable to keep book of accounts and prepare financial report by their own. Accountants assigned from MSEs agency are supposed to provide accounting service to them.

The reason is that these small firms do not have the capacity for sound financial management systems in place which will enable them to prepare financial reports. The end result is that it becomes very difficult for tax authorities to compute their taxable incomes. However, with respect to this survey, only two percent of the respondent confirmed that accountant from MSE agency are coming and keeping accounting record for their business.

From the above analysis one can see that the tendencies of recording their businesses operations on regular basis have been weak in MSEs. Regular, in this case, means a tendency at which MSEs record their business transactions, on a daily, once in two days, weekly, once in a fortnight or monthly. The frequency at which they record their business clearly indicates how much traditions of keeping financial records are entrenched in their operation. It is also clear that those businesses with a daily record keeping practice are obviously better than those keeping their records on a weekly or monthly basis.

4.6 Methods and Basis of Account Recording

Methods and system of accounting used in the enterprises are summarized by using frequency and percentage and presented in Table 4.8 below.

Table 4. 8 Method & system of accounting

Variables		Frequency	percent
System of accounting	Double entry system	32	47.1
	Single entry system	104	152.9
Reason for single entry	Easier than double	24	35.3
	Lack of knowledge on double entry	74	108.8
	other	4	5.9
Basis of accounting	Cash base	108	158.8
	Accrual base	28	41.2
Reason for cash base	Easier for application	50	73.5
	Lack of knowledge about accrual base	62	91.2
	Others (absence of credit sales and purchases; vouchers used as source documents were received or given on the date of purchase or sale)	24	35.3

Source: Survey, 2020

More than three fourth (80.6%) of the respondents indicated the recognition of revenue at the time of cash receipt or considering cash base whereas the remaining 19.4% were recognizing revenue when it is probable that future economic benefits will flow to the company and reliable measurement is possible (accrual basis of accounting). Among those respondents using the cash basis of accounting, 46.3% stated the reasons for the cash basis as lack of knowledge on accrual basis of accounting. Among the SMEs using cash bases of accounting, almost 89% were using the single entry system. Contrary to this result, IFRS for SMEs adopted by the government of Ethiopia with the proclamation No. 847/2014 require the accrual basis of accounting based on the double entry system for the preparation of general purpose financial statements by the SMEs in the country.

More than three fourth (76.1%) of the SMEs were using the single-entry accounting. Among those businesses using the single entry system, majority (72.5%) were indicated lacks of knowledge on the double-entry system as the reason to use the single-entry system. This could be due to the reliance of SMEs on external consultants to the preparation of financial statements annually for the taxing purpose. Due to the absence of strict follow up from the regulatory bodies for the day to day recording of economic events, SMEs owner managers were not forced to know about the modern accounting system. Simply they were collecting the necessary receipts and other documents and giving to their consultants so as to prepare financial statements required by the tax authority. The result also indicated that, the share of enterprises with double-entry accounting increases as the size of enterprise increases consistent with (Lindner and Hoelzl, 2012).

External Audit

An external auditor is a public accountant who conducts audits, reviews, and other work for his or her clients. An external auditor is independent of all clients, and so is in a good position to make an impartial evaluation of the financial statements and systems of internal controls of those clients. More than 95% Micro and small enterprises in this study are not audit there operational and financial results and report by external auditor, the main reasons for these are huge expense required in order to pay to auditors and lack of legal requirement by regulatory body.

Report to Members

Most of respondents have said financial issues of the enterprise described to them through meetings which held without formal schedules and meeting procedures, and this is due to sole proprietor is the only owner of the enterprise and regulates financial issues of alone and financial information about the enterprise do not concern as a significant part of their operation.

Budget Preparation and Utilization

A budget is basically a financial plan for a defined period, normally a year. It greatly enhances the success of any undertaking. As the saying goes, "if you fail to plan then plan to fail." A budget is an estimation of revenue and expenses over a specified future period of time and is usually compiled and re-evaluated on a periodic basis. Budgets can be made for a person, a group of people, a business, a government, or just about anything else that makes and spends money.

The study showed that most of MSE's prepare budget at only at initial stage of starting the business. After the starting their business operation, budgetary system in order to operate their business operation and control their output based on their preplanned budget and the main reason mention to this is low level understanding of the importance of budget and luck of knowledge with regard to how to prepare and implement budgetary system. Those who have use preplanned budget mainly use their previous year budget as a source to prepare the enterprise budget.

CHAPTER FIVE

CONCLUSION AND RECOMMENDATION

5.1 Conclusions

This study was conducted to assess practices of financial management and reporting at MSE in Addis Ababa; case of Lideta Sub city. The study has targeted employees with task of financial management and reporting in the enterprises. Data for the study was collected by using questionnaire and interview and analyzed by using descriptive statistics.

As this descriptive study result most of micro and small enterprise have minimum two maximum twenty members with 56% of them are male and from those 58.3% have college level educational completion. the most sector in which micro and small scale enterprises engaged are trade and service sectors, this is due to less startup capital requirement, in other side manufacturing sector require higher amount of capital in order to acquire necessary materials and machineries,

The study show that most micro and small scale enterprises form of ownership are sole proprietorship and partnership and their main source of initial capital is generated from owners and members contribution and microfinance institutions through loan and they described generating fund from bank is too difficult due need of collateral high interest expense.

The findings revealed that Most of MSE's do not have financial management policy and procedures and the study described the fact that most of owners and members of small businesses do not have adequate financial management skills and further training, most small businesses do not engage in financial planning, analysis, and control; do not set short and long term financial objectives; do not analyze the trend in sales, cost and profit. So, as far as small businesses have no plan most of them unable to compare their financial performance with their financial policy and procedural planes. Most of financial management issues of the enterprises hold by owners and there is no well-planned financial analysis and timely scheduled report preparation.

In relation with accounting practice, this study found that the level of awareness on the importance of keeping book of accounts and financial management is still very low in MSEs under study. The majority of the MSEs under study do not keep regular financial records. The main reasons for not doing so include smallness of the MSE and expensiveness of qualified accountants. Most of the owners or managers are also not aware of the importance of keeping regular accounting records and reporting. With regard to budget most of MSEs prepare budget only at initial starting level of the business and they do not audit their financial performance by external auditors the main reason is absence of legal requirement and high payment cost of auditors.

For those that are keeping regular accounting record, the most commonly kept record includes sales, purchase & payroll record in Single Accounting Entry System because of luck of accounting knowledge and Cash based Accounting Method due to easier for application. The common types of report prepared from these records are the profit and loss statement. With regard to budget most of micro and small scale enterprises owners and members have not adequate knowledge about budget and do not prepare and implement preplanned budget.

5.2 Recommendations

In general the financial management and reporting practice of most of micro and small scale enterprises found very poor and needs many improving activities. Based on the conclusions drawn, following recommendations are provided:

- Necessary trainings should be prepared and delivered to owners and members of micro and small scale enterprises in relation with the significance and importance of financial management including how to develop and implement financial policies and procedures, financial plans and controlling mechanisms.
- Provide training programs in financial management skills for the owners and managers of business organizations

- The ministries of finance and industrialization should provide a favorable platform for SMEs to access financing that can enable them to run their businesses at a reasonable cost of financing. This is necessary since access to bank loans was found to be difficult for SMEs and end up using only internally generated (saving & family support) funds and microfinance institution. The interest rates should be favorable;
- Financial expertise should sensitize the SMEs owners on the relevance of bookkeeping, financial reporting and analysis as well maintaining proper books of analysis. Capacity building should be organized for SMEs to help them understand why they should keep updated books so as to know their levels of performance on whether they are making profits or losses.
- Governmental and Non-Governmental institutions that have responsibilities with Micro and Small scale Enterprises – especially SEDA (Small Enterprise Development Agency) better to provide various training opportunities for owners and members with respect to areas of financial management, budgeting and practicing accounting procedures including report preparation.
- It is also advisable that, owners and members of micro and small scale enterprises try to maintain professional accountants in order to maintain complete accounting records and reporting practices. Gradually, the government better create conducive environment for financial system of the country in order to mobilize funds effectively so that, owners of small businesses can get access to finance so as to raise their investment funds. Since significant part of small business investment is in working capital, the owner of the small businesses better to consider how to keep it circulating quickly and make sure that none is lying idle.
- Government and regulatory body should put, having proper financial management and reporting practice, preparation of budget and audit through MSEs as a measurement tool to provide license, working place, selling shops, training and many other supports because financial management and reporting practice determines he future success of an enterprise, in addition it also advisable to assign professional accountants and auditors at ground level (woreda) level in order to support and monitor MSEs improvement in their financial management and reporting practices.

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Appendices

QUESTIONNAIRES ON FINANCIAL MANAGEMENT AND REPORTING PRACTICE ON SMALL AND MICRO ENTERPRISES IN LIDETA SUB-CITY ADDIS ABABA

Please read each statement and indicate your level of agreement by taking from the options provided. If you make an error, cross it out and indicate your actual response. Your elaboration will add tremendous value to the findings of this study. Hence, if you need more space to express your opinions use the back of each page in this questionnaire

1. General

1.1. Age

18- 25 ☐ 36 - 45 ☐

26- 35 ☐ >45 ☐

1.2. Sex

Male ☐ Female ☐

1.3. Responsibility in the Enterprise ---

1.4. Education

Illiterate ☐ Primary cycle ☐

Secondary cycle ☐ Collage and above ☐

1.5 What is the type of business dose the enterprise involved in?

A. Construction ☐

B. Merchandise and retail shop ☐

C. Textile and Garment ☐

D. ICT and maintenance ☐

E. Food and beverage ☐

F. If other, specify…………………………

2. What is the form of ownership in this business?

A. Sole proprietorship ☐

B. Partnership ☐

C. other ☐

3. How many employees did the enterprise have when first established including the Principal owner?

A. 2 – 5 employees ☐

B. 6 – 10 employees ☐

C. 11 – 20 employees ☐

D. >20 ☐

4. Capital

Source of Initial Capital

How did you raise funds to start-up your business?

A. Personal saving ☐ B. Family ☐ C. Banks ☐

D. Micro finance institutions ☐ E. Friends/Relatives ☐

Others (specify) -----------

5. Financial Management

5.1. Does the M&S Enterprise have financial policy/procedure manual?

Yes No ☐ ☐

5.1.1. By who was the financial manual /procedure prepared.

5.2. What are the types of services or goods provided by the M&S. Enterprise?

5.3. Does the consumer S&M Enterprise have finance manager?

Yes ☐ No ☐

5.4. If no who took the role of finance management S&M Enterprise?-----------------------
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5.5. Have ever the S&M Enterprise took loan?

Yes ☐ No ☐

5.6. If yes from which institution

Bank ☐ Micro finance institution ☐ Individual Kebele ☐

4.9 Does the S&M Enterprise prepare financial plan? If your answer is yes go to next question

Yes ☐ No ☐

5.7. For what purpose S&M Enterprise prepare financial plan? (More than one choice allowed).

A. Conservation of capital ☐

B. Efficient use of financial resources ☐

C. controlling purpose of financial flow ☐

D. Optimum capital structure at minimum cost ☐

5.8. Does the M&S Enterprise includes capital budgeting in its financial plan?

Yes ☐ No ☐

5.9. What is its source of working capital? ---
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6. Reporting

6.1. Do you have a record keeping and financial control system?

Yes ☐ No ☐

6.2 What kind of record keeping and financial control system you reusing?

A. Recording the daily transaction ☐. Balance sheet ☐ Income statement ☐

D. If other specify…………………

6.3. Who does the bookkeeping?

Employee accountant ☐ Contract out to professional accountant ☐

Finance controller ☐

6.4. Which type of account register book maintained by the M&S Enterprise?

Daily journal ☐ General journal Capital ☐ Retained earning ☐

Account receivable ☐ .Others please specify---
-

6.5. Method of account recording Bing applied by M&S Enterprise

Cash basis ☐ Actual basis☐Modified cash basis ☐

6.6 Are the M&S Enterprise audited by external auditors?

Yes ☐ No ☐

6.7. How does a member know about the M&S Enterprise finances?

Attending meetings ☐

By looking into reports ☐

Annual report ☐

Any other specifies ---

7. Budget

7.1. Dose the M&S Enterprise use a budget?

Yes ☐ No ☐

7.2. If your answer to 6.1 is no, why not?

7.3. What sources does the M&S Enterprise refer to prepare its budget?

Records of expenditure ☐ .Previous budgets ☐ .Experienced professionals ☐