Financial Management Strategies for Sustaining Small and Medium-Size Enterprises

Abstract

Financial management plays a major role in ensuring organizational sustainability. Small and medium-sized enterprises have to establish strategies for effective financial management to foster organizational productivity, growth, and sustainability. The literature review seeks to explore existing literature on successful financial management strategies that can promote organizational sustainability.

Keywords: Financial management, SMEs, organizational sustainability, small business owners

Introduction

To sustain small and medium-sized enterprises (SMEs), organizational leaders, management, employees, and other involved stakeholders have to collaborate and effectively implement different financial management strategies to foster organizational sustainability, growth, and profitability. The literature review seeks to review existing literature on financial management strategies for sustaining SMEs. The identified topics that will be explored in the literature review include financial management of SMEs, such as the use of financial accounting, management accounting, strategic approaches to successful financial management, variance analysis, and ratio analysis. The nature of SMEs will also be explored in the literature review, including strategies for sustaining SMEs, the use of the balanced scorecard as a tool for promoting organizational sustainability, SME success and failure, as well as the impact of regulatory compliance on SMEs.

Literature Review

Financial management of small and medium-sized enterprises (SMEs)

Financial management is a critical element of the success of SMEs, but also challenging to be controlled by many SMEs. Financial management has been cited as the most fundamental and important element in an organization's management system, and when managed effectively, can result in improved organizational sustainability (Hlaciuc et al., 2017). Owners of SMEs should therefore focus on maintaining the productivity and integrity of the entity's financial assets to attain strategic goals and improve investment returns. Hlaciuc et al. (2017) noted that efficient SMEs' financial administration is fundamental to warranting effective resource allocation for financing organizational activities and different operational activities such as formulation, development, and implementation of financial resources; coordination of accounts payables and receivable; and cash flows and financial metrics' regulation and analysis.

Small business owners' ability to design and adopt financial management approaches that result in organizational success is critical. Hoque (2017) maintained that entrepreneurs who participate in their companies' financial decision-making practices facilitate the adoption of exceptional initiatives and enhanced organizational productivity and motivation. Di and Wang (2017) also showed that successful small business owners often go through various financial decision-making processes, and those who fail often disregard conventional and more effective financial management strategies that have demonstrated effectiveness due to their goals and self-interest in owning a business. Therefore, considering successful financial management strategies that have been successful for other small business owners can help SME owners to identify suitable financial management strategies for their specific entities (Hossain, 2018). SME owners who are involved in the adoption of their firms' financial management activities are key to their companies' success.

Financial management. Financial management is a critical factor for organizational sustainability. Vucinic (2016) maintained that small business owners play a significant role in the financial health and performance of their organizations, and they have to be cognizant of the decisions that they make since they significantly impact their organization's success. The aim of financial management is the maximization of corporate value through profit generation and efficiency by facilitating the protection of key organizational interests (Hart & Zingales, 2017). Effective financial management can therefore help SME owners to improve their firm's profitability while improving the firm's best practices. Effective financial management encompasses different responsibilities and tasks. Suh & Lee (2018) maintained that efficient financial management is important to ensuring organizational success and plays a critical role in identifying and optimizing financial and economic resources.

Similarly, Siminica et al. (2017) asserted that strategic planning, programming, and evaluating an organization's operational activities are consolidative ways to successful

development, formulation, and adoption of financial management activities. Vucinic (2016) added that establishing the content and scope of economic policies, determining general standards and guidelines for the generation and allocation of funds, and establishing corporate structures and control of financial tasks are key points to sound financial administration. Successful adoption of financial administration strategies guarantees the integrity and reliability of financial data. Comprehension of the nature of SMEs can guide entrepreneurs to adopt financial management tactics that have been proven to enhance organizational productivity and sustainability.

Financial accounting. Financial accounting is a fundamental technique for structuring organizational expenses and revenue. Financial accounting entries record the financial and economic documents, as well as accounting records that help in formulating the income statement, the balance sheet, and the cash flows statement (Niculae, 2017). Accurate and useful information generated through financial accounting reports impacts an organization's capacity to uphold operational consistency. Financial accounting can enable SME owners to cultivate sound financial statements related to organizational financial health (Dearman et al., 2018). Financial accounting can also help in the documentation and tracking of financial transactions. The main focus of financial accounting is to identify, measure, record, and communicate accounting information, and its goal is to determine an organization's financial position to communicate such results to organizational stakeholders (Dearman et al., 2018). To reduce errors, technological tools can be used for SMEs to maintain sound financial accounting documents. SMEs can improve financial management by integrating technological innovations such as the use of accounting software to support accounting measures for improved record keeping.

Management accounting. Management accounting can be defined as the process used to identify, measure, and communicate financial information that can be used to strategically

plan, evaluate, and control an organization. While financial accounting helps in the development of financial reports for external and internal use, Samuel (2018) has cited management accounting as an important accounting tool that improves a firm's internal visibility. SME owners can use management accounting for a better understanding of their organization's performance. As shown by Jansen (2018), management accounting can help SMEs to enhance resource management. Management accounting can allow SME owners to evaluate their organizations' performance and contribute to strategic decision-making. It can also improve their visibility of organizational performance by providing SME owners with a real-time perspective of financial performance trends (Niculae, 2017). Management accounting is a reflection of the process used by business owners for preparing and accounting for accurate financial data, and to maximize the welfare of an organization's sustainability (Soni et al., 2018). SME owners can use management accounting to enhance accounting operations and strategic finance for ultimate organizational profitability and sustainability.

Strategic approaches to successful financial management. Strategic approaches have been attributed to successful financial management. For SMEs, financial management involves mapping non-financial and financial assets to strategic organizational objectives to optimize organizational performance. SME owners should therefore prioritize the implementation of financial strategies that can be used by employees as a guideline for managing an organization's financial affairs (Suh & Lee, 2018). Organizational profitability and performance have been cited to improve when organizational leaders adopt strategic financial initiatives. Greenberg et al. (2018) maintained that organizational leaders who invested in enterprise resource planning (ERP) systems often improve the efficiency of their organization's business intelligence and internal controls, in addition to improving routine evaluation of key financial performance indicators such as variance and ratio analysis.

Variance analysis. Variance analysis refers to a quantitative technique that is used for understanding the variation between planned and actual behavior. It is an important tool for evaluating an organization's financial performance (Dai et al, 2021). Variance analysis is considered to be a financial accounting control function that helps managers in identifying inconsistencies between actual and budgeted cost allocations to foster operational consciousness and the establishment of a culture of efficiency within an organization's financial operations and analysis (Dai et al, 2021). It examines the budget versus the actual costs to establish considerable cost discrepancies that can be assessed for improved organizational performance. Cost variance analysis can improve the use of standard cost systems. Jiang et al. (2018) showed that business owners often redirect organizational goals, strategies, and objectives when there is a variance between actual and budgeted costs. Variance analysis of an organization's costs can help in the integration of sustainability measures by identifying constraints, trends, threats, and opportunities. SME owners can therefore use variance analysis to discover and address problems that emanate between actual and expected costs.

Ratio analysis. Ratio analysis refers to the use of financial statement ratios to assess and analyze an organization's financial strengths and weaknesses (Subalakshmi et al., 2018). Ratio analysis can be utilized for performing a comparison of information taken from financial statements to gain an enhanced understanding of an organization's financial position, outcomes, and its cash flows. It is a useful tool, particularly for outsiders such as lenders, credit analysts, or stock analysts who need to develop an outlook of the financial position and results of a company from its financial statements. Ratio analysis can be used to assess current and historical conditions and the financial performance of an organization. Rashid (2018) asserted that ratio analysis can be used to examine an organization's current liabilities and current assets by calculating the current ratio.

Key ratio analyses that can be used by SMEs include liquidity ratios, profitability ratios, and efficiency ratios. Liquidity implies an organization's ability to meet its short-term obligations when they fall due (Kadim et al., 2020). Liquidity ratios are usually used for assessing the short-term financial position of a company. One of the most common liquidity ratios is the current ratio, which explains the relationship between current assets and current liabilities of a firm. Profitability ratios help in measuring a company's ability to generate profits from its operational activities, in addition to helping in the discovery of whether a firm's profitability is decreasing or increasing (Kadim et al., 2020).

Gross profit ratio is a typical example of a profitability ratio, and it shows a company's profit margin after deduction of the costs of goods sold but prior to deducting operating expenses. Efficiency ratio is usually used for analyzing how well an organization uses its liabilities and assets internally (Kadim et al., 2020). A typical example is the inventory turnover ratio, which measures the number of times a firm's inventory is sold in a year. Ratio analysis, therefore, offers SME owners the ability to evaluate current and past trends in their organization's financial performance, something that can be used to assess an organization's financial health. Ratio analysis provides for understanding financial statements, identifying developments, movements, and measures of an organization's overall financial health.

SMEs: There is widespread literature on the purpose, meaning, and importance of small and medium-sized enterprises. Lima et al. (2017) noted that SMEs play a critical part in the American economy, influencing different aspects of social life and societal fabric. SMEs can be defined as independent businesses with fewer than 500 employees. SMEs are considerable drivers and promoters of job development, economic growth, and poverty reduction. SME owners play a critical role in economic growth and innovation by executing their firms' strategic goals. Corporate networks are fundamental factors that relate to the effect of SMEs on economic development.

Sustainability of small businesses. Small businesses often face challenges in promoting organizational sustainability. Sustainability is an organization's ability to identify and advance corporate activities that guide it to adapt and administer transformations within its operational environment. To achieve sustainability, Suh and Lee (2018) maintained that SMEs need to perform sustainability-oriented actions such as participating in corporate social responsibility activities. The organization also has to be aware of behavioral impact as well as the impact of immaterial and material conditions of their indirect and direct environment (Imran et al., 2019). Sustainability of an SME is critical to the growth and health of economies. Therefore, SME owners have to be aware of environmental and economic transformations, with the openness to adapt and ensure organizational growth and profitability through sustainability.

The balanced scorecard. SME owners can influence their businesses' performance by adopting strategic management and planning techniques such as the balanced scorecard. Wehde (2018) showed that successful SMEs utilize the balanced scorecard as a strategic management technique for ensuring that organizational operations are aligned with organizational strategy. As a strategy implementation technique, the balanced scorecard can influence SMEs' success and performance. Quesado et al. (2018) noted that SMEs that have adopted the balanced scorecard within their organizations can yield strategies around organizational initiatives, improve processes for enhanced competitive advantage, and ensure success around organizational ideas. The balanced scorecard can allow SME owners to monitor the performance of their businesses, improve communication of corporate and strategic objectives, and identify areas of improvement.

The balanced scorecard can be used by SME owners to improve organizational communication. Malagueño et al. (2018) noted that the balanced scorecard can provide SME owners with the ability to monitor, improve, and organize internal financial and organizational

performance, in addition to scaling measurement for monitoring external aspects such as consumer experience for improved customer retention and brand loyalty. Strategic efforts and organizational plans can also be communicated using the balanced scorecard (Malagueño et al., 2018). The balanced scorecard offers SMEs with short- and long-term goals, and helps in aligning business processes and employee efforts to strategic goals. The implementation of the balanced scorecard can improve an organization's ability to communicate and attain strategic objectives and translate such strategies into achievable actions.

SMEs success. Small business owners can impact corporate success and sustainability. Moeuf et al. (2020) revealed that SME owners who are experienced and knowledgeable about key success factors often foster effective means of attaining organizational sustainability. To achieve SME success, internal stakeholders of an organization have to understand the organization's strategic goals. Kreiser et al. (2021) maintained that entrepreneurs can operationalize performance and success by attaining corporate viability through the operation of a profitable entity that does business ethically and contributes to the society in which they operate. While success cannot be guaranteed, SME and contributions to economic development depends on small business owners' planning efficiency.

For organizational success, entrepreneurs have to effectively optimize organizational resources for the strategic implementation of organizational goals. George et al. (2019) revealed that small business owners can use external network resources and internal resources as strategies for ensuring organizational success. SMEs have an advantage over large businesses in capitalization on innovation to ensure organizational success by applying corporate governance to scale sustainable practices. Bertello et al. (2021) noted that collaborative efforts and corporate networks are essential elements in governing SME sustainability. Successful SMEs employ practical resources such as professional networks to improve organizational success.

SMEs failure. There are a number of factors that influence the failure of small businesses. Eniola and Entebang (2017) indicated that poor knowledge and management of accounting and finance by business owners and entrepreneurs is a major cause of organizational failure. Ignorance of accounting and finance, and inadequate knowledge have been cited as factors that impact SMEs' sustainability. Other reasons for SMEs' failure are business owners' perception of the complicated nature of critical factors that result in SME success and market survival (Eniola & Entebang, 2017). Lack of strategic planning has also been cited as one of the major factors that contribute to SME failure.

SME owners who do not possess effective administration and visibility of organizational functioning in real-time can fail to make strategic data-driven decisions. Canhoto et al. (2021) indicated that a lack of formal training and skills within an SME is are internal influence that can fail an SME. Bertello et al. (2021) also argued that the rate of failure among SMEs differs as a result of company size, indicating that large firms have access to more and diverse resources and can easily manage fixed operational costs. However, SMEs do not enjoy such luxuries since an increase in fixed operational costs can adversely affect small firms' market share, which can ultimately result in early industry exit. While there are different factors that can lead to SME failure, the ultimate responsibility of fostering organizational success lies with business owners. Owners, therefore, have to be involved in the financial and operational management of their businesses for improved productivity and profitability.

Impact of regulatory compliance on SMEs. There are different regulatory and ethical compliance laws that have to be considered by SMEs. Badini et al. (2018) indicated that regulatory requirements are critical factors that can result in SME failure. Regulations imposed by local governments and states can be troublesome to emerging and small firms. Badini et al. (2018) posited that policies created and enforced by government bodies are often received adversely by SMEs, who perceive them as culturally remote. However, SMEs can be successful

by ensuring strict compliance with regulatory requirements and by conducting business within the applicable ethical and legal framework.

Conclusion

In the literature review, the author has explored the topic of financial management of SMEs, such as the use of financial accounting, management accounting, strategic approaches to successful financial management, variance analysis, and ratio analysis. The nature of SMEs has also been explored in the literature review, including strategies for sustaining SMEs, the use of the balanced scorecard as a tool for promoting organizational sustainability, SME success and failure, as well as the impact of regulatory compliance on SMEs. It was noted that SME owners play an important role in ensuring SME success and organizational sustainability, and they have to be actively involved in the financial management and operational management of the organization. They play an important role in ensuring measures are put in place for the successful implementation of financial management strategies for organizational sustainability, including appropriate management of the firm's financial records, the use of appropriate accounting policies and systems, and adherence to corporate governance guidelines.

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