

# Cash Management Practices and Financial Performance of Small and Medium Enterprises (SMEs) in Jordan

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## ABSTRACT

This study examined empirically the cash management practices and its effect on the financial performance of SMEs in Jordan. However cash shortage is a chronic challenge to these firms, and cash management is very crucial to the survival and growth of small and medium enterprises.

To meet the objective of this study, the researcher sampled firms operating in various sectors of economic activity. A structured questionnaire was used to collect primary data from the respondents which were analyzed to generate frequencies and percentages.

The study revealed that only (32) percent from SMEs kept track of Cash Receipts and payment. and the majority (67%) of respondents have no knowledge about cash control procedures. The study concluded that cash management practices have influence on the financial performance of SMEs. The researchers recommend to the need to for SME managers to embrace efficient cash management practices as a strategy to improve their financial performance .

**Keywords:** Cash management, cash surplus, cash deficit, cash control, small and Medium enterprises.

## 1. INTRODUCTION

All over the world small and medium enterprises (SMEs) are considered as backbone of a country's economy. They play a key role in economic development and make an important contribution to employment and GDP, and are important contributors to total employment and job creation. In Jordan SMEs comprise 98.5% from the total amount of registered companies, and 60% of formal jobs, in addition to 50% of the GDP in 2013 (1) and they are the engine of solving the unemployment.

Cash is used to pay business obligations. Cash management assumes more importance than any other current asset and the major aim is to maintain adequate control over cash position to keep the firm with sufficient liquid and use the excess cash in some profitable way.

Cash is the vital component of the working capital because it keeps a business running. It is the hub around all financial matters centre. Thus, management of cash is crucial for the success of an enterprise. The adequacy of cash and other current assets, together with their efficient handling, virtually determines the survival or extinction of a business concern. Cash is an important current asset for the operations of business. It is the basic input needed to keep the business running on a continuous basis (Abu Tabanja 2005).

No business operation is isolative of cash management. Cash is regarded as the most important current asset for the operation of business (Olowe, 1998). Cash is the basic input required to keep the business running on a

continuous basis and it is also the ultimate output expected to be realized by selling the services or products manufactured by the firm (Pandey, 2010).

The role of Small and Medium Scale Enterprises (SMEs) in the world economy have been highly emphasized as the means through which rapid industrialization and other development goals of a nation can be realized. Small and medium sized enterprises (SMEs) form a large part of economy and are regarded as the drivers of socio-economic development in all countries .

The general objective of this study is to ascertain the cash management practices among small and medium scale enterprises in the Jordan .

The study focuses on cash management practices is limited to the practices associated with management of cash and cash equivalents of small and medium scale in Jordan as well as the effect of cash management on the financial performance of SMEs.

## **2. Literature Review**

Cash generally can be said to be liquid money in form of coins, notes and other related means of instant exchange.

### **2.1 Small And Medium Business Defined**

The importance of SMEs has attracted a lot of attention internationally in past few years due to their significant contributions to the economies of both the developed and developing countries (Asiedu, 2006).

Small and Medium Enterprises have been defined in various ways according to the capital of the enterprise, size ,the number of people employed by the enterprises, the ownership and management of the enterprises and sales volume, all the definitions agree on the common views that small or medium businesses employ few people and are characterized by a relatively small amount of capital and turnover.

### **2.2 Small And Medium Business in Jordan**

There is no universal definition of small scale businesses. However, different scholars, writers, researchers and policy makers have used different definitions for small scale businesses basing on the number of people employed, capital employed among other relevant factors.

In Jordan, the Ministry of Planning and International Cooperation (2011), define small enterprises as those with less than 20 employees, and medium enterprises as those with between 20 to 99 employees. However, to bring greater precision to the analysis these numbers were further broken down into brackets.

The brackets are: 1-4, 5-19, 20-49, 50-99 which are in compliance with the Department of Statistics classifications. The private sector in Jordan is made up of large firms with 196,945 employees, and SMEs represent 60% of the total private sector and 37% of total employed in Jordan. Most Jordanian SMEs work within the formal sector and are registered, as specified by law. Formal SMEs play a vital role in job generation .

A sizeable percentage of self-employed firms are in the unregistered (informal) sector (that is, firms that deliver lawfully permitted services and products without being legally registered). There are 146,707 SMEs registered enterprises in the Kingdom. (Jordan Human Development Report, 2011).

### **2.3 Cash management**

Cash management refers to the management of an entity's cash to ensure sufficient cash to sustain the entity's daily operations, finance continued growth and provide for unexpected payments while not unduly forfeiting profit owing to excess cash holdings (Akinyomi:23).

Basically cash management is concerned with managing cash flows that is cash inflows and cash out flows. Major sources of cash inflow include cash from operating activities, sell of business assets among others. Sources of cash out flows include settling of creditors, purchase of inventory among others. Cash needs to be efficiently managed and allocated to meet routine business objectives. The gap between cash expenses and cash collection enhances liquidity position, profitability leading to overall business growth over a period of time (Brinchk, soeren & Gemuenden, 2011).

### **2.4 The Importance of Cash Management**

Cash management decision is one of the important decisions because of the scarcity of financial resources of many companies, and for different objectives and, as we know that cash is the most liquid assets, where cash is considered an important element in the management of the company's operational process in order to achieve success. The cash management is a function of financial management and that are interested financing and investment operations as the cash component affects the performance of the companies and the competitors in markets. A lot of companies interesting to think in the following decisions: capital structure, capital budgeting and the decision of the working capital where the decision of the working capital is the important decisions that affect of the performance of companies in terms of liquidity, which is reflected on the profitability and hence the level of competition in the market as it may determine the survival or the company out of the market (Appuhami, 2008)

According to Akinyomi (2014:58), the importance of managing cash in a business comprises of the following advantages:

- Managing cash helps in achieving liquidity in a business and proper control;
- It assists in the planning towards reducing cash expenses and increasing cash receipts to ensure the business is liquid;
- Proper managed cash is vital as the future cash flow behavior cannot be predicted. Therefore, it's essential to plan; and
- Through proper controls of cash, innovative procedures could be implemented for cash receipts and cash payments in the business.

### **2.5 Cash management in SMEs**

Cash is generated by MSEs mainly through their daily business activities. However, their funds from daily business activities are woefully inadequate to support expansion in their operations thereby creating a vacuum (cash deficit) which has to be handled appropriately in order to survive in the competitive business environment.

Efficient cash management involves the determination of the optimal cash to hold by considering the trade-off between the opportunity cost of holding too much cash and the trading cost of holding too little (Ross et al., 2011) there is the need for careful planning and monitoring of cash flows over time so as to determine the optimal cash to hold. Good cash management can have a major impact on overall working capital management.

### **3. Research Methodology**

A descriptive study was chosen to undertake this research to discover and understand the cash management practices of the small and medium enterprise. The research was conducted by gathering data from both primary and secondary sources. Based on the literature review and the theoretical framework, a survey questionnaire was developed to be the major instrument of this study. Questionnaires were the main instrument that was used in gathering the data. The questionnaires contained both open-ended and closed ended questions. Out of 300 samples of questionnaires sent to SME managers, 270 (90%) were returned and found to be usable.

### **4. Results and Discussion**

#### **4.1 Profile of Responding Firms and Respondents**

The results obtained from the survey through questionnaires are presented in this section. Table (1) shows that in terms of number of years in business, many of the proprietors have been in business between 5-10 years representing about 40 percent. Twenty-nine percent had been in business between 1-5 years while 13 percent had been in business for more than 10 years. And the respondents' experience showed that (18%) have less than one year. The finding shows that the largest number of SMEs (84%) is Sole Proprietorship, followed by Partnership (11%) and Limited Liability company (5%) respectively, with Limited Liability company comprising the smallest number (5%) of SME businesses.

The large number of the respondents most educated individuals to earn a living reflected by an average percentage of 44% from School certificate, Diploma, level (32%) percent and Bachelor's degree (20%) percent. This means all categories of individuals participate in operation of small scale business. Only four percent of respondents are Master's degree.

The nature of the business of the SMEs as depicted in Table 1 reveals that (34%) and percent were engaged in Wholesale, a business which is very easy to set-up in Jordan. Other businesses engaged in by respondents included Retail and Manufacturing 11 percent, . and respondents from Other services constitute only 32% (see Table 1).

**Table 1:** Characteristics of Enterprises studied and Owners

Characteristics	Frequency	percent
<b>A. Number of Years in business</b>		
Less than 12 months	49	18
1year – 5years	78	29
5 years – 10years	108	40
Above 10years	35	13
Total	270	100
<b>B. Type of Business Ownership</b>		
Sole Proprietorship	226	84
Partnership	29	11
Limited Liability company	15	5
Total	270	100
<b>C. Educational Background of MSEs Operators</b>		
School certificate	120	44
Diploma	86	32
Bachelor's degree	55	20
Master s degree	9	4
Total	270	100
<b>D. Type of Industry MSEs Operate in</b>		
Retail	62	23
Wholesale	92	34
Manufacturing	30	11
Other services	86	32
Total	270	100

### **The level of knowledge in cash management practices**

Improving cash management practices is one of the most important issues of the financial world .the table(2) below shows owner of SMEs knowledge in cash management practices.

**Table 2: The level of knowledge in cash management practices**

Cash Management Practice	Yes	Percent	No	Percent	Total	Percent
Preparation of Cash Budget	76	28	194	72	270	100.00
Operating Bank accounts	188	69	82	31	270	100.00
Keeping track of Cash receipts	94	35	176	65	270	100.00
Keeping track of Cash Payments	91	34	179	66	270	100.00
Keeping Proper Books of Accounts	88	33	182	67	270	100.00

The results of the descriptive statistics for Knowledge in Cash Management Practices are reported in Table (2). The majority (67%) of the respondents indicated they did not have Knowledge in Cash Management, Keeping track of Cash receipts, Payments, Keeping Proper Books of Accounts. And only (33) percent of respondents maintain bank accounts .

Most respondents of the medium and small-scale operators under investigation had no knowledge about how to implement sound cash management practices.

### **Keeping track of Cash Receipts**

**Table 3: Keeping Track of Cash Receipts**

Type of MSEs	Yes	Percent	No	Percent	Total	Percent
Retail	21	24	41	66	62	23
Wholesale	29	33	63	34	92	34
Manufacturing	9	10	21	11	30	11
Other services	28	32	58	32	86	32
<b>Total</b>	87	32	183	68	270	100

Table(3) shows that present information on the financial records keeping of SMEs in the Jordan. when the respondents were asked to indicate whether they kept track of cash receipts ,(32% )of the respondents ,from Wholesale(33%) ,answer yes, as indicated from (Table 3). Of the remaining (270) who answered the question, 69% indicated that did not keep track of their cash receipts ,This makes them very susceptible to the risk of misappropriation of funds.

This means that majority of SMEs didn't keep financial records of their business in order to manage their cash flows and as a result help determine the financial position of their business. Kasim, et al (2015), attributed the high rate of SMEs failure to poor financial records keeping and insufficient use of accounting.

### **Keeping Track of Cash Payments**

Table (4) presents the responses of owner managers of the SMEs, regarding the Keeping Track of Cash Payments for their businesses.

**Table 4:** Keeping Track of Cash Payments

Type of MSEs	Yes	Percent	No	Percent	Total	Percent
Retail	20	32	42	68	62	23
Wholesale	31	34	61	66	92	34
Manufacturing	8	27	22	73	30	11
Other services	25	29	61	71	86	32
<b>Total</b>	84	31	186	69	270	100

From Table(4), the Keeping track of cash payments is crucial in ensuring that the enterprises have sufficient cash balances. Cash payments must also be controlled through proper monitoring to control cash outflows. Cash payments by MSEs should be streamlined in order to ensure that these small businesses that continually face financial challenges are saved from this situation,( Attom , 2014).

The respondents who did not have kept track of their cash payments (69) percent, and only (31) percent who keep track of their cash payments, represent small portion of(270) response. See table(4).

#### Controlling cash flows by Nature of Business

**Table 5:** Controlling cash flows by Nature of Business

Type of MSEs	Yes	Percent	No	Percent	Total	Percent
Retail	19	31	43	69	62	23
Wholesale	28	30	64	70	92	34
Manufacturing	18	60	12	40	30	11
Other services	28	33	58	67	86	32
<b>Total</b>	93	34	177	66	270	100

The above result in Table( 5) revealed that on average (34%) of the SMEs under study applied cash flow control, but the majority of SMEs under the study findings revealed that on average (66%) of SMEs studied did not Controlling their cash flows.

#### Preparation of Cash Budget

When the respondents were asked to indicate whether they prepare the Cash Budget

**Table 6:** Preparation of Cash Budget

Type of MSEs	Yes	Percent	No	Percent	Total	Percent
Retail	17	27	45	73	62	23
Wholesale	22	24	70	76	92	34
Manufacturing	9	30	21	70	30	11
Other services	21	24	65	76	86	32
<b>Total</b>	94	35	176	65	270	100

From table(6) above,( 65) percent of the respondents who seldom prepares the cash budget reported they didn't need it at the time while (35) percent reported that cash budgets apply to their business. This implies that up to 176 of the respondents, who did not prepare cash budget, didn't actually see the need for its preparation. Only 94 of the SMEs indicated they prepare budgets. This finding supports the pronouncement by Waweru (2003), that majority of businesses do not prepare cash budgets. It also confirms Kwame (2007) decree that most small businesses have problems on how to prepare cash budgets.

### Types of Bank Account Kept by MSEs

Table(7) presents the responses of owner managers of the SMEs, regarding the type of bank Accounts, the most widely used was current Accounts, while saving accounts was the least used. (47) percent of the respondent operated Bank account as depicted in Table (7), as compared to( 25) percent who stated they did not maintain bank accounts. The result shows that most SMEs are beginning to appreciate the importance of having a business account. This is similar to the finding of Hamza & others(2015) who concluded that majority of respondents operated bank accounts widely in current accounts.

**Table7:** Types of Bank Account Kept by MSEs

Type of account	Frequency	Percent
savings	38	14
current only	126	47
Current & savings	39	14
Non response	67	25
<b>Total</b>	270	100

### Records Kept on Cash Transaction

Table 8 shows the documents on which records of cash transactions of SMEs are kept.

When the respondents were asked to indicate the various records they kept on cash transactions, Cash book records were the most significant (33%) as depicted in Table (8). Other forms of records kept on cash transactions with their respective responses included cash book (22), bank statement (22%) and cheque (21%). Seventeen percent and seven percent respectively of respondents indicated they also keep records of their cash transactions by way of payment voucher and note book.

**Table 8:** Records kept on Cash Transactions

Type of records	Frequency	Percent
Cash book	98	33
Bank statement	56	22
Cheque	57	21
Payment voucher	43	17
Note book	16	7
<b>Total</b>	270	100

## The relationship between cash management practices and financial performance

The results establish the relationship between cash management practices and the financial performance of SMEs. Pearson's correlation coefficient was used to address this objective.

### Pearson's correlation coefficient results

Table(9) shows that correlation results that there was a strong positive relationship between SMEs' Financial Performance (FP) and Effective Cash management (ECM) ( $R=0.612$ ,  $p<0.01$ ). Generally and as reflected in the empirical review, most researchers have showed that businesses' performance is correlated positively to cash management practices (Kotut, 2003; Kwame 2007; Dong and Tay Su 2010, and Ross et al. 2011) and are therefore supported by this research finding.

**Table 9:** Correlation results

Parameters	Variables		FP	ECM
Spearman rho	FP	Correlation	1.00	
		co-efficient		
	Sig.(2 tailed)	-		
	ECM	Correlation	0.592	1.00
		co-efficient		
	Sig.(2 tailed)	0.000	0.00	
Correlation is significant at 0.01 level (two tailed)				

### Conclusion

It is obvious from the study that cash management is an important aspect of management function and its importance cannot be over-emphasized. When companies understand and implement the concept of efficient cash management, business success will be achieved. However, shortage or bad management of cash may result in loss of cash discount, loss of reputation due to non-payment of obligation on due dates and insolvency which may result in operational shut down of the company (Tuller, 2008).

This study has revealed that the SMEs owner have not sufficient of Knowledge in Cash Management Practices, and did not have kept track of their cash payments & receipt. seldom prepares the cash budge, and operated bank accounts widely in current accounts. There was a strong positive relationship between SMEs' Financial Performance (FP) and Effective Cash management

As suggested by Gallagher (2000), implementation of a good cash management system will ensure better control of financial risk, increase the opportunity for profit, strengthen the company's balance sheet, ensure increased confidence in the company and improve operational efficiency.

Cash management is vitally important as it is the key factor to any successful business. The commonly used expression, "Cash is king" cannot be contested as its validity is more prevalent in this research study.

The results also indicated that cash management is an essential aspect that the owners/managers of the businesses have to ensure for better performance.

Based on the establishment of the fact that the financial performance of SMEs in Northern region had a low average, with majority of the SMEs describing their performance to be either deteriorating or failing,

The management need to ensure there are adequate cash management controls to ensure all the time there is optimal cash where there are strategies to be in place during minimal cash and surplus cash since either of the side will contribute to liquidity risks to the organization

### Areas for further research

For further research, it would seem reasonable to investigate cash management behavior in greater detail using the ratios of financial statement analysis as explanatory variables in the firms' demand for money function in Jordan SMEs.

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Small and medium-sized enterprises (SMEs) or small and medium-sized businesses (SMBs) are businesses whose personnel numbers fall below certain limits. The abbreviation "SME" is used by international organizations such as the World Bank, the European Union, the United Nations and the World Trade Organization (WTO). In any given national economy, SMEs sometimes outnumber large companies by a wide margin and also employ many more people. For example, Australian SMEs make up 98% of all Australian The role of Small and Medium Scale Enterprises (SMEs) in the world economy have been highly emphasized as the means through which rapid industrialization and other development goals of a nation can be realized. Small and Medium Enterprises have been defined in various ways according to the capital of the enterprise, size ,the number of people employed by the enterprises, the ownership and management of the enterprises and sales volume, all the definitions agree on the common views that small or medium businesses employ few people and are characterized by a relatively small amount of capital and. turnover.

### 2.2 Small And Medium Business in Jordan.

There is no universal definition of small scale businesses. Most small and medium enterprise owners according the study usually consider risk management as an issue relevant only to large companies. The fact that engaging in risk assessment and management requires a certain budget and human resource also hampers their ability to set up a comprehensive RM program. There are limited studies that have highlighted effect of risk management with regard to the financial performance of Small, Medium Enterprises. It is on this ground that this study sought to fill this gap.

### 1.3 Objectives of The Study.

Small and Medium Enterprises (SMEs) is an important sub sector for the Kenyan economy like many other developing countries since it employs about 85% of the Kenyan workforce (about 7.5million Kenyans of the current total employment).