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FINANCIAL CHALLENGES OF SMALL AND MEDIUM-SCALE ENTERPRISES (SMES), IN ANAMBRA STATE, NIGERIA

BEING DISSERTATION PRESENTED TO THE DEPARTMENT OF ACCOUNTANCY, FACULTY OF BUSINESS ADMINISTRATION, UNIVERSITY OF NIGERIA, ENUGU CAMPUS

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IN PARTIAL FULFILMENT OF THE REQUIREMENTS FOR THE AWARD OF MASTERS OF SCIENCE (M.Sc) IN ACCOUNTANCY

SUPERVISOR: PROF (MRS) R. G. OKAFOR

2014
DECLARATION

Ohachosim Celestine Ikem, a postgraduate student in the Department of Accountancy with Registration Number PG/M. Sc/08/53462 has satisfactorily completed the requirements for research work for the degree of Masters of Science in Accountancy.

The work incorporated in this dissertation is original and has not been submitted in part or in full for any other Diploma or Degree of this University or any other institution of higher learning.

All liabilities arising from this study is entirely mine and not of my supervisor and/or the university.

.................................

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This dissertation has been approved for the department of Accountancy, Faculty of Business Administration, University of Nigeria Enugu Campus, by

Professor (Mrs) R. G. Okafor
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Dr (Mrs) G. N. Ofoegbu
(Head of Department)

Professor G Ugwonah
(Dean)
DEDICATION

This work is dedicated to the effort of all owners of small businesses all over the world
ACKNOWLEDGEMENTS

I thank God for the gift of life.

I express my profound gratitude to my supervisor, Professor (MRS) R. G. Okafor, who has given me painstaking guidance and encouragement throughout this research work.

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In recognition of the co-operation that existed among us throughout the programme, I remember some of my Classmates: Osmond Ugwu (our able class rep), Chief Ugwu, Mr Agu Simon, Chris Udigwe, Onyia Gloria, Justine Iorun, Chief C. Nwuba and others that I cannot remember their names at the point of making these acknowledgements.

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Finally, to God I give all the Glory.

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ABSTRACT

The relevance of SME-sub sector in Nigeria’s economy has necessitated the need for empirical investigations into the nature of its financial challenges. This study evaluated the extent accountants can help to ameliorate the financial challenges of SMEs in Nigeria. It made use of questionnaire for collecting data from a sample of 348 selected out of a population of 2688 SMEs in Anambra state of Nigeria. Z-score, Chi-square($X^2$), T-statistics and F-statistics were utilized in testing the hypotheses. Also, by the technique of Ordinary Least Square (OLS), the researcher estimated the group logit (GLOGIT) model specified in the study. Our analyses revealed that SMEs in Nigeria have poor accounting system. It was also found that SMEs’ access to finance depends largely on the quality of accounting information they can generate. The study recommended that SMEs should access the services of the accountant to be able to establish reliable accounting system. Quality accounting information will enhance SMEs’ financial management as well as accessibility of finances.
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CHAPTER ONE

INTRODUCTION

1.1 Background to the Study

Small and Medium-scale Enterprises (SMEs) play very important roles in the process of industrialization and sustainable economic growth (Ogujiuba, Ohuche & Adenuga, 2004; Ariyo, 2005; Ihua, 2009; Aremu & Adeyemi, 2011; Terungwa, 2012). Since the 1960s to date, SMEs are being given due recognitions especially in the developed nations for playing very important roles towards fostering accelerated economic growth, development and stability within several economies (Gunu, 2004; Onugu, 2005; Aremu, 2010). They make-up the largest proportion of business all over the world and play tremendous roles in employment generation, provisions of goods and services, creating a better standard of living as well as immensely contributing to the Gross Domestic Products (GDP) of many countries (Ihua, 2009; Paul, 2010; Ojeka & Mukoro, 2011). In the United States of America, SMEs employ 50% of her workforce, and generate more than half of the nation’s Gross Domestic Products (Audretsch, 2010). In the enlarged European union of 25 countries of the world, some 23 million SMEs provide 75 million jobs and represent 99% of all enterprises (Gunter, 2005). The situation is not different in Africa as research reported by Kongolo (2010) reveals that in South Africa, SMEs account for about 91% of the formal business entities contributing about 51% and 57% of GDP, providing almost 60% of employment.

SMEs sub-sector came into the mainframe of policy formulation in Nigeria owing to its obvious vital contributions (Obamuyi, 2007). Like in the developed countries, SMEs have enabled entrepreneurship activities through which employments have been generated and poverty reduction and sustainable
livelihood achieved (Ogujiuba et al, 2004). It makes up about 97% of businesses in Nigeria and provide on average 50% of Nigeria’s employment, and its industrial output (Ariyo, 2005; Taiwo, Ayodeji & Yusuf, 2012). SMEs have the ability to start small and grow quickly and as well survive through rapid response adjustment in good and bad economic times (Mitchell & Reid, 2000; Nandan, 2010). Government and development experts have, therefore, realised the fact that SMEs possess the needed catalyst to turn the economy around for good (Udechukwu, 2003; Anyanwu, 2003).

However, for SMEs to perform the roles as enumerated above, they need adequate funding in terms of short and long-term loans. Due to the nature of SMEs, funds are always in short supply to them (Srinivas, 2005). It then became necessary that SMEs should be assisted largely by public initiative involving participation of the banking industry (Srinivas, 2005). Government of Nigeria has made elaborate effort to assist the SMEs in their funding problems (Anyanwu, 2003; Terungwa, 2012). According to Olorunshola (2003), the government has been active in the development of SMEs in Nigeria by initiating many schemes and instituting many agencies to help SMEs to overcome their financial challenges.

It should be noted that only few of these attempts to assist the SMEs were successful even though researches revealed that government support had never been lasting (Okpara, 2000; Obor, 2002; Ojo, 2003; Tumkella, 2003). Also records indicate that the performance of SMEs in Nigeria has not justified the establishment of this plethora of micro-credit agencies. This is supported by Odedokum (1981) who noted that in spite of the quantum of credit made available to the manufacturing sector; the contribution of the index of manufacturing to GDP was only 7% between 1970 and 1979. An appraisal demonstrated by Olorunshola (2003) showed that unviable projects were funded which led to massive loan
repayment defaults. This circumstance terminated many schemes which were actually supposed to be revolving. Also, for this, singular reason, some of the agencies become insolvent and some liquidated, for instance, the Nigerian Bank for commerce and Industry (NBCI) suffered major problems culminating in a state of insolvency in 1989. On a general appraisal anywhere, there have been increasing numbers of SMEs in the country since 1970s. The fact still remains that financial challenges of SMEs have not been put under control as it keeps changing forms (Terungwa, 2012).

It can be logically correct to conclude from the above that the financial challenges of SMEs in Nigeria today, have taken the dimension of inaccessibility of funds (Aremu & Adeyemi, 2011). Obstacles of SMEs’ access to funds in Nigeria have not been surmounted because of SMEs inability to generate and use quality accounting information (Richard, McMahon & Holmes, 1991). In the face of poor accounting or non-existence accounting information, good funds management is inhibited. Once the SME commences business operations the nature of its fund management is reflected in the new establishment. Suppose the fund management is inadequate, it will be difficult for the new business to attract additional funds for increased working capital, expansion or diversification. It is based on this reasoning that very crucial and onerous tasks are set before the accountant who is equipped with the skills and theories of business to produce accounting information. It is exigent that financial challenges of SMEs be given passionate attention by business professionals especially the accountant. SMEs financial challenges really entail extensive and constant efforts on the part of the accountant to assist owner-managers to access adequate finances at affordable costs: “A good accountant is the most important outside advisor the small business owner has” (Cornish, 1993). According to the Entrepreneur Magazine Small Business Advisor,
“The services of a Lawyer and other business consultants are vital during specific periods in the development of a small business or in times of trouble, but it is the accountant who, on a continuing basis, has the greatest impact on the business” (Encyclopaedia of Business, 2010). The onerous tasks before the accountant does not get accomplished only by producing adequate accounting information, it proceeded to include all processes to awaken the consciousness of the SME-owners to the proper uses of the information to arrest their financial challenges (Watson, 2003). This work is justified because it has holistic focus (availability, accessibility and management of funds) on the financial challenges of SMEs with respect to the roles of the accountant to overcome these challenges.

1.2 STATEMENT OF PROBLEM
Small and Medium-scale Enterprises in Nigeria die shortly after their establishment and the performances of the surviving few are far below expectations (Osotimehim, 2012). Generally, the failure rate of SMEs in Africa is very high (Adelakun, 2008; Ebiriga, 2011). The SME sub sector has neither been effective enough to create substantial job opportunities nor efficient enough to improve the standard of living of Nigerian populace; unemployment rate is very high and more than half of the population is still living below the poverty line (World Bank, 2001; CIA, 2010; Abu & Abdullah, 2010).

Out of the many specific causes of SMEs’ poor performances and failure in Nigeria, financial challenges appear most prominent (Okpara, 2000). Financial challenges relate to: fund availability, fund accessibility and fund management. The focus of most SMEs is on fund availability and accessibility with little or no attention to fund management. The fact is that they do not know that effective fund management can enhance availability and accessibility of additional fund for both working capital and expansion purposes. Current researches assert that most SMEs
can’t have access to quality funds for their business activities because of poor fund management (Stigliz and Weiss, 1981; Srinivas, 2005).

The question is how can a meaningful fund management capable of combating SMEs financial problems be put in place without a number of basic accounting practices? These practices may include among others; adequate record keeping, material control and effective budgeting. The absence of these basic accounting practices in most SMEs in Nigeria tends to compound their financial challenges. Most SMEs circumvent good accounting practices partly due to time and cost implications and partly due to sheer ignorance. Highlighting on the complications caused by inadequate accounting practices, we note the presence of improper investments in both current and fixed assets by SMEs in Nigeria. SMEs sometimes tie huge investible capital where it is not needed. Inventories are excessively stocked and more credit facility than necessary extended to customers amidst shortage of working capital. Due to inadequate investment planning and supervision, SMEs in most cases embark upon investment in fixed assets whose yield are not commensurate to the huge capital outlays. Also, observed are situations where SMEs do not have good accounting bases for determining their profits. This often results to capital erosion in consequence to excessive withdrawals.

Financial challenges have continued to militate against SME success in Nigeria because SMEs have no habit of accessing the service of the accountant. Adequate accounting practices are necessary for appropriate financial management practices. The accountant is one professional and valuable companion the SMEs hardly realise timely (Larson & Clute, 1979; Watson, 2003). In the emerging business environment, the accountant initiates the system of good financial management, thereby, providing far-reaching remedies for SMEs financial challenges. Most
studies on financial problems of SMEs in Nigeria concentrate on SMEs access to funds and dwell rather too little on the relevance of accounting information in ameliorating financial challenges of SMEs. They do not consider the fact that SMEs’ access to finance tends to be determined by the quality of financial information they can produce (ACCA, 2013). This study emphasizes the relevance of good accounting practices in combating the financial challenges of SMEs in Nigeria.

1.3 OBJECTIVES OF THE STUDY

The general objective of this study was to evaluate the effects of good accounting practices on financial challenges of SMEs in Anambra State.

The specific objectives of this study were to:

1. Examine if accounting practices affect SMEs finances.
2. Investigate the extent SMEs’ access to finance is controlled by accounting practices.
3. Assess the extent SMEs use accountants to mitigate their financial challenges.
4. Ascertain the impact of analysing accounting information on SMEs’ financial challenges.

1.4 RESEARCH QUESTIONS

The research strived to answer the following thought provoking questions.

1. How does accounting practices affect SME’ finances?
2. What is the impact of accounting practices of SMEs on their access to finance?
3. To what extent do SMEs use accountants to mitigate their financial challenges?
4. To what extent do analyses of accounting information help SMEs to overcome financial challenges?

1.5 STATEMENT OF HYPOTHESES

This study postulated the following hypotheses:

1. Accounting practices do not affect SMEs finances.
2. SMEs’ access to finance is not controlled by their accounting practices.
3. SMEs do not access the services of accountants to mitigate their financial challenges.
4. Analyses of accounting information do not help SMES to overcome their financial challenges.

1.6 SIGNIFICANCE OF THE STUDY

This study has the following significance:

Accountants have been acquainted with the nature of SME finances and their accounting needs.

SMEs have learnt the need to access the services of the accountants.

Banks have learnt an accounting-related process of accessing SMEs for loan purposes.

Government have got an accounting-related method of identifying genuine SMEs to benefit from various government schemes in Nigeria.

Academics have been provided with a new, scientific and verifiable process of studying SMEs financial challenges.

1.7 SCOPE OF THE STUDY

SMEs studied in this research are those that meet the features of SMEs as defined by Small and Medium Industries Equity Investment Scheme (SMIEIS) in Nigeria.

The area of business operations of most SMEs surveyed include; trading, service
delivery, manufacturing, construction and agriculture. The scope of financial challenges covered include: finance availability, finance accessibility and finance management.

1.8 LIMITATION OF STUDY
The major limitations of this study are the unavailability of data and the quality of the obtainable data. Due to the nature of SMEs in Nigeria, documentation of secondary data has not become efficient enough to enhance studies of this nature. The researcher understands this and has made frantic effort to overcome this problem and obtained dependable data to work with. However, the dependability is still reliant on the frankness of the SMEs who supplied most of the data used for all empirical analyses in the research.

1.9 Definition of Terms
Under this heading, terms operationalised in this study are explained to elucidate on their special meanings in the research.

Financial Challenges: This is used to refer to the difficulties that the SMEs experience in accessing funds, as well as, in managing the funds accessed for optimal use.

SMEs Finance: All forms of funds at the disposal of the SMEs for business use. Finance includes monies obtained through loans, credit supplies, plough back profits; monies saved by skilful money management, etc. which are available for business use.

Funds availability: This explains the easiness with which funds are provided for SMEs’ use by government, banks or SMEs themselves.
Funds Accessibility: This refers to the convenience with which SMEs obtain and use funds. This study is interested in what controls the accessibility of funds for the SMEs.

Accounting Practices: All activities undertaken by the SMEs to ensure good and dependable accounting system. Accountants should be able to guide SMEs to observe a set of generally accepted accounting practices (GAAPs) to ensure the generation of quality accounting information. The global practice now is that SMEs should observe the International Financial Reporting Standard (IFRS) for SMEs.

Emerging Tasks: This is used to describe the new dimension which the work of the accountant has assumed. This study explains that the work of the accountant does not end in producing accounting information but has included the use of the accounting information in solving business problems which include financial challenges of the SMEs. The work of the accountant has in recent times included financial management.
REFERENCES


CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction
This work has embarked upon this literature review under the following headings; conceptual issues/reviews, theoretical reviews and empirical reviews of financial management practices. Conceptual reviews enhance the description of basic concepts relating to SMEs and SMEs financing. Theoretical reviews x-ray theories relating to accounting practices, bank-SME financial relationship and emergent SME financing needs. Empirical Reviews explore submissions posited by scholars as a result of empirical investigations undertaken by them.

2.2 Conceptual Issues/Reviews

The concept of SMEs
Small and Medium-Scale Enterprises are generally privately owned organisations set-up for the purposes of producing goods or services for profit. The criteria for classifying business enterprises under SMEs differ from country to country (Aremu & Adeyemi, 2011). The identifiable and predominant criteria across the globe include: size of capital invested, number of staff or employees, size of turnover or sales volumes and value of assets (Ezeh, 1999; Bureau of statistics, 2001).

The reliance on the criteria identified above for the categorisation of business enterprises under SMEs still varies across the globe (Ezeh, 1999; ICAN, 2010). There is no compromise as to the exact number of employees, size of capital employed, sales volumes or value of assets that qualify a business enterprise an SME. Relying on the number of employees/staff criterion for instance, some countries describe all enterprises that have less than 100 employees as SMEs,
others are in favour of 50 employees and some expand the net to include all firms who have less than 200 employees (Stanley, 1956; Ekenyon, 1989; ABS, 2001; Ojeka & Mukaro, 2011).

Besides the controversy in defining the SME using the number of employees, there exist difficulties in other criteria. It becomes apparent that for SME to be defined using the criteria; employees, sales volumes, assets employed, capital invested or a combination of the above, care must be exercised to overcome these inherent difficulties. This view was supported by Ezeife (1988) who pointed out that definition based on number of workers may be misleading because owing to improvement in technology, so much money may be involved (say up to 1 billion naira) when only few people are employed. Ezeife (1988) also pointed out that definition based on capital should consider the time and the place. What is regarded as a large firm today may be actually an SME in the very near future and what is considered an SME in developed countries like United States of America may be a large firm in developing countries like Nigeria.

To buttress this fact, we refer to SME definition by the European Union as follows: ‘the new category of small and medium-sized enterprises (SMEs) is made up of enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding 50 million euro, and/or an annual balance sheet total not exceeding 43million euro (Gunter, 2005). The definition by European Union combined the criteria; number of employee, turnover/sales volume and capital employed. Also relying on the same criteria as the European Union, the UK defined SMEs as business organisations which have sales turnover between 6.5m pounds and 25.9m pounds, Net assets between 3.26m pounds and 12.9m pounds and number of employees between 50 and 250 (Lucas, Prowle and Lowth, 2013).
The federal Government of Nigeria in 1990 defined small-scale enterprises for purpose of commercial loan as those enterprises with capital investment not exceeding N2 million (excluding cost of land) or a minimum of N5 million (Aremu and Adeyemi, 2011). Small and Medium Industries Equity Investment Scheme (SMIEIS) defined SMEs as those “enterprises with a total capital employed not less than N1.5 million, but not exceeding N200 million, including working capital, but excluding cost of land and / or with a staff strength of not less than 10 and not more than 300 (Obamuyi, 2007). The definition given by SMIEIS has taken care of major discrepancies by maintaining a level of specification. It is of practical importance to adopt this definition in this work owing to the fact that this definition is used by banks for the purpose of making funds available to SMEs in Nigeria.

**Micro-firms and large firms**

It may be reasonable to ask this question: “where are firms smaller or larger than those firms that go under the umbrella of SMEs categorised?” This has brought to our review the concept of micro-firms and large firms. All establishments that have capital employed less than N1.5 million and at the same time employ less than 10 persons are by the definition of SMEs above micro-firms (Devi & Samujh, 2010). Micro-firms are micro-enterprises which are too small to be categorised under the SMEs. Most sole-traders who operate small shops scattered all over Nigeria, are by definition of SMEs, simply referred to as micro-enterprises. Following the same logic, any enterprise that has capital more than N200 million and at the same time has employed over 300 staff can be referred to as large enterprise in Nigeria. Large firms include: the public liability companies (Plc) and most multi-national corporations. The definition of SMEs has helped us to categorise enterprises
namely; the micro-enterprise, Small & Medium- Sized enterprises and the large corporations.

**The Idea of Book-Keeping and Accounts**

Book-keeping can be defined as the recording of business transactions in a systematic manner so that the financial state of their owners can be ascertained at any time (Hyness, 1937). Okolo (1980) defines book-keeping as the recording of transactions in money and money’s worth. Book-keeping become practically a necessity following the emergent of commerce. In fact, Riahi-Bekoui (2004) traced that the art of book-keeping is preceded by seven conditions. He puts it as follows: “The Art of writing, since book-keeping is first of all a record: Arithmetic, since mechanical aspect of book-keeping consists of a sequence of simple computations: private property, since book-keeping is concerned only with recording the facts about property rights; money (i.e. in completed transactions) since there would be little impulse to make any record whatever if all exchanges were completed on the spot; commerce, since a merely local trade would never have created enough pressure (volume of business) to stimulate men to coordinate diverse ideas into a system; capital, since without capital commerce would be trivial and credit would be inconceivable”.

Commerce which is defined in recent times as trade and aids to trade remains the most necessitating factor of book-keeping and accounting. Of all the above listed conditions, commerce popularized the usefulness of book-keeping. Riahi-Belkaoui (2004) was of the opinion that the invention of this important science accounting can be ascribed to the first considerable merchants. He posited that there are none who have a fairer claim to presidency in point than those of the Arabs who were known to be earliest great merchants in history. These Arab merchants were tradesmen in sole proprietorship and partnership businesses, presumably the
present day SMEs. They brought trading ideas to the Egyptians in spite of the Egyptians glorious appearance in commercial world. It is believed that book-keeping art was also transferred to them as they trade with these Arab merchants (Riahi-Belkaoui, 2004).

**Double Entry Book-keeping**

Double entry is the principle behind scientific book-keeping. The principle explains that a debit entry must have a corresponding credit. It logically holds that if there is a giver, there must be a receiver. The method of double entry is known as the Italian book-keeping. Despite the fact that it is referred thus, it is said to have been invented by the Arab merchants. It became the Italian book-keeping because after the notorious attacks of the Barbarians, Italy became a world power hosting the largest trading centres in the world. The double entry book-keeping became pronounced in Italy. It is; therefore, logically right to say that double entry book-keeping had been existing before Luca Pacioli’s publication Summa de Arithmetical Geometria proportioni et proportionalita in 1494. The first Double entry books known to exist are those of Massari of Genoa, dating back from the year 1340 (Riahi-Belkaoui, 2004). Nobody contests the fact that Luca Pacioli’s book popularized double-entry and Accounting in General.

**The meaning of Accounting**

Accounting is the art of recording, classifying and summarizing in a significant manner and in terms of money, transactions and events which are, in part at least of a financial character and interpreting the results, thereof (AICPA, 1989). Accounting has evolved from simple book-keeping. Also defined as the science of recording, interpreting financial records, accounting has become the often and on language of business (Okolo, 1980). It has emerged an indispensable tool of
business. It is this unique significance of accounting that has placed the accountant in the centre of attraction for all stakeholders in any organization whatsoever.

**Generally Accepted Accounting Principles (GAAPs)**

Generally Accepted Accounting Principles (GAAPs) are a basic set of rules that are supposed to be followed across all stages of accounting. Following the enlargement of business world, stakeholders in business establishments grew and it became necessary to standardize the system of accounting so that facts can be recognised and evaluated in an aligned procedure. Unlike the known sole-proprietorship and partnership businesses, where the users of accounting information are limited and in most cases involved in the day-to-day activities of the business, the evolution of modern business demands a predetermined accounting system to serve the interests of the various stakeholders who may not be part of the management. Upon this obvious need, a set of generally accepted accounting principles (GAAPs) is developed. This is the outcome of accounting bodies at both local and international levels.

In Nigeria there is the Financial Reporting Council of Nigeria (FRCN) which replaced the National Accounting Standard Board (NASB) (FRN, 2011). At the international level, there is the International Accounting Standard Board (IASB) which replaced the International Accounting Standard Committee (IASC) (Izedonmi, 2014). The Financial Reporting council of Nigeria issues Financial Reporting Standard (FRS) which replaced the Statement of Accounting Standard (SAS). The International Accounting Standard Board (IASB) issues the International Financial Reporting Standards (IFRSs) which replaced the International Accounting Standard (IAS). The FRS guides the practice of accounting in Nigeria while IFRSs guides the practice of accounting across the
boarders. The purpose of standardization is to enable a quality for reporting financial statements of companies. It is to ensure that financial Statements can be interpreted in the same way across the globe. A good number of countries have adopted the IFRS including Nigeria.

Only but recently none of the accounting bodies have thought it right to have a separate accounting standard for Small and Medium –scale Enterprises due to its unique characteristics. The International Accounting Standard Board having recognized the burden of financial reporting on the SMEs, has published a proposed IFRS for SMEs referred to as statement of GAAP for SMEs (IASB, 2007). The purpose of IFRS for SMEs as stated by the chairman of IASB is as follows:

“Our goal has been to produce a standard for use by small and unlisted companies that offers the companies the comparability of full IFRS while reducing the burden on the preparing company. When completed, the SME standard will make the accounting requirements more to smaller preparers in both developed and emerging markets with this publication, we are now actively seeking the views of companies, banks, the audit profession, and other interested parties as part of a broad consultation to see if we’ve taken out too much or not enough or if we’ve got it about right”.

On the list of companies that should use the IFRS for SMEs, IASB (2007) states that the IFRS for SMEs is intended for entities that do not have public accountability. According to the IASB (2007), an entity has public accountability (and therefore should use full IFRS) if:

- It has issued debt or equity security in a public market; or
• It holds assets in a fiduciary capacity for a broad group of outsiders, such as a bank, insurance company, securities broker/dealer, pension fund, mutual fund or investment bank.

It should be seen that the definition of SME adopted in this work fall into the category of entities that should use the IFRS for SMEs. Part of the emerging task for the accountants is to popularize the IFRS for SME in Nigeria. The two accounting associations; the Institute of Chartered Accountants of Nigeria (ICAN) and the Association of National Accountants of Nigeria (ANAN) should ware global outfits and train their members to serve the SME needs.

It is often the practice of banks and other funds providers to evaluate the risk of SMEs which they have not had much relations with by comparing it with another SME of equal strength. It usually poses difficult task to identify an SME of similar features with the SME in question. This has often compelled the banks to associate the highest level of risk to all SMEs while evaluating the viability of extending loan facility to the SME even though all SMEs in practice don’t operate at the same risk level. Part of the effort of the IFRS for SMEs is to put this problem to a paid with a standard set for the reporting of the SMEs’ financial statements, it can be picked and analysed in the same manners a financial analyst would do to quoted firms.

**Financing SMEs:** The enhancement of SMEs’ abilities to acquire funds for their business activities is called financing SMEs. The need to finance SMEs is obvious. Its role in every economy cannot be over emphasized (Ariyo, 2005; Terungwa, 2012). SMEs are vital for economic growth and development in both industrialised and developing countries, by playing a key role in creating new jobs (OECD, 2006). Financing is necessary to help them set up and expand their
operations, develop new products, and invest in new staff or production facilities. Many small businesses start as an idea from one or two people, who invest their own money and probably: turn to family and friends for financial help in return for a share in the business. But if they are successful, there comes a time for developing SMEs when they need investment to expand or innovate further. That is where they often run into problems, because they find it much harder than larger business to obtain financing from banks, capital markets or other supplies of credit.

Sources of finance to SMEs: Two fundamental concepts of SMEs’ finance are; the formal and the informal forms of financing. The **FORMAL FORMS OF FINANCING**: The formal forms of financing are the ones regulated by government. Gelina (1998) and Aruwa (2004) opine that the most popular sources of formal finances are the commercial bank and development bank for enterprises. Kauffman (2005) explains that SMEs access to formal finance is poor because of the high risk default among SMEs and due to inadequate financial facilities. Small business in Africa can rarely meet the conditions set by financial institutions, which see SMEs as a risk of poor guarantees and lack of information about their ability to repay loans. The financial system in most of Africa is under-developed however and so provides few financial instruments. Capital markets are in their infancy, shareholding is rare and no long-term financing is available for SMEs. Non-bank financial intermediaries, such as micro credit institutions, could be a big help in lending money to the smallest SMEs but they do not have the resources to follow up their customers when they expand.

The **INFORMAL FORMS**: The informal forms of financing are not regulated by the govt. Main sources of informal finances are the retained earnings, loan associations, and other informal forms like loans from family, friends’ co-operation, private placements, joint ventures, among others. The informal units are
more readily available sources of financing SMEs (Ekpoyong and Nyong, 1992; Terengwa, 2012). The problem with informal source of financing is that they are unpredictable, not very secure and have little scope for risk sharing because of their regional or sectoral focus (Kauffman, 2005). The unpredictability of the informal sources of funds is the main reason why it is not taken serious but no one can undermine the fact that the informal sources remain most accessible source of financing to SMEs all over the world.

**Problems of SMEs’ Financing:** The main problems of SMEs’ financing according to Terungwa (2012) are; the cost of capital, Risk perception, the inappropriate terms on bank loan and shortage of equity capital. These problems continue to recur because of information asymmetries. By definition, information asymmetry is a situation where business owners or managers know more about the prospects for, and risks facing their business than do lenders. Where information asymmetries exists bank lending theory predicts that lenders may respond by increasing lending margins to levels in excess of that which the inherent risks would require. Bank lending theory also suggests that banks may also curtail the extent of lending-credit- even when SMEs would have been willing to pay a fair risk-adjusted cost of capital. The implication of raising interest rates and/or curtailing lending is that firms will not be able to finance as many projects as otherwise would have been the case. Information asymmetry is more acute in case of SMEs because their relative size makes them economically unattractive to banks since they are unable to accurately gauge the level of risk involved in lending to SMEs (Ohanga, 2005, Terungwa, 2012).

**Increasing SME Access to Finance: A Four Pronged Approach**

SMEs’ financing problems have received the most tremendous research effort from researchers (Terungwa, 2012). This is due to the obvious fact that SMEs relevance
in every economy cannot be overemphasized. Kauffmann (2005), proposed four ways to increase SMEs access to finance. The four pronged approach are discussed below.

*Increasing business conditions*: Proper information, a key to deciding whether to make a loan, would be enhanced by adopting clear accounting standard, setting up independent, competent and reputable accounting firms and creating more credit bureaux supplying data on the solvency of firms (Kauffmann, 2005). An impartial legal system that can help settle contract disputes, commercial law and drafting and classifying land titles, as well as efficient bankruptcy procedures, are vital for growth of the business sectors. A country’s tax laws can either coax small businesses into formal sector of the economy or keep them out of it. Government should also make sure that they pay SMEs promptly, since public contracts are vital to the financial security of these firms.

*Helping SMEs meet the requirements of formal financing*: Apart from the need to boost SME capacities, some financial instruments can help provide missing information or reduce the risk stemming from some SMEs’ lack of transparency. Franchising, which is very popular in Southern and East Africa with the encouragement of South Africa, allows use of a brand name or know-how reduces the risk of failure. Warehouse-receipt financing (in South Africa, Kenya and Zambia) guarantees loans with agricultural stocks. Other financial instruments, such as leasing and factoring can reduce risk effectively for credit institutions but are still little used in Africa. Credit associations that reduce risk by sharing it are more common. They help financial institutions choose to who to lend, by guaranteeing the technical viability of projects, and sometimes providing guarantees. But growth of these bodies is limited by the lack of organisation among SMEs in Africa and by their focus on certain sectors and geographical
areas. Government and donor sources have thus preferred creation of guarantee funds to ensure repayment in case default. In several countries, especially in central Africa, this has not worked since provision of a guarantee has meant less rigorous choice of investment projects and a lower rate of debt recovery. Elsewhere, notably in Mozambique, borrowers and financial institution have worked together to maintain a good rate of recovery and to reduce interest rates.

*Helping the financial system more accessible to SMEs: Most African financial systems are fragmented. The “missing middle” in the pattern of size of firm is matched by one in the range of financing available. Lack of funding for SMEs has partly been made up for by micro-credit institutions, whose growth is due to the flexible loans they offer small businesses. In Angola, Novobanco provides loans free of bank charges, without a minimum deposit and with informal guarantees (property assets and a guarantor), as well as permanent contact with loan managers. Though adapted to loan needs, however, micro-credit institutions remain fragile and modest-sized. As well as lacking trained staff, micro-credit institutions face limited expansion because of their limited funds. Their mainly short-term finance means they cannot easily turn the savings they collect into medium or long-term loans. They are also up against the cost of refinancing through the formal banking sector and no refinancing access to either by the central bank or by venture capital.

Micro-credit institutions could be put on a firmer financial footing by developing and adapting long-term savings products that exist elsewhere, such as life insurance and home-saving plans, and encouraging the setting up of specialised refinance banks such as Mali’s “solidarity bank” (Banque malienne de solidarite), or working more closely with the formal banking sector (Benin’s SME support organisation PAPE and the local Bank of Africa). Some countries (such as Kenya)
have dealt with the lack of funding by supporting growth of smaller commercial banks or (in Ghana) of rural banks, so as to bring traditional banks and SME closer geographically and business-wise. South Africa passed two laws in early 2005 to expand the banking system to include savings and loan institutions (second-tier banks and co-operative banks (third-tier banks) while easing banking regulations so the newcomers could still be flexible in providing loans. In many countries, commercial banks are also setting up their own micro-credit services. Removing the obstacles to access for SMEs’ to finance requires that commercial banks, micro-credit institutions, community groups and business development services (BDS) work closely together. Pushing for agreements between financial bodies and BDS suppliers will help make up for capacity and reduce cost by more efficient division of labour. The BDS supplier makes the initial choice of projects on a purely technical basis and the credit institution look at financial viability. Making loans to intermediaries (NGOs and federations of SMEs) with the job of allotting funds to members can also help cut administration costs. Solidarity between banks, especially setting up inter-bank financing to (as in Nigeria) pool money to be invested in SMEs, reduces the extra risk of lending to SMEs, as well. Working with banks boosts the financial viability of micro-credit institutions and can also help informal financial bodies to move towards the formal sector.

*Expanding the Supply of Financing through the Non-financial Private Sector:* Financial institutions are not the only source of money for SMEs. Apart from remittances by nationals working abroad, which is a key boost to private-sector growth, the interdependence between SMEs, large firms and sectoral “clusters” is a major potential source of financial, as shown in Asia and Latin America. Big firms can do a lot to help SMEs get finance more easily by
transferring resources (money and factors of production) and guaranteeing SME solvency with financial institutions. Links with major companies can also help SMEs get export credits, which are especially important in countries with weak institutions, since commercial partners are better informed than other creditors (especially financial institutions) about the ability of their customers to repay debts. Export credits have been proved useful in Zambia’s agro-food industry. Subcontracting is still uncommon in Africa, but has grown rapidly in South Africa since 1998, though there is increasing scepticism about it because it may confine SMEs to low-skill informal activities. Clusters of SMEs, which are very active in Asia, enable member-firms to seek finance together, provide collective guarantees or even set up their own financial body. The threat of expulsion from the cluster ensures that promises are kept which allows the network to overcome shortcomings in the legal system. Frequent interaction with financial authorities, as well as the role that reputation plays in the cluster, can greatly increase confidence between firms and financial institutions and thus make it easier to get loans and lower rates of interest. Working together also means firms can get supplier credits and can borrow from other when necessary, which reduces general costs. Such clusters, however, are very little developed in Africa and are concentrated in South Africa, Kenya, Nigeria, Tanzania and Zimbabwe.

**SMEs’ Financing Framework:** We can propose a framework for SMEs financing. That is tracing the processes of funding the SMEs and identifying major determinant of SME financing. This work draws inspiration from both theoretical and empirical literatures reviewed in this work for the proposed framework shown below in figure II. The SME-operator needs finance to enhance working capital, expand existing business or diversify. He must build information about the existing
business. The zeal and accuracy with which the SME aggregates this information will determine whether the SME will get any
Fig. 2.1 - Financing Framework of SMEs

Source: Researchers’ Design
form of credit from both the formal and informal sources of fund. This is because according to Terungwa (2012), the financial system in Nigeria, is not in short supply of liquidity, but banks have been very reluctant to grant loans to SMEs, which they regard as high-risk sector. If the SMEs are able to present the information in such order as would enable the source unit to evaluate the risk or the vibrancy of the SMEs, the risk perception of financiers may reduce and loans may be made available to the SMEs. It follows that the source units receive the packaged information and use their yardsticks for adequate assessment. The informal units’ methods of assessment are actually not empirical. Some are simply based on the present or past relationship between the SME-operator and the lender while some may be based on the seemingly affluence or past exploits of the SME-operator. However, the formal units (e.g. the banks) use different methods of assessment. Some of these assessment methods are identified in the theoretical review of this research and most of them were founded on accounting information.

**The Accountant and SME Finance- The task ahead**

From the diagram describing the SME financing framework which is proposed in this research, it can be identified that business information is at the centre of business activities. This signifies that both the formal and the informal units require accurate information about the SMEs to enable them undertake the needed assessments. The ACCA (2013) asserts that “all financial intermediation relies on four raw materials: information, collateral, control, and risk appetite. Many small businesses, however, struggle to provide collateral or personal guarantees and most SME owners are unwilling to give up control of the business to outsiders (in the form of either equity shares or covenants). This means that, in comparison with large businesses, SMEs’ access to finance tends to be determined more by the quality of financial information they can produce and the degree to which
individuals, institutions and government are willing to take the risk of financing them. In countries with a stronger supply of financial information and stronger provisions for creditor protection, SMEs are more likely than in countries with weaker disclosure environments to be able to source all the finance they need, and the financial system is better at distinguishing between better and worse risks… ”.

For the formal units (apart from requiring the SMEs to produce collateral facilities) the assessment process requires much of the accounting information. This is where the accountants’ tasks begin in helping the SMEs aggregate the information that may be needed by the lenders.

SMEs financial challenges continue to get complicated, defying the efforts of government and their agencies simply because SMEs have not been able to take care of the problem of information asymmetries. The fact is that most SME-owners see their businesses as their private affairs and therefore owe no accountability to any one. It is understood from the problem statements that partly because of the stated notion and partly because of ignorance, good business practices are circumvented or disregarded. Much of these good business ethics derive their gravity from some generally accepted accounting practices (GAAPs). The religious observation of these accounting practices yields quality accounting information. It is revealed earlier that those banks and other financiers, even suppliers and intending co-owners (who will be committing their money) need accounting information to evaluate the vibrancy of the SMEs. It could be seen that the accountant is unavoidably important at this junction. The tasks before the accountant here start with designing the accounting systems. It should also be noted that the SMEs on the advice of their accountant must establish a system of dependable internal control. It is in the presence of a working accounting system and dependable internal control that the real tasks of the accountants begin. The
aggregation of accounting information commences from the crude stage of capturing simple business transactions. This is normally referred to as bookkeeping stage. At this stage, the accountant ensures that all receipts are kept (both purchases and sales receipts), subsidiary books are prepared and entries are adequately posted to the ledger in their individual accounts. The accountant could undertake some works before getting to this stage. In a manufacturing firm for instance, there is need to determine cost of production and of course determination of selling prices of the products of the SMEs. It is unassuming that most SMEs believe they can undertake all these all alone. They do not accept the fact that the efficiency of the book-keeping stage determines accuracy of the accounts reported by the accountant. Most SMEs only seek to access the services of the accountant at the reporting stage thereby making the work of the accountant a very difficult one. This is because before arriving at this stage, information which would ensure effective financial reporting would have been missed due to lack of skill. This is called the missing gap. The SMEs feel that because they are legally required to present accounts for some reasons, especially for compliance (e.g. tax purposes), that it is at this stage that they need the services of the accountant. It, therefore, seem that SMEs access the services of the accountant for compliance purposes only but this is not sound practices to achieve efficient financial management which is sine qua non for overcoming their financial challenges.

The emergent task for the accountant commences after the accountant has accomplished a good financial statement. These are activities after the reporting stage. The analysis of the financial statement in pursuance of further firm’s objectives is an exercise the SMEs may not be able to attain without the accountant around them. There may be need to undertake ratio analysis to enhance managerial performance. Other activities that enhance scientific management like; inventory
planning, working capital management, budgeting and investment planning, labour performance evaluation, among others, may not be easy ones without the accountant. The accountant is that professional that the SMEs need to be in touch with on regular bases.

2.3 Theoretical Reviews
Theories relevant to this work are reviewed under two headings, namely; those relating to accounting practice and those relating to bank practice / bank-SME relationship towards external funds provision to SMEs. Those relating to accounting practice include; proprietary theory, entity theory, fund theory and agency theory. Those relating to Bank practice/Bank-SME relationship include; Bank capital channel model, Bank capital constraint model of lending behaviour, Financial Statement Rule, Asset Based Rule, Credit Scoring and Relationship Lending. Other models from emerging economies include; Indian model, Bangladesh the Gramen model and Brazilian model. Some emergent theoretical underpinnings relating to SME financing are discussed under this heading.

Proprietary theory: RiahiBelkaoui (2004) explained that proprietary theory sees the entity as the agent, representative or arrangement through which the individual entrepreneurs or shareholders operate. The view point of the proprietor groups as the center of interest is reflected in the ways in which accounting records are kept and financial statements are prepared. The primary objective of proprietary theory is the determination and analysis of the proprietor’s net worth. Riahi-Belkaou (2004) states that for purpose of proprietary theory the accounting equation is stated as follows;

Assets-Liabilities = Proprietor’s Equity.
The proprietary theory sees the proprietor as the owner of all the assets of the entity – the liabilities which are negative assets are provided by the external people, e.g. the banks. The proprietary theory may be said to be asset ‘centered’ and consequently, balance sheet oriented. Assets are valued and balance sheets are prepared to measure the changes in proprietary interest or wealth. The revenue and expenses are considered to be increases or decreases respectively in proprietorship that do not result from proprietary investments or capital withdrawal by the proprietor. Thus, net income on debt and corporate income taxes are expenses; dividends are withdrawals of capital.

The proprietary theory’s relevance in SMEs’ financing is not questionable. The prospective capital provider, for example, the bank, may want to know the extent the proprietor’s equity covers the financial need of the business. The proprietor’s equity is no doubt the collateral for further funds that can be accessible by the SME operator. The proprietary theory like the residual equity concept (Staubus, 1959) focuses on the determination of the proprietor’s equity as the main objective of accounting. Most SMES’ accounting follows the proprietary theory because their businesses are not seen as being different from their private affairs. Capital providers may be considering other issues outside the balance sheet e.g. personal commitment, like marital status, reputation of the SME-owner, among others.

**The Entity Theory:** The entity theory views the entity as something separate and distinct from those who provide capital to the entity. Riahi-Belkaoui (2004) posited that the business unit rather than the proprietor is the centre of accounting interest. The business unit owns the resources of the enterprise and is liable to both the claims of the owners and the claims of the creditors. Following this theory, the accounting equation is:
Assets = Equities

Assets = Liabilities + Stockholder’s Equity.

Assets are resources accruing to the entity; equities represent sources of the assets and consist of liabilities and stockholders’ are equity holders, although they have different rights with respect to income, risk, control and liquidation. The entity theory provides the framework that income taxes and interest on loans, debentures, are distributions of income, just like the payment of dividend to ordinary and preference shareholders.

The entity theory applies mostly to corporate firms that are meant to be distinct from its owners. However, modern business involvements have made it possible for SME to be body corporate in the form of private limited liability companies. Accounting functions following this theory is to present the books of the accounts to show that the business is completely different from the owners. It helps the prospective capital providers to focus attention on the worth of the business as an entity while making funds available to the SMEs. This is because the owners of the business only suffer that which they have invested in the case of liquidation. The owner’s private assets are not part of the business and cannot be used to settle the obligations of the business.

The Fund Theory: This basis of accounting is neither the proprietor nor the entity, but a group of assets and related obligations and restrictions, called fund, that governs the use of the assets. Therefore, the fund theory views the business unit as consisting of economic resources (found) and related obligations and restrictions regarding the use of these resources. The accounting equation is

Assets = Restriction of Assets.
The accounting unit is defined in terms of assets and the uses of which these assets are committed. Liabilities represent a series of legal and economic restrictions on the use of the administration and appropriate use of assets.

Found theory is useful to government and governmental organization who maintains specific funds. However, SMEs also maintains specific fund through the process of domiciliation of cash proceeds in project financing (ICAN, 2009). The accounting focus is the stream of income accruing to particular provider e.g. Bank, therefore, while providing funds to the SME, the financier evaluates the viability by looking at the expected stream of incomes of the project.

The agency theory: The agency theory is concerned with how agency affect the form of contract and the way they are minimized, particularly, when contracting parties are asymmetrically informed (Obamuyi, 2007). Lenders normally don’t know the borrowers in persons. The process as in the diagram below: shows that banks and other financial houses are the agents of the lenders.

Lender (Depositors) ─────→ Bankers ---- SMEs (Borrowers)

Problems likely to arise due to agency theory include systematic bias, among others (Akerlof, 1970; kitchen, 1972; Fracer, 2004; Srinivas; 2005). Lenders are imperfectly informed about the characteristics of potential borrowers, and it may be impossible as a result for lenders to distinguish ‘good’ borrower from ‘bad’ ones. This also implies asymmetries of information (Obamuyi, 2007). Akerlof (1970) argues that small businesses, especially in developing countries, are regarded as “high – risk”, and the level of risk associated with the riskiest small business tends to be applied to all small businesses.

There are also relevant models based on agency framework which banks who provide finance for the SMEs build their practice. These models also provide
theoretical base for this research. They include bank capital channel model, capital constraint model and model of lending behaviour (Obamuyi, 2007). The bank capital channel views a change in interest rate as affecting lending through bank’s capital, particularly when banks’ lending is constrained by a capital adequacy requirement. Thus, an increase in interest rates will raise the cost of banks’ external funding, but reduce banks’ profits and capital. The tendering is for the banks to reduce their supply of loans, if the capital constraint becomes binding. However, banks could also become more willing to lend during certain periods because of an improvement in their underlying financial condition. This bank behaviour is explained by the capital constraint models. Basically, banks are subjected to both market and regulators generally require banks to maintain capital at not less than a stated fraction of the bank’s total assets. For instance, banks are expected to meet the capital adequacy requirement of Basel Accord of ten percent. Also in Nigeria, banks are expected to maintain a minimum of 40 percent liquidity ratio of total deposits. Thus, the ability of banks to grant loans is constrained by the amount of financial resources at their command, based on the capital requirement.

Owing to information asymmetries which the research has reviewed above, Ogujiuba et al, (2004) enlisted some lending rules by the banks to accommodate the aberrant characteristics of SMEs and their owners. These rules includes; the financial statement Rule, the Assets-Based Rule, Credit scoring and Relationship lending

**Financial Statement Rule:** This lending rule places emphasis on evaluating information from the firm’s financial statements. The decision to lend and terms of the contract are principally based on the strengths of the firm’s balance sheet. Financial statement lending is best suited for relatively transparent firms with certified audited financial statements. Thus, it is likely to be the rule of choice for
lending to large firms. But when adapting this rule for small firms, the firms must be ones with long histories, relatively transparent transactions and strong audited financial statements (Berger & Udell, 2001). This calls for effective book-keeping and quality accountants’ information.

**Asset-Based Lending Rule:** The most apparently guaranteed form of lending to SMEs is assets-based lending. This lending technology bases its decision to lend on the quality of the available collateral. Thus, type of lending requires constant monitoring of the business and this can prove to be expressive. The collateral in this case may be accounts receivable, inventory, fixed assets, et cetera; this is why the bank has to intensively monitor the turnover of these assets. This is the most common lending rule for SMEs in Nigeria.

**Credit-Scoring Rule:** This is a summary statistics about the borrowers expected future loan performance (Feldman, 1997). In fact, credit scoring assumes that credit analysis ultimately determines that the personal credit history of small business owners is highly predictive of the loan repayment prospects of the business (Berger, Frame & Miller, 2002). Rutherford (1995) observes that although credit scores have been used for sometime now in the United States in underwriting consumers’ loans, this lending approach has only been recently applied to small commercial credits which have been though to have non-standardized documentation and to be two heterogeneous. The method for the use of credit scoring involves attaching heavy statistical weights to the financial conditions and history of the principal owner given that the credit worthiness of the owner and that of the firm are closely related for most small business (Feldman, 1997, Mester & Kalz, 1997).
**Relationship Lending Rule:** In relationship lending, the lender bases its decision to lend in substantial part on proprietary information about the firm and its owner through a variety of contacts over time. This information is obtained through the provision of loans (Peterson & Rajah, 1994; Berger & Udell, 1995) and deposits and other financial products (Nakamara, 1993; Cole, 1998). Additional information may also be gathered through other members of the local community, such as suppliers and customers, who may give specific information about the firm owner or general information about the business environment in which they operate, importantly, the firms’ financial statements, and collateral and credit scores. Empirical studies have proved that relationship lending affects the pricing and availability of credit (Cole, 1998; Elsas & Krannen, 1998; Di Salvo & Ferm, 1998). A stronger relationship measured in various ways is empirically associated with lower interest rates for the firms (Berger & Udell, 1995; Harluff & Koiting, 1998). Berlin & Mester (1998) also report that relationship lending provides greater protection against the interest rate cycle.

However relationship lending involves the role of agents in gathering information and this could add extra costs to the banks. There is still a gap in the empirical literature as to how to determine how relationship lending and how the organizational structure of the banks aid their ability to deliver. It is also necessary to determine how recent changes in the economic environment are likely to affect the availability of credit to small businesses.

**Other Models of Funding SMEs:** This research identifies other models of SMEs lending which exist in foreign countries which have been considered relevant in this study. They include; Indian model, Bangladeshi- the Gramen model and the Brazilian model (Ogujiuba, Ohuche & Adenuga, 2004).
**Indian Model:** The basic principle guiding the funding of SMEs in India is that the government regards small business as the “egg” that hatches big business. Apart from adequate incentives, the government supports SMEs by bulk purchasing their products and retailing them both for the domestic market and for exports. To facilitate their access to bank credits, the government issues SMEs LPOs. Banks accept such contract papers as collateral. When small business bid for government contracts, big businesses must bid 15% less than small businesses for them to supply government needs. Payments are promptly made to the SMEs and this encourages their growth.

**Bangladeshi – the Gramen Model:** This is developed by Professor Yunus Mohammed. In this model, banks target potential borrowers for its core operations and form them into groups then soft loans are made available to these SMEs, repayable within a specific period before the scheme. With this system there is a subtle pressure from other SMEs that are members of this strategic core on the benefiting group to repay so that others can benefit from the scheme. This has introduced healthy capitalization among SMEs in Bangladesh through factoring the credibility of the borrowers.

**The Brazilian Model:** The main thrust of the Brazilian model is that apart from heavy funding and subsidies, the government provides infrastructure in an area and encourages the cluster of industries in such areas. The SINOS VALLEY shoe cluster industries in Brazil have revolutionized the Brazilian shoe industry. For the past 30 years, over 500 SMEs that produce shoes are located there. Today Brazil is the world’s third largest shoe exporter.
2.4 Empirical Reviews of Financial Management Practices

Empirically, it has been demonstrated by a number of studies that the accountant possesses the skill with which any meaningful financial management can be instituted in any organization (Brean, Scuilli & Calvet, 2003). Studies have also shown that sound financial management is crucial to survival and growth of small business (Mamahon & Holmes, 1991; Gorton, 1999). The fact that high rate of small business failure is attributed to poor or careless financial management has lain itself to empirical evidence. Effective financial management can only be instituted in the presence of quality accounting information. Potts (1977) states that the clearest and most startling distinction between successful and discontinued small businesses lie in their approach to uses which can be made of accounting information. Accounting information is not a mere fabrication of the accountant; it is actually the results of business undertakings of the SMEs. This would mean that the accountant should be aware of the business activities and ensure that relevant ingredients are not dropped on the way. This work would, therefore, review empirical literature on the practices of some successful SMEs with the aim of finding out what has ensured their financial breakthrough.

DeThomas and Fredenberger (1985) carried out a survey of some progressive 360 SMEs in Georgia and find out that they have installed and used very effective accounting information systems. The survey reveals that the SMEs have high standard of financial recordkeeping. Around 92 percent of respondents had some form of recordkeeping beyond check stub deposit receipts. It is quite obvious that the success of the SMEs studied is attributed to their accounting systems which were very effective in line with this, is the finding of D’Ambose and Gasse (1980) who studied the utilization of formal management techniques in 25 small shoe manufacturers and 26 small manufacturers in plastics industry in Quebec Canada.

It is briefly highlighted at the introductory part of this review that improved accounting information systems enhance the quality of financial reporting. Richard et al (1991) opines that improved accounting systems due to uprising in computerising accounting systems following innovations in manufacturing affordable computers in recent times has elevated the standard of financial reporting in small businesses in North America. Consequent upon the installation and use of an accounting information system, satisfactory aggregation of the business activities is achieved in forms of records. This has enhanced financial reporting. DeThomas & Frederberger (1985) found that 81 percent of the small businesses in their survey produced financial statements in the forms of balance sheet, income statements, and fund statements, among others. There are others who include in their financial reports, the cash flow summary, others operating summaries and bank reconciliation statements. There are more obvious evidences that adequate accounting information system enhances the regularity of financial reporting. Thomas and Evanson (1987) found among a study of 398 small
pharmacies located in the states of Michigan, North Carolina, Nebraska Rhode Island and Washington that income statements and Balance Sheets were prepared at least quarterly by 62.5 percent of the respondent and annually by 32.1 percent. Thomas and Evanson (1987) reported that over 85 percent of the respondents indicated that an outside accountant prepared the financial statements on their behalf. This is further evidence that good accounting systems prepare the grounds for effective financial reporting.

It is obvious that the quality of accounting information has improved as depicted in the review above but empirical evidence shows that the use of this information is still limited. Richard et al (1991) noted that in contrast to the amount of information available, the actual use made of financial reports by owner-managers is rather limited. Evidence provided by Lindecamp (1983) in the United States of America on the analysis and use of financial statement of 102 owner-managers of retail stores in Mississippi supports the assertion. About 23 percent reported that they analysed a detailed breakdown of their figures on a frequent or regular basis. However, 60 percent indicated that they do not maintain up-to-date figures on the contribution to profit of individual products or product lines. A little 7 percent seldom or never compared their firm’s performance with industry figures. Over 50 percent of respondents did not appear to understand the meaning of debt/equity ratio, and 59 percent did not know the value of this ratio for their firm. Also, DeThomas & Fredenberger (1986) reported in their survey that only 11 percent of the respondents use financial statement information as part of their normal process of managerial evaluation, planning and decision-making, although 61 percent of the respondents felt the statements provided the information they required for planning and decision-making. Only a small proportion of businesses (2 percent) employed financial ratio analysis and few made mere simple historical
comparisons. Even though it was not possible to demonstrate a significant association between the number and frequency of use of financial rates and small business profitability or survival, it is hypothesized that this may have been due to a lack of sophistication in financial ratio interrelation on the part of owner-mangers which prevented usage from making a discernible difference (Thomas & Evanson, 1987).

It is also noted that small businesses have very poor working capital management traditions. A study of small businesses in Northern America, show that they have no formal techniques of determining the level of cash balances (Anvari & Gopal, 1983). This would mean that there are chances of SMEs keeping more cash than they actually required or otherwise. Also, Grablowsky and Rowell (1980) in a survey found that small businesses have poor credit management. In fact, they explained that they see accounts receivable as something that is exogenously controlled. Only few small businesses among those who are included in the survey employed credit officer. In the same way Grablowsky (1978, 1984) obtained enough empirical evidence to affirm that small businesses do not view accounts payable as a source of finances for their businesses. They only accept cash discounts when it is available and do not make effort to compare the cost taking advantage of cash discount with the cash discount itself with regards to their cost of capital. Grablowsky (1984) further concludes that small businesses rarely use formal techniques for inventory management. For instance, they have poor habit of using quantitative techniques like economic order quantity. The fact is that most SMEs accounting systems were not able to provide information on inventory turnover, reorder points, ordering costs or carrying costs. The capital budgeting practices of small businesses is also very low. Grablowsky & Burn (1980) found that the level of understanding and use of more advanced capital budgeting policies
and techniques were low. Richard et al (1991) explained that approval for capital budgeting in SMEs are simply based on necessity, this is contrary to large firms who have yearly annual capital budgets.

Generally empirical evidences available in literature from advance countries reveal that SMEs’ use of accounting information is very poor. However, due to improved accounting systems owing to the increase in the use of computers and software applications, the quality of accounting information has improved tremendously.

Mamahon & Holmes (1991) expressed the view that the SMEs should be encouraged to use software accounting package as it enhances the accounting discipline. This is evident in the study undertaken by Gorton (1991). In the study, a comparative UK study of SMEs that used financial management techniques and those that didn’t found that out of 366 SME respondents who use financial plan that over two–thirds maintained a Computerized Accounting System (CAS). On this Gorton (1991) quantified the importance of planned financial management through the setting of financial plans and the maintenance of comprehensive accounting systems. There is, therefore, a relationship between the use of CAS and strategic orientation (Gorton: 1999; Smith, 1999). The use of CAS instils controls in the SMEs. McMahon (2001) argued that improved financial control in growing SMEs can and should come about through a significant upgrading of financial reporting system. This view is supported by Hans & Valeri (2010) who reported in their research that when accounting information is a good description of credit risk firms can rely on performance covenants which create access to debt financing. Their research also proved that when accounting information is poor description of credit firms resort to the more robust capital covenants which align incentive by restricting debt financing and therefore limit credit market access. It is conclusive,
therefore, that accounting-based covenants create market access through the use of performance covenants.

On the relevance of the accountant to SMEs, Association of Certified Chartered Accountants (ACCA) has carried out a number of researches to empirically investigate the particular circumstances where the accountants are really relevant.

*ACCA research report No.18, which indicates the potential role of the profession in supporting small business (Chittenden, McConnel & Risner, 1990).

*ACCA research report No.64, which highlights the role of accountants in assisting with networks providing advice on business performance and ensuring learning takes place for SMEs, particularly at the early stages of the business life-cycle(Deakins, Logan & Steele, 2001).

*ACCA research report No.85, which points that ageing populations herald a need to provide for succession planning services(Martin, 2005).

ACCA research report No.70 share perceptions from both small practitioners and SMEs about e-commerce. It is of particular interest that SMEs do not perceive that accountant could assist them beyond very basic functions (Chaston & Mangels, 2001).

*ACCA research report No.71 isolates the minority ethnic respondents’ comments and illustrates how small practitioners might expand their fee base (Ram & Carter, 2001).

*ACCA research report No. 96 finds that accountants are key advisers on regulation to all businesses, and are in the position to assist SMEs in managing their regulator obligation (Blackburn et al, 2006). The study is largely presented
from the perspective of the SMEs in the UK and Canada and contains extensive data on the use they have made of accountants

*ACCA research report No. 99 surveys both accounting practitioners and SMEs in Australia to understand how accountants help SMEs with their regulatory obligations and finds that accountants are willing to assist or refer their clients to specialist advisers. Although the service given by accountants was deemed to be very good, the issue of value for money was raised (Leung, Raar & Tangey 2008).

Still on relevance of the accountants’ advice, researches are in accords that accountants’ advices prove useful. However, there is disaccord as to the effects of their advices on the business. Accountants are of the most-used professional support providers (Atkinson and Hurstifield, 2003; Jay & Scheper, 2003). It is surprising that Accountants’ advices are not related to any of the performance measures (Jay & Scheper, 2003).

Breen, Wilmshurst & Calvert (2003) believe that the external accountant can solve variety of small business challenges including choice of software. The pre-occupation in companies work is reduced by the standardization of the accounting system through the use of computers and accounting softwares.

Obamuyi (2007) in the paper titled “An exploratory study of loan delinquency among small and medium enterprises (SME) in Ondo State of Nigeria” maintained that the lending practices towards SMEs are not different from those for large enterprises. It is because of this that makes it difficult for SMEs to meet the criteria for accessing bank loan. The paper went further to state some standard criteria to assess the creditworthiness of borrowers as follows; financial strength, profitability, network, track record, management quality, relations and payment records with other banks, business prospects, business risks and collateral
securities. All the above criteria cannot be good assessments without adequate accounting. It is because of the deficiency in the record keeping of SME that compels the banks to insist on collateral as a “must” for SME. As Obamuyi (2007) has put it, “The banks requested for collateral as an additional requirement, apart from requiring personal guarantees for SME loans, because the financial and operational transparencies of SMEs were relatively low and their accounting standards were poor”

Ojeka & Mukoro (2011) in the topic titled, “International Financial Reporting Standard (IFRS) and SMEs in Nigeria: Perception of Academic” found that there is still need to enlighten people especially the SME operators on the usefulness of the IFRS for SMEs. The accountant will really have a lot of work to do to implement the IFRS for SMEs in Nigeria. The listed advantages of IFRS for SMEs includes; improving the comparability of information presented in financial statement, increasing confidence in global annual invoices, SMEs reduce cost associated with maintaining accounting standards, presence of a complete set of accounting principles simplified for each type of entity; increased satisfaction of the needs of users of financial statements (AICPA, 2011; Marion, 2009). Ojeka & Mukoro (2011) empirically demonstrated that the IFRS for SMEs will help to gain more capital for growth and expansion. This is because such standard will attract investors and the fact that some banks like; GTB Bank, Access Bank, Zenith and First Bank, have embraced the IFRS for SMEs is evidence to the assertion (Naomi, 2010; Ojeka and Mukoro, 2011).

The fact that the SME owners are amateur in business management creates varieties of opportunities for external services providers like the accountant (Yusoff, 2006). Empirical evidence suggests that accountants play a key role in advising SMEs, because they provide the most frequent source of advice (Benneth
& Smith, 2002; Carter & Mason, 2006; Scoth & Irwin, 2009; Devi & Samujh, 2010), especially in matters relating to regulation and compliance (Gooderham et al 2004; Blackburn et al 2006; Leung et al, 2008). Following the changing of global business environment, the accountants’ services to SMEs have changed from mere regulation and compliance work (Chaston et al, 2002). CPA Australia (2007) points out that service and product mixes will change and that public practitioners will need to review their levels of knowledge, and training, and then management strategies in order to meet the demand for business advisory services. Devi & Smith (2010) concluded that due to the fact that accountants have not noticed the need for them to acquire peculiar mindset towards the SMEs that Accountant are not used as supposed by the SMEs. It is, therefore, reasonable for the accountant to prepare for the emerging tasks. There is need to increase time with the SME and also there is need to bring down the level of interaction to be compatible with the level of SME- operators.

Okafor (2012) asserts that the importance of financial information to SMEs cannot be overemphasized. The research points out that firm’s face increasing pressure from banks and other fund providers, as well as, economy regulators to provide all sorts of financial information about their operations. The paper concludes that financial challenges of SMEs will be drastically reduced if the SMEs access the services of competent accountant as this would enhance their accessibility to quality financial information.

Ohachosim, Onwuchekwa & Ifeanyi (2012) investigated the relationship between accounting information and fund accessibility among SMEs in Nigeria. The researchers applied the ordinary least squares (OLS) techniques on a type of quality response regression model specified in the paper and found positive relationship between SMEs’ accounting practices and their access to finances. The
paper concludes that SMEs should improve their accounting practices by accessing the services of the accountant. It asserts that quality accounting information enhances SMEs financial management practices and accessibility of finances.
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CHAPTER THREE

METHODOLOGY

3.0 Introduction
This chapter outlines the processes and techniques adopted to achieve the objectives of the study as stated in section 1.3. This chapter is undertaken under the following headings: research design, population, sample and sampling technique, sources of data, data collection method, reliability and validity of data collection process, developing the model (model specification and variables in the models) and Techniques of data analysis.

3.1 Research Design
Survey design was adopted for the study. The research was skilfully organised to afford the researcher the opportunity of providing answers to the research questions as well as providing scientific and unbiased bases for accepting or rejecting the null-hypotheses. The research made good use of questionnaire. Percentages, tables and graphs were utilised for the presentation of the responses gathered through the means of the questionnaire to create visual effect for better comprehension, analyses and interpretations (Spiegel, 1992; Aczel & Sounderpandian, 2006). The questionnaire was fully structured to generate responses that afforded the researcher the opportunity of testing the hypotheses of the study. While some questions were structured to yield responses that enhanced the testing of some hypotheses using the $Z_{\text{score}}$ and chi-squares, others were structured to yield data that were analysed using qualitative response regression techniques. The purpose of using structured questionnaire is to sieve irrelevant ideas. It is intended to maintain predictable level of responses. It is necessary to structure the questionnaire due to some aspects of this research that require a very
dynamic analytical approach. Specifically, the qualitative response regression technique adopted is the logit model due to its obvious advantages over other qualitative response regression models (Amemiya, 1981; Aldrich, 1984; Larry, 1987; Moghaddan & Hallie, 2009). Besides being logically conclusive, it possesses comparative mathematical simplicity (Lewis-Beck, 1980; Ray, 1996; Gujarati, 2009). The data is weighted before the ordinary least square (OLS) is applied to relax the data for homoscedasticity (Gujarati, 2009). The estimates of the Glogit model were evaluated by adopting the conventional t-tests and f-tests. All tests are performed at 5% level of significance.

3.2 Population, Sample and Sampling technique

The population of this study is two thousand, six hundred and eight-eight (2688). This is the total number of SMEs in Anambra state. This figure is obtained from the Ministry of Commerce and Industry, Anambra state. The researcher adopted the Taro Yamane’s formula to obtain the sample size. This is demonstrated as follows:

Formula: Sample size (n) = \( \frac{N}{1+N(e)^2} \)

\( N = 2688 \)
\( n = ? \) (Unknown)
\( e = 5\% \)

Therefore, sample size (n) is obtained thus:

\( n = \frac{2688}{1+2688(0.05)^2} \)
\[
\frac{60}{7.72} = \frac{2688}{7.72} = 348
\]

The research adopted the stratified random sampling technique which made it possible for all the local government areas in the state to be represented in the sample size determined above (See table 3.1 below).

**Table 3.1**

**Distribution of the population and sample for the study by local government**

<table>
<thead>
<tr>
<th>S/N</th>
<th>L.G.A.</th>
<th>Population</th>
<th>Sample</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Aguata</td>
<td>151</td>
<td>20</td>
</tr>
<tr>
<td>2</td>
<td>Awka North</td>
<td>123</td>
<td>16</td>
</tr>
<tr>
<td>3</td>
<td>Awka South</td>
<td>132</td>
<td>17</td>
</tr>
<tr>
<td>4</td>
<td>Anambra East</td>
<td>3</td>
<td>0</td>
</tr>
<tr>
<td>5</td>
<td>Anambra West</td>
<td>152</td>
<td>20</td>
</tr>
<tr>
<td>6</td>
<td>Aniocha</td>
<td>83</td>
<td>11</td>
</tr>
<tr>
<td>7</td>
<td>Ayamelum</td>
<td>109</td>
<td>14</td>
</tr>
<tr>
<td>8</td>
<td>Dunukofia</td>
<td>44</td>
<td>6</td>
</tr>
<tr>
<td>9</td>
<td>Ekwusigo</td>
<td>73</td>
<td>9</td>
</tr>
<tr>
<td>10</td>
<td>Idemmili North</td>
<td>377</td>
<td>49</td>
</tr>
<tr>
<td>11</td>
<td>Idemmili South</td>
<td>119</td>
<td>15</td>
</tr>
<tr>
<td>12</td>
<td>Ihiala</td>
<td>79</td>
<td>10</td>
</tr>
<tr>
<td>13</td>
<td>Ngikika</td>
<td>100</td>
<td>13</td>
</tr>
<tr>
<td>14</td>
<td>Nnewi North</td>
<td>77</td>
<td>10</td>
</tr>
<tr>
<td>15</td>
<td>Nnewi South</td>
<td>59</td>
<td>8</td>
</tr>
<tr>
<td>16</td>
<td>Ogbaru</td>
<td>171</td>
<td>22</td>
</tr>
<tr>
<td></td>
<td>Local Government</td>
<td>Count</td>
<td>Sample</td>
</tr>
<tr>
<td>---</td>
<td>-----------------</td>
<td>-------</td>
<td>--------</td>
</tr>
<tr>
<td>17</td>
<td>Onitsha North</td>
<td>355</td>
<td>46</td>
</tr>
<tr>
<td>18</td>
<td>Onitsha South</td>
<td>278</td>
<td>36</td>
</tr>
<tr>
<td>19</td>
<td>Orumba North</td>
<td>103</td>
<td>13</td>
</tr>
<tr>
<td>20</td>
<td>Orumba South</td>
<td>33</td>
<td>4</td>
</tr>
<tr>
<td>21</td>
<td>Oyi</td>
<td>67</td>
<td>9</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>2,688</strong></td>
<td><strong>348</strong></td>
<td></td>
</tr>
</tbody>
</table>

Source: Anambra State ministry of commerce and Industry, Awka
The inclusion of SME is by SMIEIS definition
(NB: Sample is the ratio of the population of the local government to total population multiplied by the calculated sample)

### 3.3 Data and Data sources

This research made use of primary data. This was obtained from a sample of SME-operators in Anambra state. The sample of SMEs drawn randomly from each local government is in the proportion of SMEs operating in the local government to the number of SMEs operating in the state.

### 3.4 Method of Data Collection

The research made extensive use of questionnaire. The questionnaire was fully structured. A total of three hundred and forty-eight (348) questionnaires were distributed. The questionnaire has two parts: the preliminary questions part and the main parts. The preliminary questions part yielded background information about the SMEs. The main question part yielded responses that enabled the researcher to achieve the objectives of the study. A total of eleven questions were asked in the main question part. Out of which five were structured yes/no questions. One was structured in five point likert rating order, one was structured in four point order and the rest four questions were structured in such order that lists of options were provided from which the SMEs chose. The research achieved much simplicity in
designing the questionnaire considering the level of education of the SME-operators in Anambra state of Nigeria.

**3.5 Reliability and Validity of the Data Collection Process**

3.5.1 Reliability Tests
A test is considered reliable if we get similar result repeatedly (Aczel & Sounderpandian, 2006). This research adopted test-retest method to measure the reliability of the data collection process. Standard Deviation was used to find out the deviation from the mean between test periods and re-test period.

3.5.2 Validity tests
Validity refers to the ability of a test to measure what it purports to measure (Aczel & Sounderpandian, 2006). The validity of this study is measured based on the content of the questionnaires used for extracting the data from the respondents. This is a kind of content validity. Content validity is a non-statistical type of validity that involves “the systematic examination of the test content to determine whether it covers a representative sample of the behaviour domain to be measured (Buthner, 1997).

**3.6 Developing the Model**
This research was basically built its models on conventional bank practices for making loans accessible to SMEs. The problem of information asymmetries has constrained the banks from the normal assessment of SMEs’ loans through feasibility studies (Ogujiuba et al, 2004; Srinivas, 2007). They have, therefore, devised a number of other assessment bases. These bases have much dependence on the accountants’ information (Hans & Valeri, 2010). These assessment bases which are reviewed under the theoretical reviews include; Financial Statement
Rule, the Asset-Based Rule, Credit scoring/rating Rule and Relationship Handling Rule.

It is obvious that assessment bases which are based on the rules reviewed above have its foundation on rating theories. This research, therefore, drew some theoretical balance from rating model of Karinsky, Sosyurka & Vasdyk (2009). Karinsky et al (2009) and Karinsky & Peresetsky(2005) used qualitative response econometric models of multiple choices (ordered probit models) to estimate the likelihood that firms will get the benchmark ratings to get loans from the banks in Russia. In this form of econometric model, there is an ordered dependent variable $Y_i$ with numerical values 1,2,3,---k, which Karinsky et al (2009) in the model replaced with rating grades transferred to numerical scale. The model denoted an observable (latent) variable $Y_i^*$ and specified an equation as follows;

$$Y_i^* = \beta X_i + \varepsilon_i$$  

(1)

$X_i = \text{set of explanatory variables for bank-year observation } i$

$\varepsilon_i = \text{stochastic error term (independent and posses a normal function of distribution } F(z)$

$Y_i$ is related to $Y_i^*$ as follows;

$$Y_i = 1 \text{ if } Y_i^* \leq C_1$$

$$Y_i = r \text{ if } C_{r-1} \leq Y_i^* \leq C_r, 2 \leq r \leq K-1$$

$$Y_i = K \text{ if } Y_i^* \geq C_{k-1}$$

(2)
C_r and C_{r+1} are the lower and upper boundaries for the Y_i:* to obtain grade r. Assuming equation (1) and (2) are true, the probability that Y_i equals r is specified by;

\[
P (Y_i = 0) = F (C_1 - X_i \beta) \\
P (Y_i = r) = F (C_{r-1} - X_i \beta) - F (C_r - X_i \beta), \quad 2 \leq r \leq K-1 \\
P (Y_i = K) = 1 - F (C_{k-1} - X_i \beta) .
\]

Kirminsky et al (2009) and Kirminsky & Peresetsky (2005) explained that all unknown parameters are estimated with a maximum likelihood procedure and computed the generalised Huber-white standard errors to relax the homoscedasticity assumption and the assumption of no multicolinearity.

This work adopted similar procedures as described above to estimate indices for relating SMEs’ finances to their level of accounting practices. However, in alliance with the works of Hans & Valeri (2010) and Cassar & Cavalluzzo (2011), this work will employ another qualitative response econometric method known as logit model. This will enable the model proposed in this work to be flexible enough to capture the qualitative features of this work.

3.7 Model Specification
Relying on the discussion above, the model adopted in this research for major analyses is stated below:

Access to Credit is a function of the availability of quality accounting information. Quality accounting information is a function of the level of accounting practice. Therefore, it follows that access to credit is a function of the level of accounting practice. Other variables also determine credit accessibility: this is captured by introducing another variable in the model as the availability of collateral facility. The model can be represented as follows;
Access to Credit = f (level of accounting practice and collateral facility)

Through the cumulative logistic distribution function, this is translated into the Group Logit model (Glogit)

Thus,

\[
L_1 = \ln \left( \frac{P_1}{1-P_1} \right) = \beta_1 + \beta_2 X_1 + \beta_3 X_2 + \mu_1 \quad \text{-------------------------- (4)}
\]

In the Glogit model adopted above,

\[
P_1 = \frac{n_i}{N_i} \quad \text{(which represents the probability of accessing credit at ith level of accounting practice)}
\]

At each level of accounting practice, some SMEs access credit some don’t,

\[
n_i = \text{those who access at ith level of accounting practice}
\]

\[
N_i = \text{total number of SMEs at each level of accounting practice}
\]

\[
1-P_1 = \text{represent the probability of those who do not have access to credit at ith level of accounting practice}
\]

\[
P_1 \quad = \text{odd ratio in favour of accessing credit}
\]

\[
1-P_1
\]

\[
\ln \left( \frac{P_1}{1-P_1} \right) = \text{Log of the odd ratio in favour of accessing credit}
\]

\[
X_1 = \text{ith level of accounting practice by ranking}
\]

\[
X_2 = \text{other requirements (specifically collateral facility)}.
\]

\[
\beta_1, \beta_2 \text{ and } \beta_3 \text{ are coefficients and } \mu_1 \text{ is the stochastic error term}
\]

With the weighting, the equation appears as follows;

\[
LW = \beta_1 W + \beta_2 WX_1 + \beta_3 WX_2 + \mu_1 W \quad \text{------------------------------------------ (5)}
\]

Where W is the weight.
3.8 Variable in the Models

Dependent variables

The major discourse of this research is the financial challenges of SMEs in relation to what accountants can do for the SMEs to overcome them. This research will measure the level of financial challenges to be faced by any SME based on its ability to access credit or not. The more often an SME can access credit, the less will its financial challenges be.

Credit Accessibility

Credit accessibility in this work is used as a proxy to represent SMEs’ finances. It includes all forms of finances (formal or informal) that can be accessed by the SMEs to overcome their financial challenges. These may include all sources of long and short-term loans, credit facility from suppliers, equity funds from private placements, among others. This variable entered the Model (the group logit model) as a dependant variable since it has become conventional bank practices to base their assessment of SMEs vibrancy (or their ability to repay credit) on accounting related criteria. See theoretical review on 2.2 above. Credit accessibility, therefore, is dependant on the level of accounting practices of the SMEs.

For empirical purpose, if financial challenges are viewed from the angle of not accessing credit, then the level of accounting practice in an organization will determine whether firms get credit from financiers to meet their financial needs at any point in time. Credit accessibility in this work is measured by the log of the odd ratio.

Independent Variable

The independent variables identified in this work are accounting information and collateral facility. Accounting information is represented by a list of accounting
practices which have equal weight. This work measure the level of accounting practice or rather the quality of accounting information accessible to SMEs on the benchmark of how well the SMEs undertake the following accounting practices.

* Employed an accountant (or a staff with certified accounting skill) to be in-charge of accounts.
* Safe-keeping of all documents.
* Dependable Internal control.
* Computerised Accounting System.
* Book keeping.
* Preparation of financial statements
* Access to external accountant

This research ranks each of the above listed practices equally (I point each). The SME operator is asked whether he gets credit from bank. This is simple yes or no question. He ticks yes if he accesses credit and ticks no if he does not access credits.

The responses will be grouped and tabulated as below.

<table>
<thead>
<tr>
<th>Level of Accounting Practice by ranking</th>
<th>Number of SMEs in each level of Accounting Practice</th>
<th>Number who access funds at each level of accounting practice</th>
</tr>
</thead>
<tbody>
<tr>
<td>$X_i$</td>
<td>$N_i$</td>
<td>$n_i$</td>
</tr>
</tbody>
</table>

This form of grouping is found in the qualitative response regression models, known as group logit or glogit for short.
Collateral Facility enters the model as a second variable due to its relative significance in the Nigeria financial market. It is domiciled as Yes =1 and No = 0. As an a priori statement, the research will be confident to ascribe 0 to group of SMEs under any rate if 95% and above do not provide collateral to qualify for loans otherwise it will ascribe 1. It is allowable in behavioural sciences to accommodate 5% chances of making mistakes.

3.9 Techniques of Data Analysis
This work used several techniques to derive home its objectives. Descriptive statistical tools applied to present and describe the data are: tables, graphs, standard deviation and percentages. Statistical tools applied for the test of hypotheses are: Z score, Chi-square, t-tests and f-tests.
The method used for the estimation of the group logit (GLOGIT) model adopted in this research was the ordinary least square (OLS) techniques.
REFERENCES


Ogujiuba, K. K., Ohuche, F. K., & Adenuga, A. O. (2004). Credit Availability to small and medium scale enterprises in Nigeria: Importance of new capital base for banks- background and issues. AIAE working paper


CHAPTER FOUR

PRESENTATION OF DATA AND ANALYSES

4.1 Preliminary Questions

Out of the total of 348 questionnaires distributed 336 were received. This represented 97% of the population sample. The responses provided evidence that most SME-owner have high post-primary and post-secondary education. Table 4.1 below shows that 57% of SME-owners have tertiary education, 30% have secondary education while only 10% have primary education. Also, with a representation of 40% (incorporated) and 57% (not incorporated), we assert that less number of SMEs operate with registered business names. Most SMEs in Nigeria are involved in buying and selling (Trading), out of all that responded to our questionnaires, 57% are in trading and 19% are in service delivery: 7% in Agro-Allied, 10% in construction and 7% in manufacturing. The number of years that business have operated show that most SMEs die after four years of commencement, on the average 11% of SMEs operate up to four years while only 5% exist between 5 and 9 years. There is high percentage of SMEs who have existed for ten years and above. We can assert that most SMEs that have operated up to ten years have tendencies to stay even longer in business having consolidated its resources and having understood Nigeria’s business environment.

Evidence from the responses; show that majority of SMEs start-up capitals were made up from personal savings; in Table I below 69% of the SMEs obtained their initial capital from personal savings, 12% obtained through apprenticeship settlement, 1% obtained through grant from families’ treasury and government; 8% obtained from inheritance (inherited assets in form of money and others or
inherited existing business). No SMEs got its start-up capital through borrowing from the bank but
### TABLE 4.1

**PRELIMINARY QUESTIONS: DESCRIPTION OF RESPONSES**

<table>
<thead>
<tr>
<th>Number / percentage</th>
<th>Level of Education of Director</th>
<th>Incorporation Status</th>
<th>Type of Business</th>
<th>Number of years in operation</th>
<th>Sources of Initial capital</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of questionnaire received</td>
<td>Primary</td>
<td>Secondary</td>
<td>Tertiary</td>
<td>Incorporated</td>
<td>Not Incorporated</td>
</tr>
<tr>
<td></td>
<td>336</td>
<td>35</td>
<td>104</td>
<td>197</td>
<td>139</td>
</tr>
<tr>
<td>Number of questionnaire received</td>
<td>97%</td>
<td>10%</td>
<td>30%</td>
<td>57%</td>
<td>40%</td>
</tr>
</tbody>
</table>
14% obtained initial capital through borrowing from relations, co-operative and others. It can be asserted that banks do not give loans to SMEs except when the business has shown evidence of progressive business operations. This is a preliminary support for the relevance of accounting information as a major evidence of progressively operating business.

4.2 **Responses from main Questions**

SMEs in Nigeria face high rate of financial difficulties. Table 4.2 shows that 89% of the respondents indicated the fact that they had financial challenges while only a negligible 11% indicated that they did not have financial difficulties. There is high rate of financial challenges experienced among the SMEs in Nigeria.

**TABLE 4.2**

**RESPONSES ON RATE OF FINANCIAL CHALLENGES IN ANAMBRA**

<table>
<thead>
<tr>
<th></th>
<th>Yes</th>
<th>No</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number</td>
<td>300</td>
<td>36</td>
</tr>
<tr>
<td>Percentage</td>
<td>89%</td>
<td>11%</td>
</tr>
</tbody>
</table>

The extent financial challenges affect the performance of SMEs in Anambra has been displayed below in Table 4.3. It could be seen that 184 SMEs representing 59% of the respondents believe that financial challenges affect the performances of SMEs to a great extent, 103 SMEs representing 33% of the respondents believe that financial challenges affect the performances of SMEs to an extent, 23 SMEs (7% of the respondents) believe that financial challenges affect the performances of SMEs to a lesser extent while only a negligible 3 SMEs (about 1% of the respondents) said that financial challenges affect the performances of SMEs to no
extent. It does appear that the performances of SMEs in Anambra are greatly impaired by the financial challenges facing them.

**Table 4.3: Financial Challenges and Performance of SMEs in Anambra**

<table>
<thead>
<tr>
<th>Rates</th>
<th>Frequency</th>
<th>Percentage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>To a great extent</td>
<td>6</td>
<td>184</td>
</tr>
<tr>
<td>To an extent</td>
<td>4</td>
<td>103</td>
</tr>
<tr>
<td>To a lesser extent</td>
<td>2</td>
<td>23</td>
</tr>
<tr>
<td>To no extent</td>
<td>0</td>
<td>3</td>
</tr>
</tbody>
</table>

The nature of financial challenges is shown in Table 4.4 below.

**TABLE 4.4**

**RESPONSES ON NATURE OF FINANCIAL CHALLENGES IN ANAMBRA**

<table>
<thead>
<tr>
<th>Shortage of expansion capital</th>
<th>Rate</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>173</td>
<td>52%</td>
</tr>
<tr>
<td>Shortage of diversification capital</td>
<td>12</td>
<td>4%</td>
</tr>
<tr>
<td>Shortage of running capital</td>
<td>116</td>
<td>35%</td>
</tr>
</tbody>
</table>

It revealed that SMEs in Nigeria need expansion fund and running capital more than diversification fund. It is seen that 52% of SMEs need fund for expansion, 35% need fund to make up the running capital while only 12% need fund for diversification. The nature of financial difficulties among the SMEs in Nigeria is a further evidence of lack of quality accounting information. Financiers-banks and
other fund providers- have no evidence of successful business operations which can enhance effective evaluation of the viability of the SMEs for purpose of making funds available to them. These records of successful business operations can only be provided by accounting records-and because these are lacking, SMEs are always in want of funds for expansion. Also, shortage of running capital is an evidence of inadequate use of accounting information. Good uses of accounting information enhance proper working capital management. Inventory management and planning, credit policy, Cash management, et cetera, all are dependant on proper analyses and use of accounting information. It could be seen that only few SMEs demand funds for diversification. This is yet another evidence of SMEs’ awareness of their weaknesses especially in the area of record-keeping and accounting. Only those who have good accounting systems and, therefore, have access to quality accounting information, can manage the complexity of diversified businesses.

On the question of whether SMEs obtain loans from the bank to reduce their financial challenges, Table 4.5 shows that 88 SMEs representing 26% of the respondents answered in affirmative while 266 SMEs representing 79% of the respondents said they never got loans from the bank whatsoever.

**TABLE 4.5**

RESPONSES ON RATE OF OBTAINING BANK LOAN

<table>
<thead>
<tr>
<th></th>
<th>Obtain loan</th>
<th>Do not obtain loan</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number</td>
<td>88</td>
<td>266</td>
</tr>
<tr>
<td>Percentage</td>
<td>26%</td>
<td>79%</td>
</tr>
</tbody>
</table>
It should be said that if accessibility to loan facility depends on the level of accounting practices of SMEs in Nigeria, then with low accessibility to bank loans, SMEs in Nigeria do not have good accounting system. Looking at the bases for obtaining loans, Table 4.6 shows that 28% of SMEs who responded said that they provided collateral for them to obtain loans while 72% of SMEs who responded said that they were giving loans without collateral security.

TABLE 4.6
RESPONSES ON COLLATERAL SECURITY AS BASES FOR OBTAINING LOANS

<table>
<thead>
<tr>
<th>Provide Collateral</th>
<th>Do not provide collateral</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number</td>
<td>26</td>
</tr>
<tr>
<td>Percentage</td>
<td>28%</td>
</tr>
</tbody>
</table>

It could be seen that contrary to the views of the public, banks do not tie all loans given to the SMEs to collateral security. Banks actually give loans to SMEs considering various other factors which only accounting information can help the banks to determine.

SMEs believe that they keep comprehensive accounts of their business activities. This is evidenced by the information contained in Table 4.7: 243 SMEs representing 72% of the respondents answered “yes” to the question, “Do you keep comprehensive accounts of your business activities?” while only 93 SMEs which represents 28% of the respondents accept that they do not keep comprehensive account of their activities.
TABLE 4.7

RESPONSES ON COMPREHENSIVE RECORD OF BUSINESS ACTIVITIES

<table>
<thead>
<tr>
<th></th>
<th>Yes</th>
<th>No</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number</td>
<td>243</td>
<td>93</td>
</tr>
<tr>
<td>Percentage</td>
<td>72%</td>
<td>28%</td>
</tr>
</tbody>
</table>

Table 4.8 show that 281 (representing about 84% of the respondents) are of the view that poor accounting affects the finances of the SMEs negatively while 55 (representing about 16% of the respondents) does not share the same view.

Table 4.8: Poor Accounting and its Effects on SMEs Finances in Anambra

<table>
<thead>
<tr>
<th></th>
<th>Negative Effects</th>
<th>No negative Effects</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number</td>
<td>281</td>
<td>55</td>
</tr>
<tr>
<td>Percentage</td>
<td>84</td>
<td>16</td>
</tr>
</tbody>
</table>

How comprehensive are the accounts of these SMEs who believe that they maintain comprehensive records? Only when they generate quality accounting information that is qualitative and informative enough can they be said to be doing comprehensive accounting. How far do they align with some generally accepted accounting practices (GAAPs)? To find out this, the research shows in Table 4.9 that 14% of the respondents employ accountants or persons with certified accounting skill to be in charge of accounts, 28% claim that they keep all documents relating to their business transaction safely, 41% claim that they maintain proper book-keeping and 17% claim they have computerised accounting system.
TABLE 4.9
RESPONSES ON SME’s ACCOUNTING PRACTICES

<table>
<thead>
<tr>
<th>Practice</th>
<th>Frequency (x)</th>
<th>Percentage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) Employed an accountant/staff with certified</td>
<td>46</td>
<td>14%</td>
</tr>
<tr>
<td>accounting skill</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2) Safe-keeping of all documents</td>
<td>93</td>
<td>28%</td>
</tr>
<tr>
<td>3) Dependable internal control</td>
<td>23</td>
<td>7%</td>
</tr>
<tr>
<td>4) Computerised accounting system</td>
<td>58</td>
<td>17%</td>
</tr>
<tr>
<td>5) Proper book keeping</td>
<td>139</td>
<td>41%</td>
</tr>
<tr>
<td>6) Preparation of financial statements</td>
<td>23</td>
<td>7%</td>
</tr>
<tr>
<td>7) Access to external accountant</td>
<td>23</td>
<td>7%</td>
</tr>
</tbody>
</table>

It should be noted that only a negligible 7% said they maintain dependable internal control. Educated as SMEs owner in Nigeria may appear their systems of control are devoid of scientific methods, still dependant on superstition. Only 7% said that they prepare financial statement and also only 7% access the services of external accountant. It can be said from the analyses of responses relating to accounting practices that SMEs in Nigeria have very poor accounting culture.

Does SMEs’ access to finances depend on their accounting culture/practice? This is one major objectives of this research which the research will achieve by estimating the Logit model. Meanwhile a glance at Table 4.9 and Table 4.12 may ignite some insights on the relationship between the accounting practices of SMEs in Nigeria and their access to loans in relation to their provision of collateral security.
**Table 4.10**

**Accounting Practices, Accessibility of fund and Collateral Security**

<table>
<thead>
<tr>
<th>$X_1$</th>
<th>n</th>
<th>Number who provide collateral</th>
<th>Dummy ($X_2$)</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>8</td>
<td>4(50%)</td>
<td>1</td>
</tr>
<tr>
<td>1</td>
<td>22</td>
<td>10(45%)</td>
<td>1</td>
</tr>
<tr>
<td>2</td>
<td>19</td>
<td>8(42%)</td>
<td>1</td>
</tr>
<tr>
<td>3</td>
<td>16</td>
<td>3(18%)</td>
<td>1</td>
</tr>
<tr>
<td>4</td>
<td>9</td>
<td>1(11%)</td>
<td>1</td>
</tr>
<tr>
<td>5</td>
<td>9</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>6</td>
<td>10</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>7</td>
<td>0</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

As an a priori statement, the researcher is confident to ascribe 0 to any level of accounting practice if 95% and above do not provide collateral to qualify for loans otherwise it will ascribe 1. It is allowable in behavioural sciences to accommodate 5% chances of making mistakes. It could be seen that as the SMEs increase its accounting practice, the tendency to provide collateral for loan provision reduces. This is shown in the column for number who provides collateral out of those who accessed fund.
FIGURE 4.1

The graph in figure 4.1 below relates the accounting practices of SMEs in Nigeria with the log of the odds of accessing loans. By the line graph, the researcher can establish that as the SMEs improve its accounting practices, the log of the odds of accessing loans increases. This is a further evidence of the fact that good accounting enhances accessibility to loans. A dependable decision will be reached on this after we have estimated the model specified in this study.

How many SMEs access the services of accountant to mitigate their financial challenges? Out of the total respondents, only 34 SMEs access the service of the accountant for the purpose of planning their finances while 302 SMEs do not. The table below show that SMEs’ use of accountant is very poor. The fact is that SMEs do not deem it relevant to call in accountant to plan their finances.
Table 4.11: Rate of access to accountant services for the purpose of mitigating financial challenges of SMEs

<table>
<thead>
<tr>
<th></th>
<th>Access the services of accountant</th>
<th>Do not access the services of accountant</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number</td>
<td>34</td>
<td>302</td>
</tr>
<tr>
<td>Percentage</td>
<td>10</td>
<td>90</td>
</tr>
</tbody>
</table>

It is important to note that sometimes SMEs’ financial challenges do not arise because of the inaccessibility of funds but do to mere poor working capital management. SMEs do not have the tips of best practices for good working capital management. In relation to this, those SMEs who claim to access the services of accountant were asked to tick the services that accountants do for them to enhance their working capital management from the list provided; Table 4.12 shows that their habits of employing accountants

### Table 4.12: 
RESPONSES ON SMEs’ USE OF ACCOUNTANT FOR WORKING CAPITAL MANAGEMENT

<table>
<thead>
<tr>
<th>Function</th>
<th>Frequency (x)</th>
<th>Percentage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) Cash management</td>
<td>53</td>
<td>16%</td>
</tr>
<tr>
<td>2) Inventory management</td>
<td>11%</td>
<td>3%</td>
</tr>
<tr>
<td>3) Credit/ accounts receivable management</td>
<td>42</td>
<td>13%</td>
</tr>
<tr>
<td>4) Account payable management</td>
<td>11%</td>
<td>3%</td>
</tr>
<tr>
<td>5) Capital project management</td>
<td>32</td>
<td>10%</td>
</tr>
<tr>
<td>6) None of the above</td>
<td>15</td>
<td>46%</td>
</tr>
</tbody>
</table>
for working capital purposes is very poor. Only 16% of the respondents employ accountants for the purpose of cash management, a negligible 3% employ an accountant for the purpose of inventory management, 13% employ for credit/accounts receivable management, just 3% employ accountants for accounts payable management, 10% of respondents employ accountants for the purpose of capital project management and 46% of the respondents do not employ accountants for any of the purposes. In the face of poor working capital management, SMEs can still be facing financial challenges amidst surplus funds. Sometimes, stock is excessively carried as most SMEs do not have accountants to determine their economic order quantities (EOQs). The implication is inimical to business success because money is lost in carrying larger than necessary stock. These costs include the carrying costs which are costs on insurance, pilferage/obsolescence, damages, loss/theft, et cetera. A lot of fund is accessed by adequate working capital management.

It is also found that SMEs’ use of external accountant is poor. Responses on SMEs’ use of external accountants which is tabulated in table 4.13 below

**TABLE 4.13:**

RESPONSES ON USES OF EXTERNAL ACCOUNTANT BY SMES IN ANAMBRA STATE

<table>
<thead>
<tr>
<th>Function</th>
<th>Frequency (x)</th>
<th>Percentage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) Book-keeping practices</td>
<td>23</td>
<td>7%</td>
</tr>
<tr>
<td>2) Preparation of financial statement</td>
<td>46</td>
<td>14%</td>
</tr>
<tr>
<td>3) Audit work</td>
<td>23</td>
<td>7%</td>
</tr>
<tr>
<td>4) Other financial related Management</td>
<td>81</td>
<td>24%</td>
</tr>
<tr>
<td>5) None of the above</td>
<td>139</td>
<td>41%</td>
</tr>
</tbody>
</table>
shows that 23 SMEs (7% of the respondents) access the services of the accountant for the purpose of book-keeping practices, 46 SMEs (14% of the respondents) employ external accountants to prepare their financial statements, 23 SMEs (7% of respondents) employ accountant for audit and investigation purposes. It can be inferred that only few SMEs pay taxes formally since accounts are supposed to be audited to be accepted by tax officials for the computation of the tax figures. A higher percentage of the respondents (24%) employ accountants to give financially related management advice. Other financially related management advice includes; IT installation and maintenance, designing accounting systems, designing business plan, tax planning, business registration, designing business documents/correspondents, et cetera. Large number of SMEs (139 SMEs representing 41% of respondents) do not access the services of external accountant for any purpose whatsoever. Does it imply that most SMEs do not comply with Federal Inland Revenue service?

To what extent do SMEs believe that by analysing accounting information they can learn how to overcome their financial challenges? The fact is that analyses of accounting information equip the management with the dynamics of the finance of the SMEs. Understanding certain ratios helps the management to predict the finance needs. Table 4.14 below shows: in likert rating order the perceptions of the SMEs on the analyses of accounting information. The table shows that 52% of the respondents strongly agree that by
TABLE 4.14:
RESPONSES ON THE PERCEPTIONS OF SMES ON THE ANALYSES OF ACCOUNTING INFORMATION IN OVERCOMING FINANCIAL CHALLENGES

<table>
<thead>
<tr>
<th>Likert Rating</th>
<th>Rates</th>
<th>Frequency</th>
<th>Percentage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strongly Agree</td>
<td>5</td>
<td>174</td>
<td>52</td>
</tr>
<tr>
<td>Agree</td>
<td>4</td>
<td>93</td>
<td>28</td>
</tr>
<tr>
<td>Undecided</td>
<td>3</td>
<td>23</td>
<td>7</td>
</tr>
<tr>
<td>Disagreed</td>
<td>2</td>
<td>23</td>
<td>7</td>
</tr>
<tr>
<td>Strongly Disagreed</td>
<td>1</td>
<td>0</td>
<td>0</td>
</tr>
</tbody>
</table>

analysing accounting information they can beat down their financial challenges, 28% of the respondents agree the same, 7% is undecided, 7% disagreed and 0% strongly disagreed. Can we say that SMEs in Nigeria believe that by analysing accounting information they can overcome their financial challenges? This question can be answered after we have tested the hypothesis V stated in this study.

4.3 Test of Reliability

Table 4.15

<table>
<thead>
<tr>
<th>Question</th>
<th>Stand. Deviation for Test period</th>
<th>Stand. Deviation for Re-test period</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>186.6762</td>
<td>187.1222</td>
<td>No Variation</td>
</tr>
<tr>
<td>2</td>
<td>82.685765</td>
<td>82.61343</td>
<td>No Variation</td>
</tr>
<tr>
<td>3</td>
<td>81.63537</td>
<td>79.8080</td>
<td>No Variation</td>
</tr>
<tr>
<td>4</td>
<td>125.99138</td>
<td>93.1120</td>
<td>Variation</td>
</tr>
<tr>
<td>5</td>
<td>28.99138</td>
<td>28.4440</td>
<td>No Variation</td>
</tr>
<tr>
<td>6</td>
<td>106.0660</td>
<td>105.0616</td>
<td>No Variation</td>
</tr>
</tbody>
</table>
The entire population (i.e. the twenty-one local government areas in Anambra state of Nigeria) is included in the test period while one local government is used for the re-test period. The reliability of the data collection process is undertaken by comparing the standard deviations of the responses for the test and the re-test periods. Table 4.2 above shows the results. It could be seen that the responses obtained in the test period and the responses obtained in the re-test period do not show significant variations. The only noticeable variation is on question 4 which asks the SMEs whether they get bank loan. The research asserts that this variation is not attributed to method of data collection rather it is largely attributed to the presence of many financial providers competing for customers (who are simply the SMEs operating in the locality) in the local government of the re-test period.

4.4 TEST OF HYPOTHESES

4.4.1 Hypothesis I: Accounting practices do not limit the finances of SMEs in Nigeria. Can we accept the null hypothesis that poor accounting practices do not limit the finances of SMEs in Nigeria? Referring to Table 4.7, the researcher will apply the chi-square ($X^2$) in testing the hypothesis II. From the data contained in table VI, we make the following calculations.

$$x^2 = \frac{(O-E)^2}{E} = \frac{(281-168)^2}{168} + \frac{(55-168)^2}{168}$$
\[
\frac{(113)^2 + (113)^2}{168 + 168} = \frac{12769 + 12769}{168 + 168}
\]

Calculated \(X^2\) = \(\frac{25538}{168} = 152.0119\)

With degree of freedom \((D \text{ of } F) = K-1 = 2-1 = 1\) and 5% level of significance. From the \(X^2\) distribution table, we obtain the critical Chi-square \((X^2)\) value.

Critical \(X^2\) = 3.84

Decision Rule: Accept the null hypothesis if the calculated \(X^2 < \text{Critical } (X^2)\), otherwise, reject.

Calculated \(X^2 = 152.0119 > \text{Critical } X^2 = 3.84\)

Therefore, we do not accept the null hypothesis that poor accounting practices do not limit the finances of SMEs in Nigeria. SMEs in Nigeria are aware of the fact that they do not keep comprehensive and informative accounting of all their business transactions and this limit their finances.

4.4.2 Hypothesis II: SMEs’ access to finance is not controlled by their accounting practices in Nigeria. Can we accept the null hypothesis that SMEs’ access to finance does not depend on their accounting practices? Referring to Appendix VII and following the process in appendix VI, we obtain Table 4.16.

**Table 4.16: Weighted Data for the Estimation of the Logit Model of Access to loan by SMEs**

<table>
<thead>
<tr>
<th>(L^*)</th>
<th>(A)</th>
<th>(X^*_1)</th>
<th>(X^*_2)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2.1445</td>
<td>2.6303</td>
<td>0</td>
<td>2.6303</td>
</tr>
<tr>
<td>3.7573</td>
<td>4.6550</td>
<td>4.4650</td>
<td>4.4650</td>
</tr>
<tr>
<td>0.5123</td>
<td>3.3615</td>
<td>6.7230</td>
<td>3.3615</td>
</tr>
<tr>
<td>0.8585</td>
<td>2.3367</td>
<td>7.0101</td>
<td>2.3367</td>
</tr>
<tr>
<td>0.8347</td>
<td>1.2797</td>
<td>5.1188</td>
<td>1.2797</td>
</tr>
</tbody>
</table>
It should be noted that * denote that the data has been weighted. By estimating the model specified in the study using the data in table 4.16 above, we tabulate the following results;

**Table 4.17: Regression Results**

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>T- Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>B0</td>
<td>-1.505287</td>
<td>-3.175544</td>
</tr>
<tr>
<td>X1</td>
<td>0.408335</td>
<td>6.972266</td>
</tr>
<tr>
<td>X2</td>
<td>0.428431</td>
<td>1.082857</td>
</tr>
</tbody>
</table>

R-Squared = .945338  
Adjusted R-Squared = .923473  
Durbin-Watson = 2.4411128  
F-Statistics = 43.235  
Prob(F-Statistic) = 0.0006999

Testing the significance of the relationship, we refer to the t-statistics and the F-statistics. The t and f-statistics show that accounting practice is individually and collectively significant in the model. The critical t-statistics at (7-1) degree of freedom and 5% level of significance is equal to 1.895. Therefore, we do not accept the null hypothesis that SMEs’ access to loan is not controlled by their accounting practices. The quality of accounting information determines to a great extent the accessibility of loans in Nigeria.
4.4.3 Hypothesis III: SMEs in Nigeria do not access the services of accountants to mitigate their financial challenges. We refer to Table 4.10 to apply the Zscore as follows:

\[ Z = \frac{X - \mu}{SD} \]

\[ \mu = NP = 336(.5) = 168 \]

\[ SD = \sqrt{336(.5)(.5)} = \sqrt{84} = 9.165 \]

\[ X = 34 \]

\[ z = \frac{34 - 168}{9.165} = -14.6208 \]

Zscore (calculated) = -14.6208 while Zscore (critical) @ 5% level of significance = -1.645

Zscore (calculated) < Zscore (critical)

Therefore, we accept the hypotheses that SMEs in Nigeria do not access the services of accountant to mitigate their financial challenges.

4.4.4 Hypothesis IV: Analyses of accounting information do not help SMEs to overcome their financial challenges. Referring to Table 4.9, we generate the components of Zscore as follows:

Table 4.18: GENERATION OF ZSCORE COMPONENTS

<table>
<thead>
<tr>
<th>X</th>
<th>F</th>
<th>FX</th>
<th>X-μ</th>
<th>(X-μ)^2</th>
<th>F (X-μ)^2</th>
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<tr>
<td>5</td>
<td>174</td>
<td>870</td>
<td>0.665</td>
<td>0.4422</td>
<td>76.9428</td>
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<td>4</td>
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<td>372</td>
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<td>0.1122</td>
<td>10.4346</td>
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<tr>
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<td>23</td>
<td>69</td>
<td>-1.335</td>
<td>1.7822</td>
<td>40.9906</td>
</tr>
<tr>
<td>2</td>
<td>23</td>
<td>46</td>
<td>-2.335</td>
<td>5.4522</td>
<td>125.4006</td>
</tr>
<tr>
<td>1</td>
<td>0</td>
<td>0</td>
<td>-4.335</td>
<td>18.7922</td>
<td>0</td>
</tr>
<tr>
<td>15</td>
<td>313</td>
<td>1357</td>
<td></td>
<td></td>
<td>253.7686</td>
</tr>
</tbody>
</table>
\[ X = \sum X = 15 = 3 \]
\[ \frac{N}{5} \]

\[ \mu = \frac{\sum fx}{\sum f} = 1357 = 4.335 \]
\[ \frac{\sum f}{313} \]

\[ \text{SD} = \sqrt{\frac{\sum f(X-\mu)^2}{\sum f}} = \frac{253.7686}{313} = 0.81076 = 2.8474 \]

\[ Z_{\text{score}} = \frac{X-\mu}{\text{SD}} \]
\[ = \frac{3-4.335}{2.8474} \]
\[ = -1.335 \]
\[ = -0.4689 \]

-0.4689 > -1.645

Z score (Calculated) is greater than Z score (critical)

We do not accept the null hypothesis that analyses of accounting information do not help SMEs to overcome their financial challenges.

4.5 DISCUSSION OF FINDINGS

The analyses undertaken in this research have enabled the researcher to make a number of findings which were discussed as follows.

SMEs in Anambra state of Nigeria have very poor accounting practices. This led to the generation of very poor accounting information which did not enhance both accessibility of funds and good financial management. However the fact that SMEs who responded did not have good accounting practices, the study had evidences
from the analyses to assert that SMEs finances depended on their accounting practices.

First, from the analyses of the preliminary questions, it was found that no single SME got start-up capital from the bank (which is a formal financing sector). Subsequently, after commencement and the SMEs had got some evidence of progressive business undertakings, some SMEs could obtain loan even without collateral. The most impressive evidence of the state of business is the accounting information. Further, most SMEs were involved in trading and only few wanted additional fund for expansion and diversification. Great number of SMEs demanded additional finance to enhance working capital. This basically pointed at financial management issues. A number of SMEs who demanded for loan to enhance working capital may not be in need of fund if they had adequate accounting and effective financial management.

On the part of those who had need to access fund from commercial banks or any formal financing institution, evidence from the analyses show that those SMEs who kept good accounting accessed fund. Those who could not maintain good books could not access funds except those who were able to provide collateral. Financial challenges of SMEs can be reduced with adequate accounting practices. Looking through Table 4.10, it could be seen that as the SMEs increased its accounting practices, the tendency to provide collateral for loan provision reduced. This assertion was made clear in the graph in fig 4.1. The graph related the accounting practices of SMEs in Nigeria with the log of the odds of accessing loans. By the line graph, the research established that as the SMEs improved its accounting practices, the log of the odds of accessing loans increased.
The regression results in Table 4.17 have provided support for the assertion that SMEs access to fund is dependant on the accounting practices. The intercept of -1.505287 gave the probability of obtaining a loan by those who did not have any form of accounting and without collateral. In statistics, probability cannot be negative and because our estimates show a negative value, it makes sense in econometrics to take the probability to be zero. Therefore, if SMEs do not have any form of accounting, they can not generate any quality business information and if at the same time they cannot provide collateral, then, they have zero chances of accessing loans from formal sources. The coefficient of $X_1$ is 0.408335. This means that for a unit (here a step of accounting practice) increase in accounting practices, there is 0.408335 increase in the chances of accessing loans by the SMEs. This is about 41% increase in chances of accessing loans from all formal sources. The coefficient of $X_2$ gives the elasticity of obtaining loan if one can provide collateral. The estimate of 0.428431 shows that the responsiveness of accessing loans to changes in ability to provide collateral is positively elastic. We should realise that SMEs in Nigeria may still not access loans even with collateral facility. We also realise that SMEs have almost as much chances of accessing loans with collateral as with dependable accounting system. It is important, therefore, that they maintain acceptable level of accounting practice. $R^2 = 0.945338$ and adjusted $R^2 = 0.923473$ reveal that accounting practice and collateral determine about 90% chances of obtaining loans in Nigeria by the SMEs. Durbin-Watson is approximately 2 and this reveals that there is no autocorrelation in the model. It should be accepted that the model is well fitted.

Having found from our analyses that financial challenges of SMEs depended largely on their accounting practices, the question is how could the SMEs set good accounting system? It was found that SMEs who responded did not access the
services of the accountant for the purpose of tackling their financial challenges. Most SMEs who accessed the services of the accountant had to do that for compliance purposes. The case was a situation where either the bank or the Federal Inland Revenue Services (FIRS) demanded for audited accounts. Accessing the services of the accountants at this point could not help the situation because the information must have been missed. Accounting starts from the book-keeping stage to reporting stage. SMEs should access the services of the accountants and on time. Accountants have a number of services to render to the SMEs for the purposes of combating financial challenges. The accountant will set the stage for the aggregation of quality accounting information by adopting generally accepted accounting principles (GAAPs), and as a follow-up, the accountant will analyse the accounting information and advise the SMEs on the outcomes of the analyses.
CHAPTER FIVE
SUMMARY OF FINDINGS, RECOMMENDATIONS AND CONCLUSIONS

5.1 Summary of Findings
SMEs have proved very relevant in stimulating economic growth in Nigeria. However, SMEs’ progress is seriously frustrated by financial challenges facing them which have defied all efforts of the government and the SMEs themselves. The fact is that efforts have been made neither by the government nor by the SMEs themselves to ensure good financial management practices. Therefore, generally accepted accounting practices (GAAPs) are been compromised by the SMEs who rarely access the services of the accountants. The continued existence of SMEs financial challenges is attributed to their inadequate accounting practices.

This study: “Financial Challenges of SMEs in Anambra State, Nigeria”, surveyed the economically vibrant Anambra state of Nigeria to evaluate the nature of SMEs financial challenges and their accounting practices.

On the bases of the Analyses and Tests carried out in this study, the following major findings were made:

- SMEs in Nigeria have very poor accounting practices and this has compounded their financial challenges by limiting their finances.
- SMEs that have maintained high level of accounting practices are known to access loans in Nigeria in good time.
- The level at which SMEs access the service of accountants in Nigeria to mitigate their financial challenges is poor and this further accounts for the chronic nature of their financial challenges.
- SMEs in Nigeria are aware that by analysing quality accounting information, they can overcome their financial challenges.
Other relevant findings made include the following:

- Higher proportion of SMEs in Nigeria has post-primary education.
- Higher proportion of SMEs in Nigeria is engaged in trading.
- More than half of SMEs in Nigeria die after four years of commencement.
- The few SMEs that survived the first four years have tendencies to stay longer having understood the Nigerian business environment and they have been identified with dependable accounting practices.
- Higher proportion of SMEs in Nigeria make-up their start-up capital from personal savings and apprenticeship settlement.
- SMEs have almost as much chances of accessing loans with collateral as with dependable accounting system.
- The best way to identify and evaluate a genuine and viable business is to look into their books which reflect their business activities.

5.2 **Recommendations**

To enhance the performances of SMEs in Nigeria, this study based on the above findings, recommend the following:

- SMEs should improve their accounting system to be able to generate quality accounting information so as to enhance their performances.
- Banks and other financiers should use accounting information to identify genuine and actively operative SMEs in Nigeria.
- SMEs should endeavour to consult accountants regularly to be able to maintain high accounting standard by adopting generally accepted accounting practices.
• SMEs should utilise accounting information in the management of their finances by embarking on proper analyses of accounting information.

• The accounting bodies in Nigeria, the Institute of Chartered Accountants of Nigeria (ICAN) and the Association of National Accountants of Nigeria (ANAN), should wear global outfit and train their members to serve SMEs’ accounting need due to their relevance in the economy.

• Accountants should encourage SMEs to access their services. They should avoid scaring them away by quoting very high fees.

• Government should stipulate minimum number of books to be kept by all SMEs that meet SMIEIS criteria for SMEs which will certify them to operate in Nigeria. This dimension will be in line with international order that have designed International Financial Reporting Standard (IFRS) for SMEs.

5.3 CONTRIBUTION TO KNOWLEDGE
This study has made the following contributions to existing knowledge:

• It has contributed geographically to the understanding of the link between financial challenges of SMEs and their accounting practices.

• It has brought to bare the accounting needs of SMEs, as well as, the need to repackage accounting services to suite these needs.

5.4 AREA OF FURTHER STUDIES
This study is only a stepping stone for further researchers. Suggested related areas include: working capital management of SMEs: the role of the accountant, International financial reporting standard for SMEs: relevance to SME finance, the impact of accounting information in the progress of SMEs, the level of accounting practice and the operative existence of SMEs, among others.
5.5 CONCLUSIONS

The need to build viable SMEs has emerged the focus of every economy today. The situation is not different in Nigeria following the need to reduce unemployment and enhance Nigeria’s economy. This study, “Financial Challenges of SMEs in Anambra state, Nigeria” is a dynamic approach towards the evaluation of SMEs’ finance challenges. It studied the nature of SMEs financial challenges, the nature of SMEs accounting practices and tries to establish a link between these financial challenges and their accounting practices.

Through a series of scientific and verifiable processes highlighted in the study, the researcher found among others that SMEs can overcome their financial challenges by improving the quality of accounting information generated by them. This has set emerging task for the accountant who must acquaint the SMEs on the generally accepted accounting practices. The findings of this study are in line with the submissions of Larson & Clute (1979), Opkara (2000), Ohachosim, Onwuchekwa & Ifeanyi (2012) and Okafor (2012).

This research should serve as a stepping stone on which prospective researcher can stand to make more meaningful impacts in the area of SME finances in our own part of the world. Suggested possible research areas includes; Working capital management of SMEs in Nigeria: the role of the accountant, International financial reporting standard for SMEs: relevance to SME finance in Nigeria, the impact of accounting information in the progress of SMEs in Nigeria, among others.

Finally, this study has provided empirical evidence that SMEs access to finance depend largely on their accounting information. It concludes that for SMEs to overcome their financial challenges they should access the services of the accountant to improve the quality of their accounting information.
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Sir/Madam,

Request to respond to the questionnaire designed to carry out research on the topic “Financial Challenges of Small and Medium-size Enterprises (SMEs) in Nigeria: Relevance of the Accountant”

I am a post graduate student of the above named Department and Institution. I am carrying out a research on the topic shown above, as a partial fulfilment of the requirements for the award of Masters of Science Degree (M.Sc.) in accountancy.

I humbly request you to do me the favour of filling this questionnaire as the questions relate to your independent opinion and experience. You are assured that the exercise is purely academic and that the highest level of confidentiality will be given your responses. You are also assured that your answers/responses will be strictly used for the purpose highlighted here and nothing beyond that.

Thanks for your anticipated co-operation.

Yours faithfully,

Ohachosim, Celestine Ikem
APPENDIX II: Questionnaire for the study of SMEs financial challenges in Nigeria

Preliminary

Name of Director: ______________________________________

Level of Education: Primary/Secondary/Tertiary

Name of Company: ______________________________________

Incorporated: Yes/No

Activity/Line of Business: Trading/Agriculture/Agro-allied/Service
  Delivery/Construction/Manufacturing

Number of years Company has operated: ____________________

Source of Initial Capital: Personal saving/Apprenticeship settlement/Borrowing-
  Bank or Relations or credit society-/ Grants-Government or Relations-/ inheritance

1. Do you think you face financial challenges in your business?: Yes/No

2. If yes, tick as appropriate the nature of financial challenges you face.
   Need for fund for expansion/Need for fund for diversification/Need for fund
   for running the existing business efficiently.

3. To what extent do financial challenges exert negative effects on the
   performances of your company?
   To a great extent
   To an extent
   To a lesser extent
   To no extent
3. Do you get loan from the Banks? : Yes/No
4. If yes, do you provide collateral to get loans? : Yes/No
5. Do you keep comprehensive Account of your business activities? Yes/No
6. Do you think that poor accounting limits the finances of SMEs in Nigeria? Yes/No
7. If yes, tick as appropriate from the list below your practice to enhance quality accounting information in your company.
   * Employed an accountant (or a staff with certified accounting skill) to be in- change of accounts.
   * Safe-keeping of all documents.
   * Dependable Internal control.
   * Computerised Accounting System.
   * Proper book keeping.
   * Preparation of financial statements
   * Access to external accountant
8. Do you access the services of the accountant to overcome your financial challenges? Access the services of accountant. / Does not access the services of accountant.
9. Tick as appropriate the activity you employ accountant to do for you to enhance your working capital management
   * To use formal accounting technique to determine cash level
   * To use formal accounting techniques to manage inventory
   * To use formal accounting techniques to manage credit/accounts receivable
   * To use formal accounting techniques to manage accounts payable
   * To use formal accounting techniques to plan for capital projects
* None of the above

10. If you access the services of the external accountant, tick as appropriate what he does for your company.
* He advises me on book-keeping practices
* He prepares my financial statements
* He audits financial statements for the purpose of filling returns to Corporate Affairs Commission/Tax Agency
* He analyses my company’s financial statements and gives me financial related management advice
* Other business advice
* None of the above

11. Analyses of accounting information help SMEs to overcome financial challenges in Nigeria

   Strongly agreed, Agreed, Undecided, Disagreed, Strongly Disagreed
### APPENDIX III: DERIVATION OF WEIGHTED DATA FOR MODEL ESTIMATION

\[
W = \sqrt{\frac{N}{p(1-p)}}
\]

<table>
<thead>
<tr>
<th>(X)</th>
<th>(W = \sqrt{\frac{N}{p(1-p)}})</th>
<th>(\sqrt{\frac{N}{p(1-p)}})</th>
<th>(N)</th>
<th>(W)</th>
<th>(L_i\sqrt{W})</th>
<th>(X_1\sqrt{W})</th>
<th>(X_2\sqrt{W})</th>
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</thead>
<tbody>
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<td>0</td>
<td>60(0.133)(1-0.133)</td>
<td>(\sqrt{6.91866})</td>
<td>6.91866</td>
<td>2.6303</td>
<td>-2.1445</td>
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<td>2.6303</td>
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<tr>
<td>1</td>
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<td>(\sqrt{19.9362})</td>
<td>19.9362</td>
<td>4.4650</td>
<td>-3.7573</td>
<td>4.4650</td>
<td>4.4650</td>
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<tr>
<td>2</td>
<td>46(0.434)(1-0.434)</td>
<td>(\sqrt{11.2996})</td>
<td>11.2996</td>
<td>-3.3615</td>
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<td>3.3615</td>
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<tr>
<td>4</td>
<td>11(0.818)(1-0.818)</td>
<td>(\sqrt{1.6376})</td>
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<td>6.3985</td>
<td>1.2797</td>
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<td>7</td>
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<td>(\sqrt{0})</td>
<td>0</td>
<td>0</td>
<td>0</td>
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</table>
APPENDIX IV:

Level of accounting practice and generation of the log of the odds

<table>
<thead>
<tr>
<th>Level of accounting practice</th>
<th>Number of SME’s in each level of accounting practice</th>
<th>Number who access loans</th>
<th>Probability of accessing loans</th>
<th>Odds</th>
<th>Log of odds</th>
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