

FINANCIAL ACCOUNTING LITERACY AND GROWTH OF SMALL AND MEDIUM SCALE ENTERPRISES (SMES) IN ONDO STATE

Gbemigun, Catherine Omoleye

*Department of Accounting,
Faculty of Administration and Management Sciences,
Adekunle Ajasin University Akungba Akoko Ondo State.
gbemiguncatherine@gmail.com*

&

Agbaje Wale Henry

*Department of Accounting,
Faculty of Administration and Management Sciences,
Adekunle Ajasin University Akungba Akoko Ondo State.
wale.agbaje@aaua.edu.ng*

Abstract

Businesses collapse in recent times due to illiteracy of management and stakeholders on how to deal with the financial aspect of their activities. As a result, the study examined the effect of financial accounting literacy and growth of small and medium scale enterprises. The study adopted descriptive research design and obtained data from structured questionnaire, the respondents targeted were Small and Medium Enterprises (SMEs). Data were analyzed using percentages, frequencies, means and ANOVA. Thus, the study concluded that there is a significant relationship between financial accounting literacy and the growth of SMEs in Ondo State thereby having an influence on their growth and development as it is also essential for the survival and continuity of any SME. Based on the findings, the study recommends that the ministry or agency responsible for SMEs in the state should initiate accounting training programs for entrepreneurs running small businesses, since keeping proper accounts enhances profitability and growth of small scale enterprises, also, emphasis should be stressed on the teaching of basic accounting concepts and skills to all students so as to enhance their entrepreneurial skills in every sector.

Keywords: Financial Accounting, financial literacy, small and medium scale enterprises.

Introduction

Financial accounting literacy is important in controlling businesses and organizational operations in today's complex and dynamic environment. Financial literacy is the set of skills and knowledge that allows an individual to take appropriate financial decisions. Financial literacy has been made a priority by several governments globally to deal with the need to increase financial knowledge and the skills necessary for entrepreneurs to navigate the financial world. In addition, financial literacy plays a pivotal role in economies achieving economic growth and development (Bongini and Zia 2021; Lusardi and Mitchell 2011; Nkomazana, Sibanda and Duve 2015; Organisation for Economic Co-operation and Development (OECD) 2020).

As opined by Mashizha, Sibanda and Maumbe. (2019), Small and medium enterprises (SMEs) are notably the engines that drive economic development. Arellano, Cámara & Tuesta (2018), Cucinelli, Trivellato & Zenga (2019) posited that, in an endeavour to strengthen the functioning of the SMEs sector, financial literacy has been considered a prerequisite for the sector, as business owners make routine financial decisions daily that have a bearing on their success and growth. Thus, in order to operate efficiently and attain the envisaged economic growth and sustainability, SMEs need to be equipped with the necessary skills to undertake effective financial decisions (Mabhandu, 2015). Financial literacy has been made a priority by several governments

globally to deal with the need to increase financial knowledge and the skills necessary for entrepreneurs to navigate the financial world. In addition, financial literacy plays a pivotal role in economies achieving economic growth and development (Bongini & Zia 2018; Lusardi & Mitchell 2011; Nkomazana, Sibanda & Duve 2015; Organisation for Economic Co-operation and Development [(OECD) 2013).

It has been proven that financial literacy is essential in any economy, (Arrellano et al. 2018; Cucinelli et al. 2019). Mutegi, & Phelister, (2015), affirms that financial accounting literacy facilitates the decision making processes such as payment of bills on time, proper debt management which improves the credit worthiness of potential borrowers to support livelihoods, economic growth, sound financial systems, and poverty reduction. Hasler & Lusardi (2017), also stressed that financial accounting literacy provides greater control of an individual's financial future, more effective use of financial products and services, and reduced vulnerability to overzealous retailers or fraudulent schemes.

According to Ofunre, Oyinlola, and Grace, (2017), businesses face challenges in taking certain financial decisions and making informed judgments regarding financial services that impact on their financial activities. Making such decisions requires financial literacy. Despite all these challenges SMEs have ability to fuel economic growth because they create new jobs, expands the tax base, and is drivers of innovation. According to Wanjohi (2011) SMEs enhance competition and entrepreneurship hence has external benefits on economy wide efficiency, innovation and aggregate productivity. They are the primary vehicles by which new entrepreneurs provide the economy with a continuous supply of ideas, skills, and innovations. The concentration of SMEs has a close relationship with the dominant economic activities. SMEs dominate the world economies in terms of employment and number of companies, yet their full potential remains remarkably untapped (Atsede, Patricia & Adebimpe 2008). SMEs are the backbone of the economy, providing a prime source of new jobs, playing a crucial role in income generation, reducing poverty by helping boost employment in rural areas and recognized as an engine of economic growth and development. Common SMEs include farming, hawking, trading, public

transport service, professional services such as lawyers and doctor etc.

Evidence shows that many of the financially excluded SMEs lack knowledge about basic financial accounting literacy and features of available financial products in developing countries (Berg & Zia, 2017). Despite the efforts towards ensuring the Nigerian economy is deepened by way of financial accounting literacy, small businesses in the country are still faced with several financial problems (Njoroge, 2013). As a result, this study examined the influence of financial accounting literacy and the growth of SMEs in Ondo State, Nigeria. The study hopes to provide answer to this question, what is the impact of financial accounting literacy on the growth of SMEs in Ondo State?

Small and Medium Scale Enterprise

A review of the literature on small and medium enterprises (SMEs) shows that the definition of SMEs significantly varies from country to country depending on factors such as the country, number of employees, the value of fixed assets, production capacity, basic characteristics of the inputs, level of technology used, capital employed, management characteristics, economic development, and the particular problems experienced by SMEs (Eniola & Entebang, 2015). SMEs are now strategic and essential for accelerating economic growth in Nigeria. SMEs constitute about 90% of all businesses in Nigeria, creating more than 80 percent of employment in the region. The contribution of SMEs to the Nigerian economy cannot be overstated. Across the African continent, research by the IFC suggests that 90% of all MSMEs is informal or micro, with the remaining 10% being the formal SMEs (8.6% are small and 1.4% medium) (IFC, 2010; Ketley, Lightfoot, Jakubec, & Little 2012). Studies by the IFC show that approximately 96% of Nigerian businesses are SMEs. In Nigeria, the National Policy on Micro, Small and Medium Enterprises (MSMEs) define micro enterprises as employing less than ten people with assets (excluding land and buildings) of less than ₦5 million, small enterprises as between 10–49 employees and assets between ₦5million - ₦50 million, whilst medium enterprises are those with between 50 and 199 employees and assets between ₦50million – ₦500 million.

Financial Accounting Literacy

One of the striking things about the literature is that financial accounting literacy has been variably defined as a specific form of knowledge, the ability or skills to apply that knowledge, perceived knowledge, good financial behavior, and even financial experiences (Hung, Parker, & Yoong, 2009). Financial accounting literacy as sufficient knowledge about facts on personal finances and is the key to personal financial management (Garman & Forgue, 2002). Their study likewise reviews the lack of knowledge in personal finance, intricate financial situations, in addition to a large range of choices for making decisions on financing, and time constraints on learning about personal finance which is a barrier to financial accounting literacy. Many researchers have defined financial literacy in many studies in the area of personal finance; many fail to define the concept financial literacy properly because it does not capture the owner (manager) and the business people. Gitman (2003) outlined financing provision and indicates that financial service is the section that will include the delivery of financial products to individuals. Financing literacy is listed as one of the critical managerial competencies in SMEs firm and development (Spinelli, Timmons, & Adams, 2011). Most scholars agree that entrepreneurs, regardless of their age, are consistently engaged in decision-making activities concerning resource procurement, allocation and utilization. Such activities almost always have financial consequences and thus, in order to be effective, entrepreneurs must be financially literate (Oseifuah, 2010). There is the only reference made to the importance of managing money and the author only describes the management process of individual households, but there is no clear description of SME owners/manager financial literacy.

Financial Knowledge: Financial knowledge is defined as the understanding of key financial terms and concepts needed to function daily (Huston, 2017). It is defined by (Potrich, Kelmara and Wesley, 2016) as a particular kind of capital acquired in life through the ability to manage income, expenditure and savings in a safe way. Financial knowledge is associated with a number of “best practice” financial behaviors, including possessing an adequate emergency fund, monitoring credit reports, avoiding checking account overdrafts, avoiding revolving debt, owning a dedicated retirement account, and

having insurance protection (Robb, 2014). The Organization of Economic Co-operation and Development (OECD), added that financial knowledge is an important determinant of whether the individual is financially literate, involving questions related to concepts such as simple and compound interest, risk and return and inflation (OECD INFE, 2011).

Financial Behaviour: Financial behavior as defined by Zeynep(2015)as the capability to capture the understanding overall impacts of financial decisions on one’s circumstances and to make the right decisions related to the cash management, precautions and opportunities for budget planning. Research has shown that financial literacy consistently predicts measures of financial behavior of individuals (Hung, Parker and Yoong, 2009). Sucuahi (2013) highlighted that a good financial behavior involves the ability to make financial decisions that increase wealth and prevent uncertainties of businesses and individuals. These activities generate more financial assets, prevent over- indebtedness, finance retirement, and insure against major life contingencies.

Financial Attitude: Financial attitude can be defined as the application of financial principles to create and maintain value through decision making and proper resource management (Latif, Razak, and Lumpur, 2011). Financial attitude is one of the factors that have significant impact on financial management practice. It is defined by Eagly and Chaiken (1993) as psychological tendency that is expressed by valuating a particular entity with some degree of favor or disfavor”. That is, it a psychological predisposition when it comes to agreeing or disagreeing with certain financial management practices. Latif et al. (2011) defined financial attitude as the creation of value in decision making and resource management through application of financial principles. Financial attitude is improved through procurement of adequate information (Abiodun, 2016).

Firms’ Growth and Development

However, there are definitions of financial literacy specifically addressed to managers and business people. A financially literate SMEs owner/manager was defined as someone that knows what are the most suitable financing decisions on the business performance at the various growth stages of the business; knows

where to obtain the most suitable products and services; and interacts with confidence with the suppliers of these products and services (USAID, 2009). Lusardi and Tufano (2009) emphasized on (owner's) manager's ability and decision-making aspect of financial literacy. Likewise, they target on a particular form of financial literacy and debt literacy. Moore (2003) goes far as including practical experience, on the contention that it provides the basis for knowledge and other faces of financial literacy. In the present paper, financial literacy is conceptually of how firms manage and strategize financial knowledge, which significantly affect decision makers' behaviors, awareness and attitudes, concerning sound decision making and eventually achieving organizational growth and performance. Growth may have two strategic outcomes that are often referred to in the literature as firm success or failure (Eniola&Entebang, 2015a). In the management field, firm growth can be interpreted as measures of good or indifferent management (Jennings & Beaver, 1997; Sefiani&Bown, 2013) The effects of a firm's growth depend on whether the firm has attained its goals or not (Davidsson, 2004). According to Abiodun and Harry (2014) SMEs growth forms a very important part of the Nigerian economy. The SME sector is a major engine which encourages the growth of jobs and wealth creation in the country's economic system. SMEs growth act as a significant part that is linked to the strengthening and enhancement of the development of the country. Firm growth is a focal phenomenon in business management. It has been proposed in the literature (Barney, 2002). The general growth of the organization depends on the correct management at the three levels of management (Eniola&Entebang, 2015a). Growth can be characterized as the firm's ability to create acceptable outcomes and actions.

Financial Accounting Literacy and its Influence on SME Firm Growth

Positive relationships between financial accounting literacy and growth have been noted by a number of researchers (Hilgert et al., 2003; Huston, 2010; Kidwell &Turrisi, 2004; Lusardi, Mitchell, &Curto, 2010; Piprek&Coetzee, 2004). Financial resources are essential resources for obtaining both tangible and intangible resources and arranging other resources (Alsos, Isaksen, &Ljunggren, 2006; Brinckmann, Salomo, &Gemuenden, 2011). According to (Lusard and BassaScheresberg, 2013), the concept of financial literacy as comprising three dimensions in

knowledge, attitude and awareness (Rahmandoust, Shah, Norouzi, Hakimpour, & Khani, 2011). Knowledge is about understanding how business performance, business growth and business condition are measured using the mental model to facilitate, support, or enrich decision-making (Lusardi&Michell, 2007; Moore, 2003). Lusardi and Michell (2006) suggested that financial literacy is needed to create a measure of financial competence, i.e., to stay knowledgeable about financial matters.

Empirical Review

Empirical studies reviewed present both convergent and divergent views on the role of financial accounting literacy and growth SMEs. Most scholars concur that financial literacy greatly influences enterprise growth. While several factors may play a role in determining enterprise growth, the skills of the entrepreneur have been found to be a crucial determinant. Cherugong (2013) examined the effect of financial literacy on growth of SMEs in Trans Nzoia County, Kenya. The study was carried out to examine the aspect of the present day financial literacy of SMEsin Trans Nzoia County on business growth. The results of the study established that there was a positive strong effect of financial literacy on SMEs. The study recommended the providers of various financial literacy programs to consider implementing a program which fits the culture and traditions of the context targeted and avoid one size fits all because different SMEs have different experiences, this study is in line with Lusimbo (2016) who analyzed the relationship between financial literacy and the growth of SMEs in Kenya. Findings reveal that although SMEs managers had a fair knowledge of debt management majority do not understand the effect of inflation and interest rates on loans they borrow and were not comparing terms and conditions before purchasing financial products which could affect their financial decisions of when to borrow, how much and from whom, leading to sub- optimal business performance. Results also indicate that most SMEs owners have low level of budgeting and Book keeping literacy since they do not engage in formal financial planning, budgeting and control and do not keep proper books of account as well as preparation of financial statements which increases their information opacity and may constraint their access to finance. Koech, Oyungi and Memba (2015) established in their study that the source of

funding significantly affects the growth of SMEs. Onugu (2005) argues that despite the incentives, programs, policies and support aimed at revamping the SMEs, they have performed rather below expectation in Nigeria. While an average operator would always hinge their failure to lack of access to finance, evidence has shown that fund/finance contributes only about twenty-five percent to the success of SMEs, which sounds insignificant, the study specify the same opinion of Umogbai monica, Agwa and Asenge (2018), in their work which is mainly to analyze the effect of financial knowledge on the performance of SMEs in Benue State, Nigeria concluded that financial knowledge and attitudes influences SMEs performance. It was recommended among others that there is a need for training programs on budgeting and planning, debt management, record keeping; saving and retirement plans in schools and other institutions that seek to promote financial literacy and practice. Thus, the creation of other appropriate support systems and enabling environment are indispensable for the success of SMEs in Nigeria. Seoul Summit (2010) eluded that SMEs' face a challenge of information asymmetry due to lack of accounting records, inadequate financial statements or business plans which make it difficult for them to access credit. Similar views were extended by Kipngetich (2016) who added that lack of financial literacy skills including operating skills, accounting skills and finance skills still present a formidable challenge for SMEs borrowers. The quality of the accounting information is greatly affected by the quality of accounting systems used. Diamond and Khemani (2006) identified that SMEs' use either manual accounting systems which are supported by very old and inadequately maintained software applications and hardware. This has a damaging effect on their functioning hence adversely affect the appropriateness and reliability of the collected accounting information. Lusardi and Michell (2006) suggested that financial literacy is needed to create a measure of financial competence, i.e., to stay knowledgeable about financial matters. These literate people are more participating in financial markets because they know financial matters.

Lusardi and Bassa Scheresberg (2013) examined the impact of financial literacy and high cost of the borrowers. The result indicated that there is a relationship between financial literacy and low-cost borrowers. Most high-cost borrowers display very low levels of financial literacy, lack

knowledge of basic financial concepts, which affect their performance level in a business. Kidwell and Turrisi (2004) indicated that firms with better financial knowledge keep detailed firm financial records and have a more competitive advantage in accessing external funding than their counterparts who keep not. While, Hilgert et al. (2003) insisted that a strong link between financial knowledge and financial behavior subsists. Kolvereid and Bullvag (1996) state that high growth firms have entrepreneurs with high level of education. On the contrary Njoroge (2013) argues that the level of education may not be the only determinant as there are very successful SMEs run by illiterate managers while others run by highly educated managers have failed. Ezijioforetet al, (2014); Fatoki, 2014; and Agyei,(2014) opine that although book keeping allows a business to file tax returns, compare its business performance with others and put in place appropriate financial controls to prevent business failure most SMEs do not keep proper business records due to lack of accounting knowledge. On the contrary, Waweru (2007) asserts that failure to produce financial information by SMEs is a strategy to avoid taxation although it eventually impacts on their ability to access external finance due to in transparent information. These studies also reveal limited use of budgeting by SME managers which negatively impacts on business performance as well as personal money management (FSD, 2009; Warue and Wanjira,2013; Fatoki,2014).Through business training, SME managers can acquire the right skills, knowledge and attitudes necessary to improve financial management of their businesses and increase their uptake of financial products to realize growth, survival and transit to the next level.

Research Gap

Careful examinations of several studies carried out in Nigeria and other developing countries on financial accounting literacy and growth of SMEs, it can be seen that most emphasize and focus on financial training of small businesses and few on financial accounting literacy. Therefore, this study will examine financial accounting literacy and growth of SMEs in Nigeria.

Theoretical Framework

Dual-Process Theory

The dual process theory is considered relevant to this study because it shows that individuals who are high on cognition will seek out for

information and are more likely to be influenced by a relevant message. The dual-process theory was propounded by Lusardi & Mitchell (2011). This theory posits that financial decisions can be driven by both intuitive and cognitive processes which mean that financial literacy may not always yield optimal financial decisions. The Dual Process Financial literacy theory argues that the behavior of people with a high level of financial literacy might depend on the prevalence of the two thinking styles: intuition and cognition (Lusardi & Mitchell, 2011; Glaser & Walther, 2013). Intuition is the ability to acquire knowledge without inference or the use of reason. Intuition provides views, understandings, judgments, or beliefs that cannot be empirically verified or rationally justified. Taylor (1981) as cited by Chan and Park (2013) asserts that individuals who rely on intuition prefer to use mental short cuts as they make decisions which tend to be largely influenced by their emotions. Glaser and Walther (2013) point out that the positive effect of financial literacy on reasonable investment decisions is diminished by a high prevalence of intuition. Therefore, increased use of intuition results to sub optimal investment decisions.

Methodology

The survey research design was adopted in this study. The data collection technique used was questionnaire. The population of this study is narrowed to Akoko South West Local Government Area of Ondo state. In this local

government, the study investigated a total number of 100 SMEs in the local government area. This study employed a systematic sampling technique to investigate skills that can be boosted by financial literacy training using simple easy to understand methodologies. Ten (10) small and medium scale enterprises in ten (10) wards in the local government area. Primary data was collected using a structured questionnaire and the respondents targeted were SMEs owners. The structured questionnaire contained both open and closed ended questions. Closed ended questions was used since they are easier to analyze and facilitate harmonization of information to be obtained from the respondents. To derive useful meaning from the data and examine the propositions of this study, data from the survey was analyzed using SPSS 20.0 (Statistical Package for Social Sciences). Data collected was coded as specified in the measurement of variables to make it amendable to computer analysis. The hypothesis was tested at 0.05 level of significance (95% confidence level).

Presentation and Analysis of Data According to the Model of the Study

This section illustrated and analyzed the descriptive statistics of the research findings, correlations table, the model summary table, and analysis of variance table. The results were interpreted and conclusions were made accordingly.

The impact of financial accounting literacy on the growth of SMEs

Table 1: Variables Entered/Removed(b)

Model	Variables Entered	Variables Removed	Method
1	Financial Accounting Literacy(a)		Enter

a All requested variables entered.

b Dependent Variable: SMEs Growth

Source: Researcher’s Field Survey 2021

Table 2: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.767(a)	.589	.584	2.06437

a Predictors: (Constant), Financial Accounting Literacy

Source: Researcher’s Field Survey 2021

This table provides the R and R² values. The value represents the simple correlation and it is 0.767 (the “R” column) which indicate a high degree of correlation. The R² value (the “Rsquare” column) indicates how much of the total variation in the dependent variable, SMEs growth, can be explained by the independent variable, Financial Accounting Literacy. In this case, 58.9% can be explained, which is still good enough.

Table 3: ANOVA (b)

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	597.362	1	597.362	140.173	.000(a)
	Residual	417.638	98	4.262		
	Total	1015.000	99			

a Predictors: (Constant), Financial Accounting Literacy

b Dependent Variable: SMEs Growth

Source: Researcher’s Field Survey 2021

The ANOVA table above reports how well the regression equation fits the data (i.e predicts the dependent variable). Looking at the “Regression” row and go to the “Sig” column, it indicates the statistical significance of the regression model that was run. In the above ANOVA table, we will focus on the F-statistic. An F-statistic of 140.173 was obtained. This is highly significant as the p-value is less than 0.05.

Table 4: Coefficients(a)

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta	B	Std. Error
1	(Constant)	.850	1.288		.660	.511
	Financial Accounting Literacy	.492	.042	.767	11.839	.000

a Dependent Variable: SMEs Growth

Source: Researcher’s Field Survey 2021

The coefficient table above gives us the values that we need in order to write the regression equation. The regression equation will take the form:

Predicted variable (dependent variable) = slope* independent variable + intercept

This means that: SMEs Growth = 0.850 + 0.411 (Financial Accounting Literacy).

However, the t-column tests to see if the coefficients are significantly different from zero (0). The p-values (0.000) reveal that Financial Accounting Literacy has a positive effect on the Growth of SMEs.

Table 5: Variables Entered/Removed (b)

Model	Variables Entered	Variables Removed	Method
1	Financial Accounting Literacy(a)		Enter

a All requested variables entered.

b Dependent Variable: SMEs Survival

Source: Researcher’s Field Survey 2021

Table 6: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.922(a)	.850	.848	1.57292

a Predictors: (Constant), Financial Accounting Literacy

This model summary table shows the R and R² values. The value represents the simple degree of correlation and it is 0.922 (the “R” column) which indicates a very high degree of correlation. The R² value (the “Rsquare” column) indicates how much of the total variation in the dependent variable, SMEs Survival, can be explained by the independent variable, Financial Accounting Literacy. In this case, 85% can be explained, which is very good.

Table 7: ANOVA(b)

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	245.126	1	245.126	17.584	.000(a)
	Residual	1366.184	98	13.941		
	Total	1611.310	99			

a Predictors: (Constant), Financial Accounting Literacy

b Dependent Variable: SMEs Survival

Source: Researcher’s Field Survey 2021

The ANOVA table above reports how well the regression equation fits the data (i.e predicts the dependent variable). Looking at the “Regression” row and go to the “Sig” column, it indicates the statistical significance of the regression model that was run. In the above ANOVA table, we will focus on the F-statistic. An F-statistic of 17.584 was obtained. This is moderately significant as the p-value is less than 0.05.

Table 8: Coefficients(a)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta	B	Std. Error
1	(Constant)	3.729	2.329		1.601	.113
	Financial Accounting Literacy	.315	.075	.390	4.193	.000

a Dependent Variable: SMEs Survival

Source: Researcher’s Field Survey 2021.

The coefficient table above gives us the values that we need in order to write the regression equation. The regression equation will take the form:

Predicted variable (dependent variable) = slope* independent variable + intercept

This means that: SMEs Survival = 3.729 + 0.315 (Financial Accounting Literacy).

However, the t-column tests to see if the coefficients are significantly different from zero (0). The p-values (0.000) reveal that Financial Accounting Literacy is relevant to any business and has a positive effect on SMEs Survival.

Conclusion and Recommendations

This study concludes that there is a strong positive effect of financial literacy on growth of SMEs. SMEs that are more successful are run by entrepreneurs who are financial literate and understand key financial concepts that include, risk management, debt management, record

keeping and budgetary skills. Financial literacy regarding the budgeting skills assist in reducing the SMEs running costs and ultimately enabled advance planning on loan repayment. In addition, financial literacy skills enhanced the ability to do a self-internal audit that enabled beneficiaries to identify resource leakages and ensure proper

channeling of resources towards credit management. This revelation appears to compliment Miller's (2009) argument that financial literacy helps in empowering and educating investors so that they are knowledgeable about finance in a way that is relevant to their business and enables them to use this knowledge to evaluate products and make informed decisions. It is widely expected that greater financial knowledge would help overcome recent difficulties in advanced credit markets. Financial literacy prepares investors for tough financial times, through strategies that mitigate risk such as accumulating savings, diversifying assets, and purchasing insurance.

Based on the findings, the study recommends that the ministry or agency responsible for SMEs in the state should initiate accounting training programs for entrepreneurs running small businesses, since keeping proper accounts enhances profitability and growth of small scale enterprises, also, emphasis should be stressed on the teaching of basic accounting concepts and skills in every sector.

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