

## Financial Management Practices and Growth of Micro, SMEs of Tanzania

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### ABSTRACT

Micro, SMEs are seen as a motivating force for the promotion of an economy and they contribute enormously to the economic growth of the organization particularly in Tanzania. Due to the lack of understanding of financial management combined with the uncertainty of the business environment often leads Micro, Small and Medium Enterprises to serious problems concerning financial growth. The significant Objective of this study was to explore financial management practices and growth of Micro, SMEs of Tanzania. This research was guided by the following objectives: financial innovations, investing activities, risk management practices and working capital management. Since the Micro, SME population is quite high, the target population for this study was estimated at over 400 management staff from selected Micro, SMEs in Dar es Salaam. The methodology used was simple random sampling technique to select the sample of 85 respondents. Primary data was collected using a self-administered questionnaire. Content analysis was used to analyze qualitative data. The model applied to determine the relative importance of each of the four variables with respect to the growth of Micro, SMEs was multivariate regression model. The study discovered that financial innovations influence the growth of Micro, SMEs of Tanzania to abundant scope. The study recognized that the reason for innovation in an organization growth is to make profit for particular company. Similarly, Investment described as the redistribution of resources from being consumed today to generating benefits in the future. Improvement of an effective business support system is also an important condition for the success of investment capacity building. Respondents strongly agreed that investing requires business support organizations which have a demonstrated capability of penetrating the Micro, SMEs organization. The study concludes that financial innovations influence the growth of Micro, SMEs of Tanzania to a great scope and that the aim for innovation in an enterprise is to make a profit. Consequently, Risk management has become fragment of a strategic constituent of the modern organization's survival and development. Finally, statistical significance between working capital and organization growth, the study found that there is essential need for a compromise between receivables and holding inventory when the organization is to achieve the required profits. Owner/managers of micro, SMEs are recommended by the study that, they should embrace financial innovations in order to produce long term stability and for the firm to have competences. The study also recommends that it is important for Micro, SMEs to invest so that investments can grow to competition against inflation and future reservations. Managers should increase an effective business support system as a key condition for the success of investment capacity building. The study found that there is a need of looking the challenges facing Micro, SMEs of Tanzania.

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### 1. Introduction

The involvement of Micro, SMEs is more than double that of the large manufacturing sector, which stands at 27% of the GDP (the Republic of Tanzania, 2015). Overall, Micro, SMEs create 85% of all new jobs. Estimates show that, in the year 20015, the Micro, SMEs sector had employed about 6,412,354 people, up from 18,928,900 in 2003 (Ebner, 2014). This was an increase of 986,000 persons and consisted of 84.7% of total national employment. The average income of organizations surveyed were about Tshs260, 000/- per month, and/or the minimum legal monthly wage for unskilled workforces in which the year 2010 was Tshs170, 000/-. The share of the Micro, SMEs sector's contribution to GDP was estimated at 28.4 percent. It is recognized that Micro, SMEs constitute a significant portion of the Tanzanian private sector.

In Tanzania, Micro, SMEs have contributed to the extension of price-based signals into areas such as urban service delivery; garbage collection, urban transport, water distribution and manufacturing of a widespread of domestic and commercial appliances (Baum & Wally, 2003).

The significance of Tanzania's Micro, SMEs movement has continued to grow since the sector was brought to the publicity in 1970's. In Tanzania, it widely acknowledged that the promotion of the Micro, SMEs sector is feasible and dynamic strategy for achieving national goals, including employment creation, poverty mitigation and balanced development within sectors. The findings of the 2013 Micro, SME Baseline Survey underscored the important role that Micro, SMEs play in Tanzania's development process, predominantly in the

context of creating employment and income opportunities for the mainstream of poor people throughout the entire Micro, SMEs of the region. Micro, SMEs sector provides employment for considerably more people than does the formal enterprises sector (Anonymous, 2013).

## 2. Problem Statement

Financial management practices and growth is one significant topic in the field of entrepreneurship and Micro, SME sector development as evidenced by an increasing number of publications and studies on the topic. According to Flemming (2014), approximately 84% to 92% of Micro, SMEs fail within 5-10 years. According to the Tanzania Economic Survey 2013, the performance of Tanzanian Micro, SMEs is weak as demonstrated by the deterioration in growth rate from 4.3% in 2010 to a 5.9% in 2013. Such a decline in growth leads to unemployment in Tanzania which as a result leads to social injustices and corruption (Farashah, 2013). Consequently, the behaviors to address the bimodal dissemination of an enterprise where 77% are Micro, SMEs, 27% medium firms, and 28% Micro organization is still an empirical matter (Atow-Zahir, 2012). Failure to organization growth in the Micro, SME sector has for long remained mysterious most especially in the developing countries perspective where the SMEs occupy the large part of the economy (Neumann & Dul, 2005). Studies from developed nations like USA, Japan, and Dubai find financial management practices and growth contribute enormously to Micro, SMEs poor business performance.

Past studies which have studied Micro, SMEs among which Karimi, Chizari, Biemans, and Mulder (2010), found out that Micro, SMEs are not performing to the desired expectations and if this situation is not addressed, then the Micro, SMEs contribution to the growth is likely to be affected. Moreover, these studies had unresolved contradictions applicable to Micro, SMEs thus, calling the study in a developing countries background like Tanzania to be done and assist in establishing the relationship between financial management practices and growth of Micro, SMEs. Consequently, this study is significant not because it fills the gap, but also it sets out to address this gap knowledge.

Locally, studies on financial management practices that have been done include, Farashah (2013) who did a research financial management practices and growth of Micro, SMEs, while Altamony, Tarhini, Al-Salti, Gharaibeh, and Elyas (2016) did research on selected financial management practices as well. None of these local studies has ever focused on financial management practices and growth in Micro, SMEs in the whole of Tanzania. It is in this light that the study investigate to fill the existing research gap by studying the Financial Management Practices and growth of Micro, SMEs of Tanzania.

## 3. Objectives of the Study

### General Objective

The main objective of this study was to explore financial management practices and growth of Micro, SMEs of Tanzania.

### Specific Objectives

- i. To assess the effect of financial innovations of Micro, SMEs of Tanzania.
- ii. To establish whether investment activities affects the growth of Micro, SMEs of Tanzania.
- iii. To determine the effect of risk management practices of Micro, SMEs of Tanzania.
- iv. To find out the effect of working capital management of Micro, SMEs of Tanzania.

## 4. Literature Review

### Financial innovations

Financial Innovation is the process of creating a commercial product from an invention (Paterson, 2009). The study discovered that Financial Innovation can distribute four types of reimbursements besides cash: brand, knowledge, ecosystem, and culture. But the most important reason for financial innovation in an enterprises is to generate a profit. A firm makes a profit by contribution of products or services at a lower cost than its competitors or by contribution distinguished products at premium prices that more than reimburse for the extra cost of differentiation (Smith, 2012).

Salum et al. (2017) attributed the emergence of new ideas for product innovations in Micro, SMEs to entrepreneur. Micro, SMEs very actively explored new product ideas and the most frequent way of achieving this included contacts with customers. Altamony et al. (2016) recognized demand positioned on commercial by clients/customers, nearby working relationships with a key important customers and close analysis of competitor products are the major drivers of innovation in Micro, SMEs covered in four different countries like USA, UK, Dubai, and France.

### Investment Practices

Investment practices can be defined as the redistribution of resources from being consumed today to create benefits in the future organization growth (Mori, Kazungu, Mchopa, & Box, 2014). Micro, SMEs have to use assets to earn income or profit. Though it is no longer a negotiating society where goods and services were often more perishable, it is preferable, if not essential, to invest instead of keeping assets idle, so that more investments can lead to growing to compete alongside inflation and future uncertainties for the business growth. Micro, SMEs must be able to respond more rapidly and professionally to global market signals to take advantage of investment opportunities and acquire the benefits of the global trading system. Although they want to be more competitive and higher productive of goods and services in an organization. However, effective organizational business support systems are required to improve more competitiveness and high productivity and growth of Micro, SMEs. It is also observed that the development of an effective organizational business support system is a significant factor for the success of investment for capacity building business growth. Investing activities for organization growth require business support agencies (including financial organization) and government support which are customer-oriented as well

as demonstrated capability of penetrating the Micro, SMEs sector.

Consequently, multinational enterprises are looking out for new markets and investments offer capable Micro, SMEs the opportunity to pullout themselves to an international value chains through commissioning relationships. Though those that are incompetent to do so and organizations had progressively face the danger of losing their existing markets. Although the competition within the developing global world for export markets, foreign investment activities and organization resources are also intensifying. Against this backdrop of increased global competition, Micro, SMEs associations, support institutions, and governments in transition and developing global countries have to adjust and adopt new organization approaches as well as formulate new ways of working together to adoptive Micro, SMEs competitiveness

**Risk management**

Risk management is defined by Maehr, (2008) in Baum and Wally (2003) as “the identification, analysis and economic control of those risks which threaten the assets as well as earning capacity building of an organization”. Management of risk has explicitly or implicitly become an important part of a strategic planning component of the modernized organization’s survival and development of the enterprises (Atow-Zahir, 2012). Though risk can be considered as the probability of economic or financial gains or losses, as a significant consequence of the ambiguity in associated with undertaking a course of action (Baum & Wally, 2003). Risk encompasses all human engagements, various categories of business organization as well as every area of management of a company. Although, risk management can be more so predicted on the basis of experience, trying to better govern the disorder of an organization business growth. Risk Management has the responsibility of identifying risks, and treating risks, determining the probability and the possible control of events, reducing or eliminating their effect with the minimum investment of resources for business growth. Risk Management is being more developed in business growth as well as global adopted in a lot of fields within enterprise management.

In the developed and developing countries all over the global world, micro, SMEs are considered significantly important to the growth of any organization economy. Micro, SMEs require the adoption of a risk management strategy as well as methodology because they lack the resources to respond promptly to external and internal threats, causing the potentially enormous losses that extremely threaten their survival.

Studies by the Singapore Government (2012) and the Chartered Accountants Institute in Wales and England coincidentally prove that the most significant risk among small businesses involves human factor. A large number of employee turnover and a shortage of know-how experts both result in wastage of manpower and the additional cost of training. In long term, the human factor will lower the productivity and affect the brand image of small businesses as an employer (Richard, Devinney, Yip, & Johnson, 2009).

**Working capital management**

The study was done by Mori et al. (2014) entitled “effects of working capital management and growth of Micro, SMEs profitability in Spain” found a significant negative association between working capital management and MSME profitability. Invariance to the findings of Mori et al. (2014), the results from the study conducted by Altamony et al. (2016) indicate significant positive correlations between working capital business components with firms’ performance in Malaysia. Majama and Magang (2017) investigated the effects of working capital management and growth on the profitability of a sample of SMEs of Spanish firms. Consequently, the findings revealed that owners/managers can create value by reducing their inventories as well as the number of days for which their accounts are outstanding.

**Performance and Growth of Micro and SMEs**

Performance is one of the most important objectives of financial management growth because the goal of financial management is to maximize the owner’s growth wealth (Mori et al., 2014). Performance and growth is an important in determining the failure or success of a business. At the initial stage, a business organization may not be profitable because of investment activities and expenses for establishing the organization business in these Micro, SMEs. When a business organization becomes more mature, organization’s profits have to be produced in an enterprise’s growth. Due to the importance of performance, Baum and Wally (2003) among other researchers have suggested that small firms need to concentrate on performance and growth. Richard et al. (2009) found performance to be a significant determinant of a small firm’s credit risk. Salum et al. (2017) stress the aim of a business organization is not only the growth of sales but also the achievement of organization profits. Profit is more important because it is the most requirement for the survival of the business of the organization. Low performance contributes to under-capitalization problems due to retained earnings and therefore to be more confidence on external capital (Richard et al., 2009).

**5. Data Analysis/Findings**

**Regression analysis**

This discussion of the results of inferential statistics has critically described here. The analysis used multiple regression analysis to determine the relative importance of each of the variables with respect to the financial management practices and growth of Micro, SMEs. IBM-SPSS statistical package has used to enter and compute the measurements of the multiple regressions for the study. The summary of the findings are presented in the following tables;

**Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.948 <sup>a</sup>	.899	.705	.514

Source: Research, 2018

- a. Predictors: (Constant), risk management practices, investment activities, financial innovations, and working capital management.

- b. Dependent Variable: management of financial practices and growth

For each variable the Coefficient of determination in this study demonstrate the extent to which changes in the dependent variable can be demonstrated by the transformation in the independent variables as well as the percentage of variation in the dependent variable (financial management practices and growth of Micro, SMEs) that is explained by all the 4 independent variables (risk management practices, investment activities, financial innovations, and working capital management).

The this study independent variables which were studied, explain 89.9% of the variance in financial management practices and growth of Micro, SMEs particularly in Dar es Salaam as represented by the R<sup>2</sup>. This means that other factors not studied in this research contribute 10.1% of the variance according to the dependent variable. Hence, it is recommended that further research should be conducted to establish the financial management practices and growth of Micro, SMEs.

**ANOVA (Analysis of Variance)**

Model		Sum Squares	Df	Mean Square	F	Sig.
1	Regression	40.566	3	0.374	86	.001a
	Residual	4.686	7	0.366		
	Total	45.252	11			

Source: Research, 2018

- a. Predictors: (Constant), risk management practices, investment activities, financial innovations, and working capital management.
- b. Dependent Variable: management of financial practices and growth

The Analysis of Variance described that F critical value at level 5% of significance was 5.33. Whereas the ANOVA which is the value of F calculated is greater than the value of ANOVA which is F critical (value = 86.0), as a result, it shows that the overall model of the study was significant. Since the significance is less than 0.05, so it is indicating that the predictor variables, explain the study variation in the dependent variable whereas financial management practices and growth of Micro, SMEs. Consequently, if it could be observed that the significance value of F was larger than 0.05 then the independent variables would not explain the study variation in the dependent variable of the model.

**Multiple Regression Analysis**

Model	Unstandardized Coefficients B	Standardized Coefficients Std. Error	Beta	T	Sig.
1. (Constant)	3.31	0.79		6.55	0.01
Financial innovations	2.188	0.261	0.28	0.27	0
Investment activities	2.064	0.248	0.57	0.25	0.03
Risk management practices	1.443	0.551	0.33	0.18	0
working capital management	1.252	0.547	0.33	0.12	0

Source: Research, 2018

- a. Predictors: (Constant), risk management practices, investment activities, financial innovations, and working capital management.
- b. Dependent Variable: management of financial practices and growth

The regression findings model

$$\hat{Y} = \hat{\beta}_0 + \hat{\beta}_1 X_1 + \hat{\beta}_2 X_2 + \hat{\beta}_3 X_3 + \hat{\beta}_4 X_4$$

The substitution of the regression equation becomes like this

$$\hat{Y} = 3.310 + 2.188X_1 + 2.064X_2 + 1.443X_3 + 1.252X_4$$

Where  $\hat{Y}$  is the dependent variable (financial management practices and growth of Micro, SMEs),  $X_4$  is the working capital management,  $X_3$  is risk management practices,  $X_2$  is investment activities, and  $X_1$  is financial innovations.

According to the equation, taking all factors (financial innovations, investment activities, risk management practices, and working capital management.) constant at zero, financial management practices and growth of Micro, SMEs will be 3.310. The data findings also show that a unit increase in financial innovations, variable will lead to a 2.188 increase in financial management practices and growth of Micro, SMEs;

a unit increase in investment activities will lead to a 2.064 increase in financial management practices and growth of Micro, SMEs; a unit increase in risk management practices will lead to a 1.443 increase in financial management practices and growth of Micro, SMEs; and a unit increase in working capital management will lead to a 1.252 increase in financial management practices and growth of Micro, SMEs. The analysis concludes that the most significant factor is financial innovations.

**6. Performance and Growth of Micro, SMEs**

From the analysis of findings, the respondents from the study strongly agreed with the statement that Performance is very significant in determining the failure or success of a business, in this case, Micro, SMEs of Tanzania. Secondly respondents agreed with the statement that the aim of a business is not only the generation of high sales as well as generation of profits which influences the performance and growth of Micro, SMEs of Tanzania; Thirdly respondents agreed with the statement that Profit is especially important because it is necessary for the survival of a business, therefore, influencing performance and growth of Micro, SMEs of Tanzania; finally respondents indicated that Low performance contributes to under-capitalization problems because it leads to retained earnings as well as reliance on

external capital which influences the performance and growth of Micro, SMEs of Tanzania.

The study findings relate with literature review by Salum et al. (2017) who indicated that the aim of a business organization is not only the generation of high sales as well as generation of profits for an organization growth. The study observed that profit is especially important because it is necessary for the survival of a business organization and Low performance contributes to under-capitalization problems because it contributes to retained high incomes and therefore to a dependence on external capital for the organization growth.

## 7. Conclusions

The study concludes that financial innovations influence the performance and growth of Micro, SMEs of Tanzania to a very great extent and that is the reason for organization's innovation is to make a profit. Also SMEs Financial innovation is essential in order to develop long term stability of the business and that Innovation requires the organization to be competencies in relating to current technology. The study concludes that customer perspective of innovation demands a change in technology as well as consumer behavior in organization to accommodate new product usage conditions in business growth.

Consequently, the study concludes that Business Investment can be demonstrated as the redirection of an organization resources from being consumed today to creating benefits of organization in the future; that It is

significant to invest in an organization so that investments can grow the enterprises to fight against inflation and future uncertainties and that Development of an effective business organization support system is also a key condition for the success of investment capacity building of an organization, while investment requires business organization support agencies which have a demonstrated capability of penetrating the Micro, SMEs sector.

The study also concludes that Risk Management has become part of business strategic planning component of the modern organization's survival and development of an enterprises; that risk management can also be seen as the possibility of financial or economic losses or gains; that Micro, SMEs require the adoption of an enterprises risk management strategy for business growth and methodology; and that the most significant risk among small businesses involves human factor.

Finally, the study concludes that there's a statistical significance between business working capital and organization performance and growth. There is a highly significant negative relationship of an organization between the time it takes for an enterprise to collect cash from their customers development. Heavy business investment in inventory raising up business capital which in the end decreases organization' profitability. Also, in business growth there is a need for compromise between organization receivables and holding business inventory if the organization is to achieve the required profits.

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