

CASH MANAGEMENT PRACTICES IN MICRO AND SMALL BUSINESSES IN MALAYSIA

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ABSTRACT

Cash management is important for all businesses to strengthen their financial management and financial survival. Each business needs to have high level of cash management practices to meet the business purposes. Therefore, this study explores the extent of cash management practices applied in the micro and small businesses in four main states in Peninsular Malaysia. Overall findings of this study showed that cash management practices in these states are high. However, the results show that the internal control on cash management has very low implementation level. Thus, the capital providers need to re-educate the entrepreneurs on the importance of having good internal control on cash management in order to avoid any manipulation, cash shortage and other financial issues. Besides that, the result of this study is important to ensure the effectiveness of cash management in order to be able to support the financial sustainability of the business.

Keywords: Cash Management Practices; SMEs; Malaysia

Introduction

Small Medium Enterprises (SMEs) play an important role in the economic growth, especially in the developed and developing countries (Ahmad, 2012). However, despite the contributions of small businesses to the local economy, including fostering the Gross Domestic Product (GDP), alleviating poverty, and creating jobs, SMEs worldwide are highly prone to failure. This problem happened when the entrepreneurs have limitation in handling the business from the financial aspect and the non-financial aspect. According to Abdul and Ahmad (2013), the financial limitations in SMEs are that the business is unable to manage the cash flow and unable to generate enough sales and revenue. In terms of the non-financial aspect, the failed business has issue with service quality, owner experience, customer satisfaction and competitors.

Besides that, Aren and Sibindi (2013) revealed that the majority of SMEs failed due to poor cash management. It is because there are inevitable links between small business failures and poor or careless financial management (Drever & Hartcher, 2003). Moreover, only certain SMEs prepare good cash flow, as others are unaware or unconvinced of the benefits of accounting and financial reporting requirement for the purpose of control and also for decision-making (UNCTD, 2000).

This study is able to fill the gaps since there are limited literatures on cash management in Malaysia. This issue of cash management practices only arises in other countries for examples, a study by Alala, Deya and Busaka (2013) in Kenya and Uganda, a study by Aren and Sibindi (2013) done in South African Retail Sector and a study by Gilbert, Nellson and Nicholas (2013) in Northern Uganda. Therefore, this study aims to explore the current cash management practices in micro and small businesses in Malaysia for the service sector.

The contribution of this study is at least twofold. First, this study provides some insights on cash management practices in micro and small businesses. Second, this study could assist the regulators in governing the policy on financial management specifically on cash management. The paper proceeds as follows: section 2 reviews the literature review on cash management practices. Section 3 describes the research method including the sample selection and instrument used. Section 4 presents the results of the study, and the final section concludes the study and addresses its limitations and suggestions for future research.

Literature Review

Cash management practices

Cash management is the business strategy in managing cash for the purpose of optimizing liquidity (Linert, 2009). Deb, Dey and Shil (2015) specifically defined cash management as the managing of (i) cash flows into and out of the firm, (ii) cash flows within the firm, and (iii) cash balances held by the firm at a point of time. Each business needs to have proper cash management to achieve the targeted goals and objectives by enhancing their allocation and planning in the cash. From that, a good cash management will ensure that the business can achieve their main objectives in the long term period and plan for a good strategy.

Although cash management is a good and important practice, many of micro and small businesses do not practice it (Jayabalan, Dorasamy, Roman & Ching; 2009; Sunday, 2011; Alala, Deya & Busaha, 2013). According to Abanis, Sunday, Burani and Eliabu (2013), among the serious issue in cash management practices is that some of the businesses do not have bank account to track and control their business income and expenses. If they have the bank account, the business would be able to reduce the tendency of cash shortage, set minimum cash balance and have monthly reconciliation of cash book with the bank to monitor their cash.

The business also needs to have internal controls for cash management for example, sell their goods and provide their services using cash. Good internal control also requires the separation of duties in managing cash including the separation of the cashier personnel from the accounting duties. Besides that, the business needs to appoint the person that has the skill and ability to do the budgeting. Some businesses give the responsibility to do the budgeting to the owner or manager who has self interest in the business. Nonetheless, the persons are that involved with the budgeting need to avoid conflict of interest to ensure that they review the cash budget to identify if the budget is prepared based on business needs.

Importance of Cash Management Practices

The cash management practices are essential for every business to increase profitability, sustainability, and future planning. Cash management practices also include cash budgets and cash flows. Cash management is important in describing the inflow and the outflow of cash, which refers to the movement of cash in the receiving to payment cycle. Cash management also is the most crucial task for entrepreneurs (Avika & Hari, 2014) in order to maintain the profitability and sustainability of their businesses. Besides that, poor cash management can also become challenging when it is employed to maintain the skill and knowledge among employees.

In addition, according to Evans (2012), cash flow management helps SMEs to maintain an optimal cash balance, that is, it is neither in excess nor in deficit. It can minimize the positive items and maximize the negative items that affect the cash cycle. Besides that, cash management also helps in spotting potential cash flow gaps. In particular, cash management serves as a reference tool for seeking funds from bankers, and in enhancing effectiveness. Furthermore, cash flow is an important measurement used by investors for evaluating business because cash management focuses on the actual operation, eliminates one-time expenses and non-cash charges, and indirectly, it will give a clear picture of what the company is truly doing. Hence, efficient cash flow management system plays a vital role and helps to demonstrate if an SME is profitable (Minnery, 2006).

Moreover, proper cash flow management can prevent a business from bankruptcy, and therefore, profitability and sustainability of the business are ensured (Inc., 2013). In fact, proper and efficient management of cash is imperative towards the growth of small businesses. Usually, the cash flow of a small business could become a problem when the business deals with a number of customers who are difficult to be tracked and when the business sells products due to higher demand compared to the competitors (Inc., 2013). These problems can be avoided if cash flow is managed properly.

Issues in Cash Management Practices

Muinde (2013) contended that the Small and Medium Enterprises (SMEs) play a vital role in economic contribution, property alleviation and employment. However, SMEs faced a number of constraints especially in practicing cash management. According to Abanis, Sunday, Burani and Eliabu (2013), among the weaknesses that occur in micro enterprises in terms of cash management is that, most owners do not have bank account to record their sales. This problem occurred because they do not have experience in managing enterprise. This may cause the owner to be incapable in managing their cash if there is any shortage of money. In addition, unavailability of book account can minimize the ability of owner to monitor their cash flow and manage the usage of their cash ("The importance of keeping on top of your business accounting records", 2015). Besides that, monthly reconciliation of cash book with the bank to monitor their cash is important to each enterprise. From that, the owner may be aware if there is any cash problem and would be able to improve their cash practices.

In addition, internal control plays a vital role in cash management practices. However, only some owners practice internal control and are aware of its importance. Those enterprises that sell their goods or services by cash must have proper internal control. In order to improve internal control, owner of enterprise may have separation of duties in managing cash. Besides that, the other element of cash management practices in the enterprise is the ability of the person that is responsible to prepare the budget. Some enterprises give the responsibility to do the budgeting to the owner or the manager. Then, the owner or manager needs to review the cash budget and identify if the budget is prepared based on their needs. In addition, the internal control can help the owner to identify their opportunities and strength of the enterprise (Jim, 2015). Moreover, Abanis et al. (2013) concluded that the person that is responsible in preparing the budget is important because good budget preparation may influence the practices of cash management in the enterprise.

The researches done in South Africa and Uganda proved that cash management practices in SMEs are poor (Avika & Hari, 2014; Abanis et al., 2013). A number of small businesses are being managed without appropriate strategy and with poor skills in cash management. The efficiency of a business in managing cash may influence the growth of business operations. Failure to do so can affect business operations, as sustenance of business operations can come to a halt. Marion (2011) proved that out of five, three businesses failed within a short period of time - three years. It shows that in order to be successful in business, entrepreneurs must possess good strategies and ensure that they can achieve their targets. Besides that, according to Gupta, Wilson, Gregorioua and Healya (2014), evidences pertaining to SME financing strongly indicate that firms which are unable to generate sufficient operating cash flow (OCF) are more susceptible to bankruptcy.

According to Gilbert, Nelson and Nicholas (2013), problems in cash management practices occur when the management takes for granted the importance of managing cash. This happens when the entrepreneur does not focus on cash management. This will directly affect business operation. When businesses do not prepare cash management, they will be unaware if there is any loss in the business. Then, when the businesses realize the loss and the need to recover, loan is obtained from the bank. This will cause the winding up of the businesses as they fail in improving their cash to cover the losses, and are unable to pay their loans.

According to Avika (2014), one of the reasons for failure in cash management is the reluctance among entrepreneurs to prepare cash statements, such as cash inflow and cash outflow, due to the time constraint that they face. Another issue in cash management failure is that some businesses do not control and monitor their sales and income. These problems will cause businesses to have insufficient money to cover their expenses. Moreover, due to this issue, statistics have proven that 40% of small businesses fail within the first ten years as the businesses fail to stand and sustain for a long period. As revealed in the statistics, most businesses fail in cash management because they find it difficult to improve their performance and growth. For that case, only 9% out of 60% have a chance to recover their businesses.

Research Methodology

Sample selection

To achieve the objectives of this study, micro and small enterprises were selected as the respondents. The reason for this selection is because they have the largest number of establishments in SMEs which represent 92% of the total SMEs (Economic Census, 2011). This study specifically chose the micro and small enterprises from the service sector which constituted 90% or 580,356 establishments, and contributed the gross output in total of RM218.8 billion in year 2011. Besides that, the total of value of gross output and value added for service sector is RM286.6 billion (41.3 % of total gross output) and RM165.3 billion (42.9% of total value added) in year 2011. Further, small enterprises had the highest contribution to gross output and value added with the respective shares of 45.8% and 46.3% respectively (Economic Census, 2011).

Specifically, the micro and small enterprises from the service sector was selected from four states in Malaysia. The four states are Selangor, Wilayah Persekutuan Kuala Lumpur, Perak and Kelantan. Selangor has one of the largest numbers of SMEs, followed by Wilayah Persekutuan, and Perak (Economic Census, 2011). In this study, Kelantan was selected because Kelantan has the largest number of micro business in SMEs which is 93.1% (Economic Census, 2011). Therefore, a total of 200 questionnaires were distributed equally to these areas using the simple random sampling.

The questionnaire: construction

The questionnaire consists of two parts. The first part covers the Demographic profile (D), which gathers information of the business. There are six questions in this part. The second part of the questionnaire comprises of 11 questions to test the level of cash management practices in these businesses. The questions were adopted from Abanis et al. (2013). In this part, the respondents are instructed to show the extent of their agreement or disagreement using a four-point Likert-type scale, ranging from 4 for “strongly agree” to 1 for “strongly disagree”.

According to Abanis et al. (2013), the cash management practice can be interpreted in the range of very high to very low based on the following legend:

Table 1: Extent of Cash Management Practice

| Mean range | Response mode | Interpretation |
|------------|-------------------|----------------|
| 3.26-4.00 | Strongly agree | Very high |
| 2.51-3.25 | Agree | High |
| 1.76-2.50 | Disagree | Low |
| 1.00-1.75 | Strongly disagree | Very low |

Data Analysis

Frequency Distribution of Demographic Variables

Table 2 shows the demographic profile of the respondents.

For the socio-demographic profiles, a total of 168 businesses (84%) had less than five staffs and 32 businesses had five to 19 staffs. In terms of last year's annual sales, 110 respondents (55%) reported annual sales of RM100,000 and below, 50 respondents had RM100,001-RM200,000 sales, 24 respondents (12%) had RM200,001-RM300,000 and 26 businesses reported earning between RM300,001-RM500,000.

In terms of capital, the majority of respondents (53.5%) started their business using their own fund. Meanwhile, other entrepreneurs obtained their fund from other capital providers including Majlis Amanah Raya (MAR), Malaysian Investment Development Authority (MIDA), Tabung Ekonomi Kumpulan Usaha Niaga (TEKUN), SME Corporation Malaysia (SME Corp.) and Amanah Ikhtiar.

Table 2: Demographic profile

| | | Frequency | Percentage |
|-------------------|---------------------|-----------|------------|
| Number of staff | Less than 5 | 168 | 84.0 |
| | Between 5-19 | 32 | 16.0 |
| Annual sales (RM) | RM100,000 and below | 110 | 55.0 |

| | | | |
|---|--------------------------------------|-----|------|
| | RM100,001-RM200,000 | 50 | 25.0 |
| | RM200,001-RM300,000 | 24 | 12.0 |
| | RM300,001-RM400,000 | 13 | 6.5 |
| | RM400,001-RM500,000 | 3 | 1.5 |
| Capital provider | MARA | 46 | 23.0 |
| | MIDA | 5 | 2.5 |
| | TEKUN | 30 | 15.0 |
| | SME Corp. | 7 | 3.5 |
| | Private | 107 | 53.5 |
| | Amanah Ikhtiar | 5 | 2.5 |
| Types of service | Bookshops | 13 | 6.5 |
| | Clothing, handbags and footwear shop | 80 | 40.0 |
| | Health and social services | 6 | 3.0 |
| | Restaurants and cafe | 37 | 18.5 |
| | General Household items | 24 | 12.0 |
| | Computer and IT services | 4 | 2.0 |
| | Boutique | 21 | 10.5 |
| | Printing services | 3 | 1.5 |
| | Laundry shop | 3 | 1.5 |
| | Others | 9 | 4.5 |
| Accounting records | Yes | 193 | 96.5 |
| | No | 7 | 3.5 |
| The person who handles the accounting records | Accountant | 5 | 2.5 |
| | Cashier | 80 | 40.0 |
| | Nobody handles them | 2 | 1.0 |
| | Manager/owner | 109 | 54.5 |
| | Clerk | 4 | 2.0 |

80 businesses (40%) for this study were retail shops that sell clothing, handbags and footwear, followed by 37 (18.5%) which were restaurants and cafés. The business that sold general household items were 24 (12%) while 21 (10.5%) were boutiques. Less than 10% of the respondents were bookshops, health and social services, computer and IT services, printing services and laundry shops respectively.

In terms of accounting records, 193 (96.5%) of respondents prepared all the transactions in the accounting records completely and only 7 (3.5%) did not prepare it. Half of the respondents (54.5%) agreed that this preparation was done by the manager/owner, followed by cashier (40%), accountant (2.5%) and clerk (2.0%).

Extent of Cash Management Practices

From Table 3, the results indicate that cash management practices are very high among micro and small businesses. This shows that most businesses applied good practices in managing their cash. However, this result contradicts with the result from Abanis et al. (2013). This may be caused by the micro and small businesses in Malaysia having more awareness on the importance of cash management practices. However, results of the internal control on cash management are consistent. In Malaysia, the entrepreneurs have some weaknesses in their practices where the internal control on cash management was not properly implemented, for example, the owner/manager was involved in the preparation of cash budget. Besides that, in terms of preparing the accounting records, most of the cashiers were involved in this accounting process. These practices need to be avoided since they may lead to bias and manipulation in their recording.

Table 3: Extent of Cash Management Practices

| | Item | Mean | Interpretation | Rank |
|------|---|-------------|----------------|------|
| CP1 | This business only sells goods or provides services in cash. | 3.77 | Very high | 1 |
| CP2 | This business sets the minimum cash balances based on owner/manager's experience. | 3.22 | High | 2 |
| CP3 | This business monitors the cash budget. | 3.21 | High | 3 |
| CP4 | This business has a bank account. | 3.17 | High | 4 |
| CP5 | This business prepares the cash budget. | 3.13 | High | 5 |
| CP6 | This business receives and has a monthly bank statement. | 3.11 | High | 6 |
| CP7 | This business has internal control on cash. | 3.01 | High | 7 |
| CP8 | This business has never faced a shortage of cash. | 2.95 | High | 8 |
| CP9 | This business always has a cash surplus. | 2.88 | High | 9 |
| CP10 | The cashier is not involved in any matter of accounting records. | 2.36 | Low | 10 |
| CP11 | The owner/manager is not involved in the preparation of cash budget. | 1.75 | Very low | 11 |
| | Average mean | 2.96 | High | |

Conclusion And Discussion

The findings of this study revealed that the businesses implement high level of cash management practices. However, the cash management practices are still poor in terms of the internal control of cash management practice particularly on the person who is involved in the accounting record and the preparation of cash budget. The result of this study is important to entrepreneurs in evaluating their current cash management practices. It is important to ensure that they are aware of the benefits of cash management including strengthening business efficiency, improving the performance and enhancing long term survival of the SMEs. Besides that, the government and the capital provider also need to have more proactive roles in educating the entrepreneurs on the best ways to manage the cash including planning cash flows, monitoring cash flows and controlling cash flows in order to support the financial management.

This study has some limitations. The respondents of this study are only covering four states which are Kuala Lumpur, Selangor, Perak and Kelantan. Future study needs to explore this issue in other states to ensure that the result can be generalized to the whole Malaysia. Besides that, this study selected only the micro and small businesses in the service industry. Therefore, other researchers can extend the study to medium businesses in other industries and also identify the factors that influence the implementation of good cash management practices. Besides that, future researchers also can investigate the factors that influence SMEs in implementing the cash management practices.

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