

Impact of SMEs' financial reporting practices on their creditworthiness in Zimbabwe.

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Abstract

The purpose of this paper was to investigate and analyse how the financial reporting practices of the SMEs influence their ability to get funds from lending institutions. The study was grounded upon the mixed methods methodology. This methodology enabled the identification of both numerical and non-numerical consequences of the lack of financial reporting as a barrier to finance for SMEs. Explanatory Sequential design was used. Forty (40) owners representing different SMEs in diverse economic areas made up the study's population. A sample had to be chosen after the study population was chosen. Purposive or judgmental sampling was employed in this study. To obtain first-hand knowledge from the respondents, primary data was gathered through interviews, and questionnaires. Questionnaires were used to gather quantitative data while interviews were used for qualitative data. It was found out that most SMEs in Zimbabwe are failing to access credit facilities since they are not producing standard financial reports. Most respondents alluded that preparation of the financial statements is costly and would surely eat up upon the working capital of SMEs. As a recommendation, SMEs are encouraged to try to engage qualified Accountants who can interpret the IFRs for SMEs. More so the IASB should simplify the IFRs for SMEs such that the SMEs manage to make use of this crucial framework. The current position with financiers is that SMEs are failing to provide them the information they require. Therefore, there is need to upgrade the information systems and close the information gap that exists between the SMEs and the financiers.

Key words; SMEs Financial Reporting Practices, Creditworthiness, SMEs, IFRs for SMEs

1.0 Introduction

Most SMEs are started by entrepreneurs with little prior expertise and sometimes even limited exposure to an established corporate environment. Additionally, SMEs lack the trained staff needed to manage their operations, especially the financial accounting practices. They cannot provide audited financial accounts, which are necessary to obtain funding and other forms of financial aid, hence they are unable to publish high-quality financial reports like large corporations can.

SMEs also face the issue of having insufficient capital bases, which banks demand as collateral security before extending any credit. To improve financial management in SMEs, current research emphasises the creation of reliable accounting systems in these businesses. Is financial reporting important for SMEs? Can it ensure financial assistance in Zimbabwe? Would this enhance financial reporting in these businesses? The purpose of this paper is to investigate and analyzing how the financial reporting practices of the SMEs influence their ability to get funds from lending institutions.

1.1 Background to the Study

The background of the study was divided into the importance of SMEs and an exposition of the SMEs accounting practices. The importance of SMEs was exposed through showing the contribution of the SMEs to the economies of several nations in the world including Zimbabwe.

1.1.1 Why SMEs are important Globally

Essentially, the SMEs have considerable and respectable impact on Gross Domestic Product (GDP) of most countries to the extent that SMEs contribute between 16% to 20% to GDP in most developing countries and high-income countries, SMEs perform much higher and contribute more than 50% to GDP (Haselip et al, 2014). In emerging economies like Malaysia, where many public companies are family owned, the minority shareholders bear a disproportionate amount of the cost of bad corporate governance. A crucial necessity for greater financial disclosures and more transparent business reporting is to have effective corporate governance processes.

Over 50% of business entities and 90% of all jobs are in SMEs, and formal SMEs in emerging economies can contribute up to 40% of the country's GDP (World Bank 2022). When informal SMEs are considered, these figures are substantially higher than the aforementioned figures. . According to a projection by the World Bank, 600 million jobs

would be required by 2030 to accommodate the expanding global labour force, making the development of SMEs a top priority for many governments globally. SMEs development engines are now extensively acknowledged in the African region, according to study by a scholar (Otman 2021).

Since financial access is the second most frequently stated barrier to SMEs' ability to expand their operations in emerging markets and developing nations, it serves as a restraint on SMEs expansion. The microfinance gap in Africa is US\$57 billion, while the financing gap for small- to medium-sized businesses is US\$138 billion (World Bank, 2022). SMEs are currently driving industrial expansion in many North African nations. For the SME items produced in the African continent to be marketed globally, there must be market expansion in the continent. In fact, corporate growth will diminish without the precision and focus of a business strategy, which will result in a sharp slowdown in the expansion of domestic and regional sectors. SMEs in North Africa should be supported in expanding and participating fully as strategic bridges for relevant stakeholders who can provide guidance on policy advocacy and create a competitive business environment.

Most firms in Egypt are tiny, with 97 percent having fewer than ten employees. Around 2.7% of all businesses, from little stalls to large corporations, are medium-sized businesses with 10 to 50 employees. Large companies with more than 50 employees make up 0.4% of all firms in the country (CIB, 2020) the existence of SMEs can spur commerce, allowing the African food industry to continue and learn about cutting-edge technologies and new market trends.

SMEs are the main drivers of economic growth in Zimbabwe, accounting for more than 70% of all economic activities, more than 60% of all jobs, and more than 50% of GDP (RBZ, 2016).

The importance of the SME sector is well recognized worldwide due to its significant contribution to gratifying various socio-economic objectives, such as higher growth of employment, output, promotion of exports and fostering entrepreneurship (Keksin, Senturk, Sungur, and Kiris, 2018). In the European Union countries, for example, there are some 25 million small businesses, constituting 99% of all businesses; they employ almost 95 million people, providing 55% of total jobs in the private sector. Important contribution is also on exports and on productivity growth (OECD, 2004). Keksin, Senturk, Sungur, and Kiris (2018) note that SMEs have taken on a significant role as advocates of a healthy and effective economic development in developing nations over the course of the 20th and 21st centuries.

As a result, several nations are establishing structures and regulations to encourage SMEs' growth. The National Micro, Small and Medium Enterprises Framework was developed in Zimbabwe by the Ministry of Small and Medium Enterprises and Cooperative Development in 2018. (2019-2018 period) (<https://www.veritaszim.net/node/663>).

According to the Ministry of SMEs and Corporative Development's 2018 report, SMEs play a significant role in Zimbabwe's development efforts, contributing 60% of the country's GDP and an estimated 50% of all jobs (Research Council of Zimbabwe, 2019). The idea of "firm financial performance" encourages the effective and efficient use of financial resources to meet overall business goals, which include maximizing profit and shareholder wealth (Urhoghide & Omolaye, 2017).

SMEs development can help Zimbabwe's government and professionals address the country's growing trade deficit (Mudavanhu, Mubata & Mudavanhu 2014). Small and medium-sized enterprises (SMEs) have the power to strengthen Zimbabwe's economy and contribute to the creation of the crucial jobs required to combat the country's extreme levels of unemployment and poverty. SMEs can be a strategy to enhance trade balance and livelihoods given the country's current stagnant export growth trend and trade deficits (Calabr & Mussolino 2013). Sanderson (2019) added that arrangements for supporting SMEs have been made in the Zimbabwean financial institution Zim-Asset.

1.1.2 SMEs Financial Accounting and reporting Practices

Musah (2017) investigated the advantages and difficulties of SMEs' bookkeeping and accounting methods, as well as their impact on performance and growth in Ghana. The purpose of the study was to determine the types of bookkeeping and accounting practices used by SMEs, the degree to which these practices' information supports the performance and growth of SMEs, the general attitude of SMEs owners toward these practices, and the difficulties faced by SMEs entrepreneurs in these practices. The study's findings revealed that although most SMEs do not maintain comprehensive bookkeeping and accounting records due to a lack of accounting skills, these owners generally have a good attitude toward keeping accounting records.

Nyathi et al. (2018) conducted research on how accounting data contributes to the development of SMEs in Zimbabwe's Harare. According to the study's findings, most small and medium-sized businesses don't even maintain any accounting records. It was noted that persons who solely keep personal journals do not have enough knowledge to support

economic decision-making. The survey also showed that small and medium-sized businesses store accounting data more for security than for decision-making. This was linked to the inability to apply decision-making techniques like ratio analysis due to a lack of accounting understanding. It was shown that the majority of small to medium businesses did not use accounting data as a decision-making tool. Additionally, it was discovered that SMEs in Harare use non-skilled accounting personnel, which make their information unreliable and inadequate for decision-making purpose.

Lack of credit information has a role in the limitations SMEs confront because determining their creditworthiness is a difficult task. An SME may find it more challenging to establish credit than a larger company since they have less access to traditional sources of funding like banks and other financial institutions, whose information is frequently used to create credit reports. SMEs also frequently lack access to fixed assets, such land, or buildings, which banks typically require as security to receive loans. Instead, moving assets are the main source of financing for SMEs. To provide proper legal and institutional protections, it is necessary to find alternatives to conventional collateral-based lending and use collateral registries.

1.2 Research Questions

- i) What are the effects of SMEs financial reporting practices on their ability to access financing from lending institution
- ii) What are the problems being faced by SMEs in the production of financial reports?

1.3 Literature review

A critical review of literature was carefully done.

1.3.1 SMEs financial reporting practices and their Creditworthiness.

SMEs, like any firms make use of accounting practices. However, their financial reporting practices are usually substandard since they lack the necessary expertise. Thus, they cannot afford the costs of hiring the professional accountants and auditors. It is crucial to note that the failure to prepare the standard financial statements has negative impacts upon the way financiers view SMEs.

The SMEs financial reporting practices are generally poor. This was echoed by Chilembo (2021) who reiterated that SMEs ought to improve on their business record keeping such as

cash flows and income statements for them to attract potential sources of finance such as venture capital investors and/or angel investors. Due to a lack of efficient financial management abilities, SMEs are unable to accurately identify and communicate their funding needs or to provide reliable financial information reporting. This surely disadvantages the SMEs when it comes to accessing loan facilities since their creditworthiness is highly compromised on this note.

According to Musah (2017), SMEs have a sizable "unexpressed desire" for external financing (SMEs are not able to judge when and how much financing they need). Another sign of their poor cash management skills may be the fact that roughly one-third of SMEs ask for loans to refinance their debt. Hence the financiers use qualitative criteria to screen loan applications basing on SME proprietors' expertise and their loans repayment records (Musah 2017). This is used to identify the weaknesses of financial accounting/ management practices of SME firms.

Business risk and genuine profitability are difficult to estimate due to low financial statement reliability and insufficient disclosures (especially because of operations in the informal economy), which further restricts access to finance and raises costs. According to the World Bank (2017), SMEs rarely provide specific information about the maturity structure of their stocks, inventory, unfinished goods, and receivables and payables. The present component of debt held by SMEs is sometimes not distinguished from long-term debt, and related party transactions are not disclosed. This makes it challenging to comprehend the entire debt and dependency of companies. Consequently, it is challenging to evaluate business risk. According to Loshto (2021), a significant issue that has an impact on the reliability of financial accounts is the significance of the informal economy. Thus, the cost accounting and financial management principles seem not to be followed by the SMEs owners or management.

Banks want current, recurring financial information, but SMEs-provided data is frequently of low quality. The absence of timely and accurate interim financial reporting from SMEs is a significant barrier to bank credit. For loan applications, annual financial statements are typically insufficient, and banks typically ask businesses to provide current interim financial information, including trial balances. SMEs frequently offer interim financial data that is of poor quality and frequently isn't presented correctly, which slows down the loan application procedure.

Only medium-sized and large-sized businesses that are subject to a legislative audit mandate conduct financial statement audits. Less than 5% of smaller businesses reportedly furnish audited financial accounts, despite not being required by law to do so, according to the banks questioned. Banks feel that requiring audits for small businesses would make them less competitive (in terms of time and expense). Banks see the quality of audit services as being unequal, according to Johns (2018). Most SMEs aim to cut costs on accounting and auditing, which has a corresponding influence on quality.

Organization for Economic Co-operation and Development says that overall, banks need to exercise greater due diligence due to SMEs' poor financial management abilities and poor financial reporting quality (2020). This is an expensive and time-consuming exercise that slows down the loan application process, raises the interest rates on loans provided to SMEs, and makes banks more dependent on guarantees and collateral when setting loan prices. According to Harvie (2021), all banks have implemented internal controls of some kind to detect discrepancies between officially declared financial accounts of SMEs and the other information they supply. To address the ignorance about and informality in SMEs' business procedures, a thorough due diligence approach is required. The interest rates that SMEs pay reflect this expensive and drawn-out process. Furthermore, banks are still very likely to rely on personal guarantees and collateral to support loan pricing (Orsenigo 2018)

The financial framework required to support SMEs' access to credit must include credit reporting. Asymmetric information can be created in credit markets due to the smaller size, lax transparency rules, and uncertain life cycles of SMEs in comparison to larger companies. Nevertheless, successful credit reporting in this industry comes with certain special difficulties. One of them is being able to accurately recognize small businesses and track their repayment histories starting from the moment they are established. The importance of consistency in this area relies on several factors. For this to be viable, the regulatory framework must provide the framework for the exchange of such information, and the pertinent parties, including data suppliers, regulators, and consumer organizations, should be convinced of the advantages of participating in such projects (Chingwaru 2019). The most useful credit reports for SMEs are those that offer thorough details on the behavior of the firm's past. There is space for improvement in this area, according to the data. For instance, more than 40% of CRSPs only report negative data or only a little amount of positive data, and in 20 economies, the negative data is immediately removed when the debts are cancelled.

In addition to banks, SMEs also rely on a wide range of sources Improving Access to Finance for SMEs through Credit Reporting.

Manyani et al (2014) looked on the venture financing of SMEs in Zimbabwe, notably those operating in the town of Bindura in the Mashonaland Central Province. He discovered that the majority of SMEs in Bindura obtain funding for their companies from personal savings, friends, and family, and other sources. It was also determined that due to strict restrictions and a lack of collateral security, the financing options accessible to SMEs in Bindura are unable to fund the capital needed for their operations.

To determine whether SMEs were receiving loans from financial institutions, Gombarume and Mavhundutse (2014) conducted a study to evaluate the difficulties Small to Medium Scale Enterprises (SMEs) in Chitungwiza faced. According to their analysis, Zimbabwe's macroeconomic instability was impeding the growth of the SMEs sector. They advised the Zimbabwean government to establish a loan guarantee program and advised SMEs to legalize their operations to obtain financial support from financial institutions.

According to the United Nations Conference on Trade and Development (UNCTD) (2001) one of the major obstacles that SMEs face when they initially start or need to scale up operations is access to financing. Maintaining proper accounts and generating meaningful financial statements enhance their chances of obtaining financial resources. UNCTD (2001) also mentioned that to attract foreign investment, SME reporting also needs to meet international requirements and standards such as those set by the International Accounting Standards Board (IASB). However, in response to the rapid globalization of the world economy and increasing interconnectedness of global financial markets, international accounting standards (IASs) are becoming too complex, voluminous, and costly for many SMEs to apply in an effective manner.

According to the World Bank (2017) , banks need up-to-date, periodic financial information, but such information from SMEs tends to be of poor quality. A major obstacle to bank lending is the lack of timely and reliable interim financial information from SMEs. Annual financial statements are usually not sufficient for loan applications, and banks customarily request companies to submit up-to date, interim financial information, including trial balances. Interim financial information provided by SMEs tends to be of poor quality and is often not presented clearly, which causes delays in the loan application process.

In Zimbabwe, SMEs performance is mostly determined by access to financing (World Bank Group 2018). Fanta et al. (2017) noted that roughly 50% of small business owners in Zimbabwe start and build their entrepreneurial endeavours out of their own money and a third out of informal finance in their study on four SADC nations, namely Malawi, Mozambique, Zambia, and Zimbabwe. He stated that only a maximum of 2.3% of SMEs in Zimbabwe have access to bank credit, 11.3% rely on unofficial funding, 1.6% on other formal sources, and none do so through trade.

According to Brijlal, P. et al. (2014) most of the SMEs owners were found to lack interpretation skills and an awareness of how to use information from financial statements. An implication of this study therefore is that policy makers, business support organizations, banks and academic institutions need to focus on educating SMMEs more effectively in financial management, thereby mitigating the risk of cash flow problems and business failure.

According to Van Eeden et al. (2014), the lack of financing was the primary factor in the high failure rate of SMEs. Similar findings were made five years later by Beck and Demircuc-Kunt (2006). Access to financing for newly founded SMEs with no credit history may be highly challenging, especially if the owner has limited assets to show lenders that he or she has the ability to repay the loan. The second issue is moral hazard, which refers to the possibility that SME owners or management will use the funds for secretive purposes. This problem is exacerbated by the SMEs' notoriously lax financial controls (Stokes & Wilson 2019).

1.3.2 Accounting Information Systems practices by SMEs

SMEs, just like any other business entity go through financial accounting and reporting practices. Thus, the SMEs follow the same accounting cycle and they do so through following accounting information systems. However, for SMEs there is serious information asymmetry which is made worse by SMEs' lack of information infrastructure. Thus, the accounting and reporting practices are quite poor.

Non-financial information (such as business specifics) as well as financial information—which is essential—are frequently utilized to assess a SME's creditworthiness. The latter frequently contains data from a company's yearly accounts, data on its credit history, data on its repayment capacity, and data on its payment performance (i.e. positive payment performance – information about payments that were made, and negative payment

performance – information about payments that were missed). Small firms frequently lack the information needed for a loan provider to properly assess their cash flow condition, such as a history of audited financial records.

According to a recent analysis by the European Commission, there are significant differences across Member States in the way that credit and financial information about SMEs is disclosed (OECD, 2015). Banks benefit from this. Typically, banks are in the greatest position to evaluate the genuine creditworthiness of their SME clients since they have established a long-term connection with them, are familiar with their financial state, level of debt, and payment patterns. Their constant interactions with SME clients yield extremely useful data for determining their creditworthiness. Their comparative advantage, for instance, is increased by the information obtained from the disclosure of current and credit card accounts. The amount of information that banks can share with other market participants (such as business registrations, credit bureaus, and business information and scoring services) is constrained and varies from one Member State to the next.

To promote (alternative) investors' and lenders' access to a wider choice of funding options, it is crucial to increase the accessibility of SME credit and financial information (OECD, 2015). Regulation of disclosure could be used to increase the flow of information. SMEs are particularly sensitive to rises in the regulatory load, though. Only a small percentage of them are keen to diversify their revenue streams. Additionally, a lot of SMEs are reluctant to disclose their information due to privacy concerns and the related expenses of continual disclosure requirements. Therefore, any action in this area needs to be taken in a proportionate manner.

The simplest option for SMEs and financial institutions to lower the risk premium in loan formulations in collateral-based lending is to provide collateral. But when the Basel capital agreement was established, several governments increased policy-based financing for SMEs to lessen the restrictions on SME financing as a necessary emergency countermeasure. In such a case, SME financing required the use of effective and reasonably priced credit risk evaluation tools, particularly for transaction-based lending (OECD, 2015). Comprehensive information infrastructure is required to handle the substantial credit limitations that SMEs must overcome to comply with Basel II risk management standards.

Zimbabwe is not the only country where there is a financial deficit in the financing of SMEs. SMEs in the region seem to have difficulty getting access to funding for expansion and development. According to the World Bank (2022), the International Finance Corporation (IFC) estimates that 65 million firms, or 40% of formal micro, small and medium enterprises (MSMEs) in developing countries, have an unmet financing need of \$5.2 trillion every year, which is equivalent to 1.4 times the current level of the global MSME lending. East Asia and Pacific accounts for the largest share (46%) of the total global finance gap and is followed by Latin America and the Caribbean (23%) and Europe and Central Asia (15%) (World Bank, 2022).

Huyghehaert and Van de Gucht (2009) noted that lenders become reluctant to extend significant amounts of debt to SMEs if issues related to SME information and incentives appear to be significant. Deakins et al. (2008) further claimed that because the founder possesses a wealth of information, information at an early stage of the business is not necessarily clear. Such knowledge asymmetries deter financiers from providing startup finance to SMEs. Every finance transaction includes the idea of knowledge asymmetry. This is because businesses may not have easy access to critical information about their operations for potential lenders and outside investors.

According to Musah (2017), most SMEs do not maintain proper accounting records due to lack of accounting knowledge and absence of specific guidelines for bookkeeping and accounting recordkeeping. The SMEs management also lack education and training skills. Of the same notion were Madurapperuma et al. (2016) who revealed that majority of SMEs do not maintain proper accounting records because of lack of accounting knowledge, and the cost of hiring professional accountants and lack of specific accounting regulations. Musah (2017) also noted that there is an inefficient use of accounting information to support financial performance measurement by SMEs.

Financial information carries significant weight in the SME loan decision process in Serbia, whereas pure collateral-based lending has been phased out (World Bank Group, 2017). Thus, basing on the survey that was carried out in Serbia, five out of the six banks surveyed request unaudited financial statements as part of their credit application. Financial statement lending is ranked as the most popular lending channel for SMEs classified as retail and corporate clients, while pure asset-based lending (thus, banks look at collateral as the primary source of repayment) is used the least (World Bank Group, 2017). All the banks interviewed see

external audits as important for enhancing the reliability of the information provided by SMEs; however, too few audits are performed, and their quality is uneven (World Bank Group, 2017). Financial statement audits are only performed for medium and large-sized firms, which face a statutory audit requirement.

Small business owners are not transparent or do not open up on their businesses to outsiders. For some reasons, they do not give the true information about their assets, liabilities, profits and others to tax collectors, their employees, and outsiders (Kwaning , Nyantakyi & Kyereh, 2015) . Access to external finance depends on an open trade of information between the one receiving the fund and the giver. The refusal of small business owners to give right information about their business to outsiders make it difficult to assess creditworthiness and also difficult to lend. This means that many SMEs in developed and developing countries do not produce reliable financial information, which could be used by creditor or investors. (Ricupero, 2002). Bass and Schrooten (2005) concluded that the lack of reliable information leads to comparably high interest rates even if a long-term relationship between borrower and bank exists. In many countries, banks are reluctant to extend credit to SMEs because of the inability of the borrower to produce formal financial statements and audited accounts. Strengthening accounting and auditing is therefore a key requirement for widening access to banks by SMEs (Kwaning et al, 2015).

1.4 Research Methodology

The study was grounded upon the mixed methods methodology. This methodology enabled the identification of both numerical and non-numerical consequences of the lack of financial reporting as a barrier to finance for SMEs (Christopher 2017). The approach makes sure that all factors are covered even though both qualitative and quantitative methods are being used (Quinlan, Zikmund, Babbin, Carr and Griffin , 2015)

.The mixed methods methodology was beneficial at analyzing both qualitative and quantitative data to learn as much as possible about the SMEs (Saunders, Lewis, and Thornhill,2019). The mixed methods research approach was suitable in that it required the researcher to examine both qualitative and quantitative characteristics to fully understand the complexity of the SMEs. Thus, the motive for combining the two methods is the idea that both the quantitative and the qualitative research methodologies are complementary, and therefore, there will be an added value in combining them (Dawadi, Shrestha, & Giri, 2021).

The researchers used both data sets to answer each research question which enhanced production of greater certainty and wider implication in the conclusion. In other words, mixing the two methods helped to produce a more complete picture and provided an opportunity for a greater assortment of divergent or complementary views.

The Explanatory Sequential Research Design was used. This design occurs in two distinct interactive phases, the beginning with the collection and analysis of the quantitative data to expand the first phase quantitative results followed by the designing of the second, qualitative phase based on the quantitative findings (Creswell & Plano Clark, 2018). In this design, a researcher follows up on a specific quantitative finding and explains it with the qualitative data (Creswell & Plano Clark, 2011). The level of the SMEs' failure to prepare and maintain financial reports was successfully revealed through the explanatory sequential design. It was also used because it gave the researcher the chance to utilize data collection techniques like questionnaires and interviews to gather information that was crucial and appropriate for the research because it primarily points to the experts and knowledgeable respondents in the SMEs sector to reveal the truth about the problems that they face because of not producing and maintaining financial reports.

Forty (40) owners representing different SMEs in diverse economic areas made up the study's population. A sample had to be chosen after the study population was chosen, and according to Casteel and Bridier (2021) a sample had to accurately represent the entire study population. Purposive or judgmental sampling is a strategy in which settings persons or events are selected deliberately in order to provide important information that cannot be obtained from other choices (Maxwell, 1996). It is where the researcher includes cases or participants in the sample because they believe that they warrant inclusion. The researcher is using judgmental sampling because every respondent has more in-depth information of the SMEs sector in Zimbabwe. Because judgmental sampling was used, it was also necessary for the researcher to carefully choose from the sample of respondents those who have more in-depth understanding of the subject at hand. Given that the researchers have been in the nation for a considerable amount of time, they may also clearly identify the respondents who have sufficient expertise of the field under examination. To obtain first-hand knowledge from the respondents, primary data was gathered by the researchers, in accordance with Westin and Roberts (2010). According to Taylor (2022), primary data was collected through interviews, and questionnaires. Questionnaires were used to gather quantitative data while interviews were used for qualitative data.

1.5 Results, Discussion and Analysis

The results were gathered, and discussions were made upon them.

1.5.1 Quantitative data Analysis

Data that was gathered was tabulated and later graphs were drafted using the collected data. All data was gathered from primary sources as outlined in the methodology section.

1.5.1.1 Production and maintenance of financial reports by SMEs

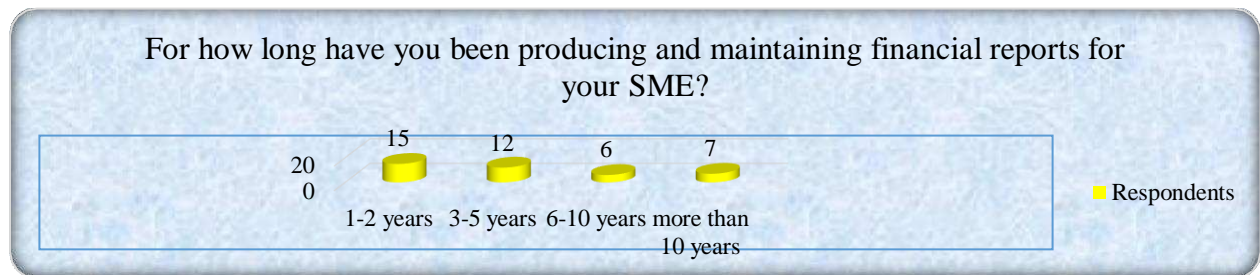


Figure 1 How long SMEs have been producing and maintaining financial reports

When the researcher queried the respondents about their backgrounds, Fig. 1 reveals that 15 of them, or 38% of the respondents, have experience creating and maintaining financial reports for their SMEs. Twelve (12) respondents have been creating and maintaining financial reports for three to five years, and 13 respondents have been doing so for six or more years, totalling a combined 33%.

1.5.1.2 Funds seeking by SMEs

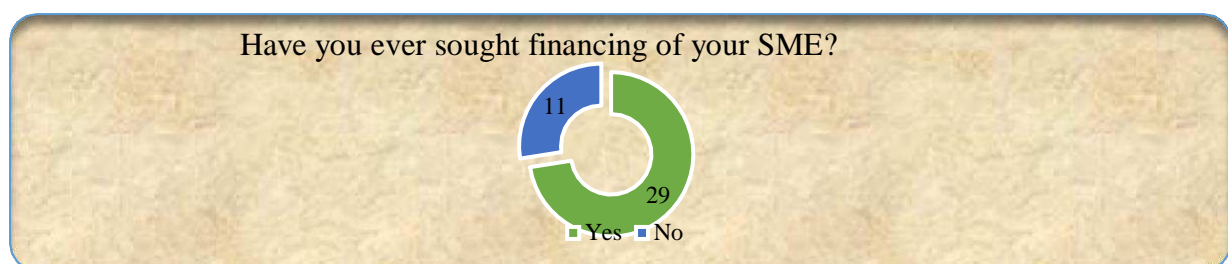


Figure 2: Extent of seeking funds by SMEs

The above analysis clearly shows that 29 respondents mentioned that they have sought funding for their SMEs before and this represents 73% of the total respondents asked. 28% of the respondents mentioned that they have not sought financial support for their SMEs before and this represents 11 respondents. There could be reasons for them not seeking any funding

which are the fact that they have for enough funding, or they do not see themselves as good enough to qualify for funding from both government and finance houses and institutions.

1.5.1.3 Lack of access to finance by SMEs because of lack of financial reports

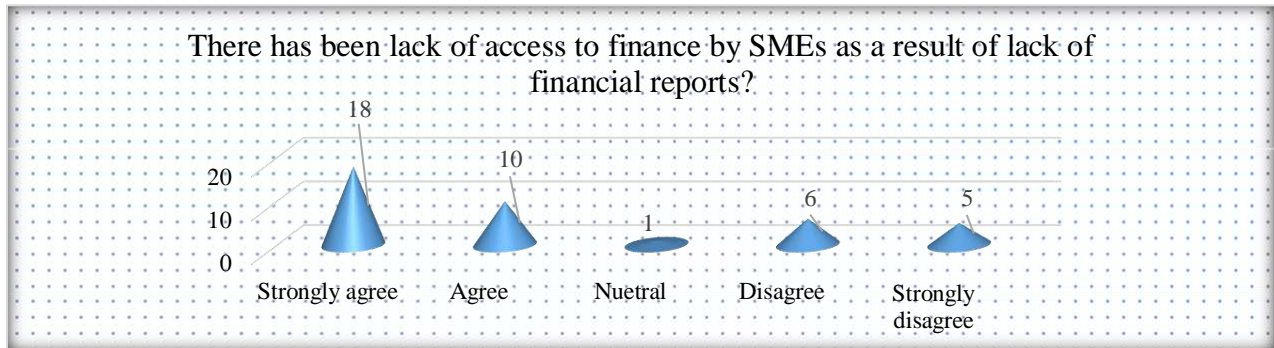


Figure 3: Responses on the fact that there has been lack of access to finance by SMEs because of lack of financial reports

According to the above, 45% of the respondents strongly agreed that there has been a lack of access to finance by SMEs because they do not possess any financial report. 10 of the 40 respondents agreed the same but however, only one was neutral to that fact. 6 respondents disagreed while 5 strongly disagreed.

1.5.1.4 Problems encountered by SMEs in accessing funding because of lack financial reporting

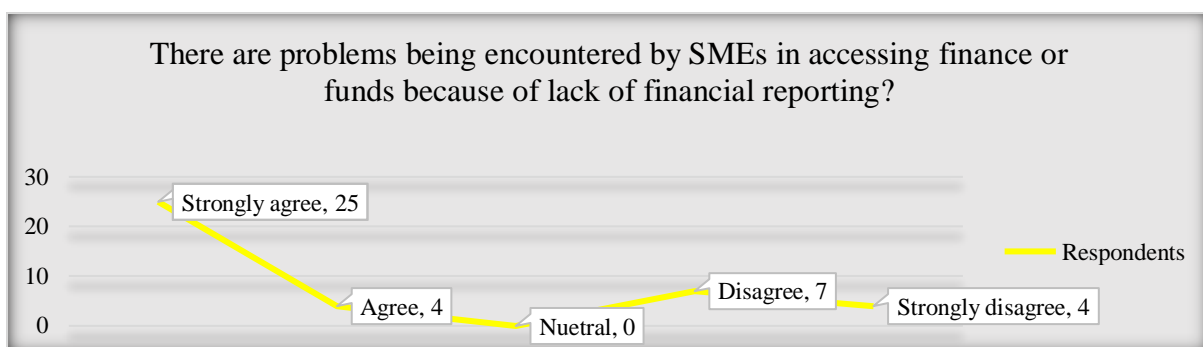


Figure 4 Responses of whether there are problems encountered by SMEs in accessing funding because of lack financial reporting

The above depicts responses given by respondents on whether there are problems being encountered by SMEs in accessing finance or funding because of lack of financial reporting. 25 respondents strongly agreed that problems are there, and this represents 63% of the 40 respondents. 10% (4 respondents) agreed to that fact as well. No respondent was neutral to that fact but 18% and 10% disagreed and strongly disagreed respectively.

1.5.1.5 Responses on whether the current failure to access funding by SMEs has been caused by factors outside lack of financial reports

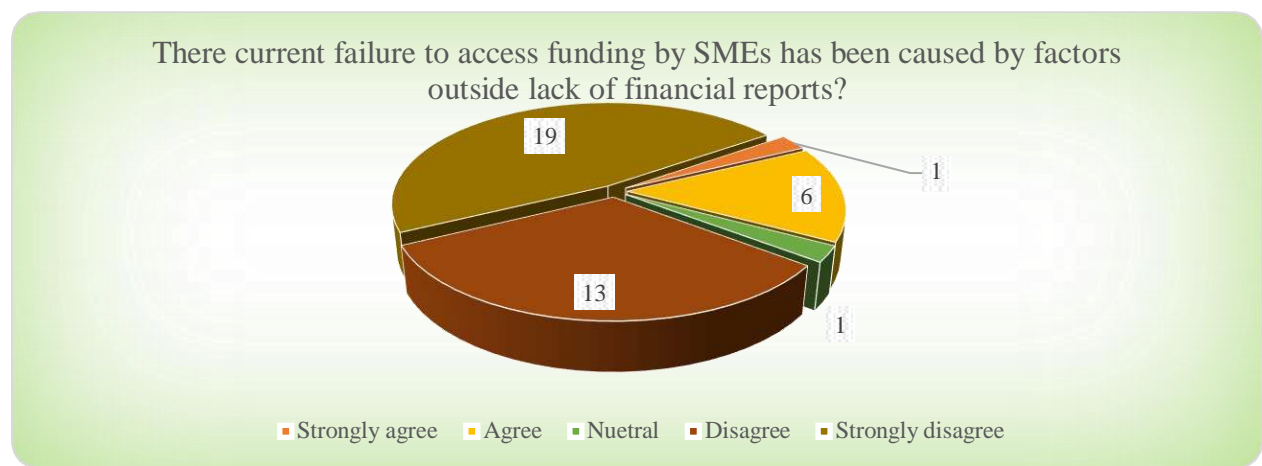


Figure 5 Responses on whether the current failure to access funding by SMEs has been caused by factors outside lack of financial reports

The above depiction shows that 3% strongly agreed that the current failure by SMEs to access funding has been caused by factors outside lack of financial reports. A huge chunk strongly disagreed to that and these points out to the fact that most of the respondents believe that for SMEs to thrive, they need more funding and that can only be sourced when financial reports are prepared and presented to finance institutions and those stakeholders who have the capacity to avail funds to SMEs. 33% of the respondents disagreed to that while only 3% was not sure (neutral) to that fact. 15% agreed that failure by SMEs to produce and maintain financial reports has hindered them from accessing funding.

1.5.2 Analysis of interview data

The researcher carried out interviews to create a chance for the clarification on unclear issues from the respondents and was able to collect as much required data as possible to validate the

results of the research. The main aim of carrying out interviews was to get the views of the effects of failure by SMEs to access funding because of lack of financial reports. The following are the results of the interviews

1.5.2.1 Is failure by SMEs to produce and maintain financial reports hindering SMEs from accessing funding?

The first respondent had uncertainty on whether to put blame on the failure of SMEs to produce financial reports. Respondent 2 argued that although regulations had a fair share of problems in the SMEs sector, the country is facing uncertainty by looking with an analytical eye at the economy at large. Thus, the SMEs felt they were being disadvantaged by the strictness of the lenders upon requiring them to present their financial statements prior to accessing the funds. This is in synch with the assertion by the World Bank (2017) that SMEs rarely provide specific information about their inventories, inventory, receivables, and payables. All this information hinders the progress of SMEs on acquiring loans since banks require such information in a standard and systematic manner.

Respondent 3 mostly emphasized on the need for government and other funding institutions to quickly take a forward step to combat the effects of lack of financial reports as a requirement for sourcing funding. This is in synch with OECD (2022) who said bank financing will continue to be crucial for the SME sector though there is a broad concern that credit constraints will simply become “the new normal” for SMEs and entrepreneurs. Respondent 4 said that there is much greater awareness in the country about the challenges SME sectors of the economy are encountering and a smaller percentage of the negative effects must be coupled with necessary operational adjustments. However, Respondent 5 stated that all was not well with SMEs with regards to sourcing funding, though the whole sector is being regarded as expanding by the analysts and one of the respondents argues that it seems as if SME sector is thriving, but it is like a sugar-coated pill which is sweet outside but bitter inside. After analysing that 80% of the interviewees were concurring, the researcher concluded that SMEs have been neglected as far as funding is concerned.

1.5.2.2 Is there any relationship between production and maintenance of financial reports and the SMEs’ ability to access funding?

Respondent 1 reiterated that some of the owners of the SMEs cause a challenge to themselves by being reluctant to release information to the financiers. He even mentioned that at times the information that is passed to the financiers won’t be accurate enough to warrant the banks

to offer the SME firms loans. This concurs with Hwingwiri who was of the notion that financial institutions are not satisfied with the financial information they are getting from SMEs. Hwingwiri (2013) further alluded that in as much as SMEs claim to be furnishing financiers with all the required information, the financial institutions find the information highly insufficient.

Respondent 2 agreed that failure of SMEs to provide financial reports is a serious constraint upon loan acquisition by SMEs in Zimbabwe. They might be blamed for failure to acquire loans. They however lamented that there are other factors that impede SMEs from acquiring the loans from the banks. Respondent 3 stated that a relationship ought to exist in the sense that the financiers must check first the ability of the SME to pay back the money they would have borrowed. Hence this member was in support of the need for SMEs to submit their financial statements to the banks prior to accessing the loan facility. Preparation and maintenance of financial reports was thus considered as a necessity to assess the credit worthiness of the SMEs. Respondent 4 stated that with a bird's eye view believed a relationship exists between provision of finance reports to the financier and the SMEs access to funding. Respondent 5 argued that there is a very strong relationship citing that most SMEs that have accessed credit from financiers would have gone through a process of preparing and maintaining financial reports. The researcher concluded that there is a relationship between preparation and maintenance of financial reports and the SMEs access to credit. Thus, the SMEs ought to ensure they prepare financial statements. However, there is need to be guided by the IFRS for SMEs.

1.5.2.3 Failure of SMEs to produce and maintain financial reports. How much is it impeding SMEs on acquiring funds from financiers?

The researcher asked the respondents if there were clearly visible problems caused by the failure by SMEs to produce financial statements or reports. Respondent 1 cited mainly financial problems which result in failure by SMEs to recruit finance personnel that are competent enough to prepare and maintain finance reports. He had this to say:

‘ Our SMEs do not have adequate financial resources to meet the costs of hiring the qualified and experienced Accountants who can produce the required financial statements at each year end. More so we cannot afford to attract these professionals who always target large firms.’

Respondent 2 concurred when he alluded that most if not all SMEs have failed to access credit from financiers because of lack of the necessary financial reports and reluctance to release information to external users such as the banks and Microfinance Institutions. The respondent also mentioned that some firms are even reluctant to share financial information with the government agencies such as ZIMSTAT (Zimbabwe National Statistical Agency) and ZIMRA (Zimbabwe Revenue Authority) not knowing that such information will benefit them only if such agents have it. Respondent 3 went on to reiterate that SMEs' inability to prepare and maintain finance reports have posed visible financial problems since most financiers are not willing to extend credit to SMEs that are not compliant. The member went on to explain the fact that some financiers require the SMEs to have audited financial statements prior to awarding them access to the loans. This agrees with the World Bank Group (2017) who noted that most firms would prefer audited financial statements for them to grant the SMEs credit. Thus, creditworthiness for such SMEs bases upon provision of audited financial statements which they allude to be more reliable than what can be of creative accounting nature (if not audited).

Respondent 4 stated that SMEs business has not been halted by lack of credit but by the existing economic crisis. Respondent 5 stated that the blame should be put on government to effectively manage the SME sector by putting laws flexible enough for financier to support SMEs financially without hesitation.

1.6 Conclusions and Recommendations

The researcher concluded that the failure to produce financial statements is a serious constraint hindering the SMEs to be credit worth in the eyes of banks and other financiers such as Microfinance Institutions. This is in line with what several authors said including Musah (2017) who noted that SMEs fail to provide Banks with accounting information to substantiate their financial performance. This surely repels the financiers who would want to release funds to reliable people who have great potential to repay the loans. . As a recommendation, SMEs are encouraged to try to engage qualified Accountants who can interpret the IFRs for SMEs. There is also need to ensure that the IFRs for SMEs be as simple as possible such that the SMEs manage to make use of this crucial framework.

SMEs ought to upgrade their Accounting Information Systems practices. They should also ensure transparency prevails upon the way they govern their business entities. More so the information they record in their books of accounts must be able to convince financial

institutions to award them loans. This concurs with Hwingwiri (2013) who reiterated that the information SMEs provide should be able to convince financial institutions on the creditworthiness of the . The current position with financiers is that SMEs are failing to provide them the information they require. Stiglitz and Weiss (2009) argued that SMEs financing is constrained by the existence of such information asymmetries. Therefore, there is need to upgrade the information systems and close the information gap that exists between the SMEs and the Financiers.

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