International Journal for Multidisciplinary Research (IJFMR)
E-ISSN: 2582-2160 ● Website: www.ijfmr.com ● Email: editor@ijfmr.com

Exploring Financial Management and Performance of Small and Medium Enterprises

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Abstract
This study examines the financial management practices and performance of small and medium enterprises (SMEs) in Cauayan City, aiming to identify how financial strategies control business sustainability and growth. SMEs are extensively acknowledged as vital contributors to local economic development, employment generation, and innovation. However, many face persistent challenges related to financial planning, capital access, and cash flow management, which can significantly impact their performance and survival. Using a mixed-method approach, this research combines quantitative data from structured surveys with qualitative insights from in-depth interviews with SME owners and financial officers. Key areas of analysis include budgeting, financial reporting, investment decisions, debt management, and the use of digital tools for financial monitoring. The study also evaluates performance indicators such as profitability, liquidity, and operational efficiency. Findings reveal that while many SMEs in Cauayan City exhibit strong entrepreneurial drive, a lack of financial literacy and strategic planning often hinders optimal performance. Access to financing remains limited, with many enterprises relying on informal funding sources. The research underscores the need for targeted financial education programs and policy interventions to support SME development. It also highlights the potential of technology adoption in enhancing financial transparency and decision-making. Ultimately, this study provides valuable insights for local government units, financial institutions, and development agencies seeking to empower SMEs in Cauayan City through improved financial management practices, fostering sustainable economic growth in the region.

Keywords: Financial Management; SME Performance; Small and Medium Enterprises; Cauayan City

1. Introduction

Small, and Medium Enterprises (SMEs) play a dominant role in the business landscape of the Philippines, significantly contributing to the country's economic development. They promote job creation, entrepreneurial activity, creativity, and innovation. The effective practices in working capital management, financial reporting, accounting information systems, investment planning, and overall financial management have a significant positive relationship with financial performance and business development [18]. Globally, MSMEs contribute approximately 45% to economies, highlighting their potential to generate employment and drive economic activity.

Financial management is essential for the success of SMEs, as it directly influences their financial performance and overall sustainability. Effective financial management allows businesses to manage cash flows, inventory, and payables and receivables efficiently while ensuring timely and accurate financial reporting [8]. The quality of financial performance often reflects how well financial management practices are implemented.

SMEs are defined as business entities engaged in industry, agribusiness, or services, classified based on their asset size and number of employees, regardless of business ownership type. In addition to creating jobs, micro and small businesses give entrepreneurs creative spaces to create new goods and services and lift people out of poverty[10]. In the Philippines, MSMEs make up 99.51% of all businesses. Among these, 88.77% are micro-enterprises, 10.25% are small enterprises, and only 0.49% are medium enterprises. These businesses generate 62.66% of total employment, with the remaining 37.34% provided by large enterprises [5].

Financial management practices involve procedures related to accounting, budgeting, reporting, and other financial activities [17]. These practices allow business owners to evaluate their financial status and make informed decisions.

Financial performance is a broad measure of how well a business utilizes its assets to generate income and is often used to assess its financial health [9]. While financial reports can help forecast future growth, they may not always reflect the business's overall earnings strength.

Despite the growth of SMEs in the country, not all businesses thrive. Some struggle due to poor financial performance linked to inadequate accounting practices and underutilized financial reports [1].

Cauayan City hosts a considerable number of SMEs, but few studies have assessed how their financial practices affect their business outcomes. This study aims to explore the relationship between financial management practices and financial performance among SMEs in the city. It also seeks to understand whether strong financial practices contribute to greater business profitability and growth.

Specifically, this study addresses the following questions:

1. What are the financial management practices of the respondents in terms of recording, budgeting, reporting, and inventory management?
2. What is the level of financial performance of the respondents in terms of the Balance sheet, income statement, and cash flow statement?
3. What is the relationship between the financial management practices and the financial performance of the respondents?

Financial management lies at the heart of business success [11]. Poor practices in this area often lead to the downfall of enterprises across many regions [14]. A study in Anambra State found that many SMEs lacked consistent strategies for financial allocation and often failed to monitor their accounting records. Notably, the length of experience of business owners did not significantly affect their use of financial practices [13]. To address these gaps, it was suggested that entrepreneurial organizations offer updated financial management training and resources.

2. Research Methodology

The study adopted a descriptive-correlational research design to explore the relationship between financial management practices, specifically in recording, budgeting, reporting, and inventory management, and the financial performance of SMEs in Cauayan City, Isabela. The variables were observed without manipulation.

The respondents were selected from 250 SMEs in Cauayan City. Using Raosoft Software, a sample size of 152 was determined. Ultimately, 150 business owners participated in the survey.

A research-made questionnaire was used to collect data. The tool consisted of two parts: the first gathered demographic profiles, and the second assessed financial management practices and financial performance. The questionnaires were directly distributed to SME owners.

The study measured the following variables:

1. Independent Variables (Financial management practices):

Recording: gathering information on earnings, outlays, sales, purchases, and other financial transactions to guarantee precise financial monitoring and reporting

Budgeting: set business objectives, estimate future financial requirements, manage expenses, and distribute resources effectively.

Reporting: creating and presenting financial summaries and statements, including cash flow reports, balance sheets, and income statements.

Inventory Management:guarantees that the appropriate quantity of inventory is available when needed, lowers carrying costs, avoids stockouts or overstocking, and enhances operational efficiency and profitability.

2. Dependent Variables (Financial Performance):

Balance Sheet: evaluates the company's assets, liabilities, and equity to determine its financial standing at a given moment in time.

Income Statement: provides information on revenues, expenses, and net income or loss to calculate profitability during a certain time period.

Cash Flow Statement: assesses the company's cash flow and divides it into three categories: financing, investment, and operating.

Ethical protocols were followed, including securing university approval and obtaining informed consent from participants. The researchers also maintained professionalism and objectivity throughout the study.

For data analysis, both descriptive and inferential statistics were applied. Tools used included frequency, percentage, mean, weighted mean, and Pearson-r correlation coefficient. Specific point scales were employed to interpret financial management practices and performance levels, ranging from “Always Practiced” to “Never Practiced,” and from “Very Effective” to “Not Effective.” Correlation results were also categorized based on strength, from negligible to very high.

3. Results and Discussions

Table 1. Financial Management Practices of SMEs in terms of Recording Activities

INDICATORS	MEAN	SD	INTERPRETATION
1. I record my daily cash transaction.	4.41	1.11	Most Often Practiced
2. I record my daily revenue transaction.	4.4	1.06	Most Often Practiced
3. I record all my daily expenses incurred.	4.25	1.19	Most Often Practiced
4. I record all the charges, fees, and payables in the book.	4.16	1.24	Most Often Practiced
5. I record all my inventory in the book.	4.21	1.31	Most Often Practiced
Weighted Mean	**4.28**	**1.08**	**Most Often Practiced**

Table 1 shows a weighted mean of 4.28 which indicates that the MSMEs in Cauayan City, Isabela practiced recording financial transactions most of the time. Recording the daily revenue transaction is most often practiced. As such, failure to track revenue does not give businesses an idea of how much money they are bringing in to cover expenses and other payables. Performing and keeping of records are an integral part of SMEs because it ensures that records and documents are properly maintained and retained [12].

Table 2. Financial Management Practices of SMEs in terms of Budgeting Activities

INDICATORS	MEAN	SD	INTERPRETATION
1. I spend less than my revenue.	4.35	0.89	Most Often Practiced
2. I make a budget schedule for paying business expenses.	4.35	0.84	Most Often Practiced
3. I make a budget schedule for adding inventories.	4.32	0.85	Most Often Practiced
4. I make a budgetary allocation on all the expenses incurred in the business operation.	4.33	0.9	Most Often Practiced
5. I forecast future operating expenses of the business.	4.09	0.94	Most Often Practiced
Weighted Mean	**4.29**	**0.64**	**Most Often Practiced**

Table 2 shows a highest weighted mean of 4.35 was observed in spending less than revenue and making a budget schedule for paying business expenses. This shows that the MSMEs are profit-oriented, and the proper means of budgeting for business expenses was practiced most of the time so that late payments and due charges would be avoided. On the other, the lowest mean of 4.09 was in the forecasting of future operating expenses of the business and was most often practiced. Thus, financial management is crucial to the survival and well-being of small enterprises of all types [6].

Table 3. Financial Management Practices of SMEs in terms of Reporting Activities

INDICATORS	MEAN	SD	INTERPRETATION
1. I prepare different financial reports like income statements, etc.	3.16	1.58	Sometimes Practiced
2. I hire external accountants/bookkeepers to check the reports to be submitted from the government.	2.11	1.54	Rarely Practiced
3. I submit my financial reports to the government on time.	3.37	1.46	Sometimes Practiced
4. I file my income tax annually.	3.22	1.67	Sometimes Practiced
5. I report all my revenues to the government.	3.17	1.58	Sometimes Practiced
Weighted Mean	**3.01**	**1.32**	**Sometimes Practiced**

Table 3 shows that the respondents sometimes prepare different financial reports like income statements, etc., as shown by the mean of 3.16. Based on the mean of 3.37, they sometimes submit their financial reports to the government on time. With the mean of 3.17, the respondents sometimes report all their revenues to the government. Moreover, they sometimes file their income tax annually by the mean of 3.22. While the lowest mean of 2. 11 was hiring external accountants/bookkeepers to check the reports to be submitted from the government, which is rarely practiced. Only large businesses are able to afford to hire a bookkeeper and accountant on a regular basis so that they can maintain accurate accounting records and prepare BIR documentation. Thus, the weighted mean of 3.01 indicates that the financial management practices of MSMEs in terms of reporting activities are sometimes practiced only. Financial reports tell a story about a company's overall financial health and also provide insight and transparency to a firm's financial position and operation, however, inaccurate financial reports can hinder a company's value and reputation [15].

Table 4. Financial Management Practices of SMEs in terms of Inventory Management

INDICATORS	MEAN	SD	INTERPRETATION
1. I record new and daily inventories in the book.	4.13	1.28	Most Often Practiced
2. I conduct physical counting of inventory regularly.	4.11	1.18	Most Often Practiced
3. I follow the first in, first out (FIFO) rule in inventory.	4.05	1.32	Most Often Practiced
4. I forecast the required level of inventory at a specified time.	3.84	1.09	Most Often Practiced
5. I apply technology in managing the inventory with the use Point of Sale system, etc.	2.51	1.77	Rarely Practiced
Weighted Mean	**3.73**	**1.00**	**Sometimes Practiced**

Table 4 shows that the respondents practiced the recording of new and daily inventories in the book often based on the mean of 4.13. The respondents often practiced (most often practiced) the conduct of physical counting of inventory regularly, with the mean of 4.11. The respondents often practiced the first in, first out (FIFO) rule in inventory, as shown by the mean of 4.05. The forecasting of the required level of inventory at a specified time, as shown by the mean of 3.84, is most often practiced. And lastly, the usage of technology in managing the inventory with the use Point of Sale system, etc., was rarely practiced, with the mean of 2.51. There were only a few business entities that could afford to buy computer units and software for the automation of the recording of all business transactions because the hardware and software requirements for any automated inventory systems are quite expensive. More SMEs generated income were classified into the lesser income category. These businesses would, therefore, only manually compute their revenues, expenses, and other business transactions. With the findings, the weighted mean of 3.73 indicates that SMEs mostly practiced inventory management. One measurement of a firm's success can be determined on how inventory management is used in an effective way [16]. Regardless of the size of the company, having a proper inventory management system is essential for any SMEs. It can help you keep track of all your inventories and determine the exact prices. It can also help you manage and monitor changes in demand without sacrificing customer experience and product quality.

Table 5. SMEs Level of Financial Performance Based on their Financial Management Practices

MEASURES	MEAN	SD	INTERPRETATION
Balance Sheet	3.04	1	Moderately Effective
Income Statement	3.25	0.91	Moderately Effective
Cash Flow Statement	3.11	0.96	Moderately Effective
Weighted Mean	3.13	0.92	Moderately Effective

Table 5 shows that based on the answers of the respondents, the financial management practices are moderately effective for the Balance sheet, Income statement, and Cash flow statement, as shown by the weighted mean of 3.13. Therefore, there were instances when SME owners were not using some financial management practices- they were simply using a manual record. Since a company's financial condition are a major concern of its owners, financial statements should be well-performed. Balance sheet, income statement, and cash flow statement measures impact of a firm's effort toward growth and expansion, budget determination, cost-cutting, and decision-making [4].

Table 6. Relationship between financial management practices and financial performance of SMEs (α=0.05)

	R	p-value	Remarks	Decision
1. Recording				
Balance Sheet	0.448	0.00001*	Low Positive Correlation	Ho Rejected
Income Statement	0.551	0.00001*	Moderate Positive Correlation	Ho Rejected
Cash Flow Statement	0.473	0.00001*	Low Positive Correlation	Ho Rejected
2. Budgeting				
Balance Sheet	0.243	0.0027*	Low Positive Correlation	Ho Rejected
Income Statement	0.263	0.0011*	Low Positive Correlation	Ho Rejected
Cash Flow Statement	0.226	0.0054*	Low Positive Correlation	Ho Rejected
3. Reporting				
Balance Sheet	0.647	0.00001*	Moderate Positive Correlation	Ho Rejected
Income Statement	0.594	0.00001*	Moderate Positive Correlation	Ho Rejected
Cash Flow Statement	0.607	0.00001*	Moderate Positive Correlation	Ho Rejected
4. Inventory Management				
Balance Sheet	0.635	0.00001*	Moderate Positive Correlation	Ho Rejected
Income Statement	0.645	0.00001*	Moderate Positive Correlation	Ho Rejected
Cash Flow Statement	0.656	0.00001*	Moderate Positive Correlation	Ho Rejected

Table 6 shows that there is a significant relationship between the financial management practices in terms of SMEs' recording activities, balance sheets, income statements, and cash flow statements. This result implies that recording the transaction has something to do with the three fundamental financial statements. This finding is similar to the findings of [3], states that recording of revenue, costs, profits, and losses incurred by a business over a specific of time are the main focuses of the income statement. The SMEs' budgeting is also significantly correlated with the three financial statements. It indicates that after a business understands its expenses and earnings, it will be able to plan its finances effectively. Budgeting is a crucial technique for businesses to use when developing financial plans to forecast and prepare for earnings and losses over a specific period[7]. Based on past performance, an income statement is helpful for businesses, but a budgeted income statement may help businesses forecast and plan for future earnings. Moreover, another significant relationship exists in the financial management practice in the aspect of reporting activities and balance sheets, income statements, and cash flow statements, where income is used for the report to be submitted to the government. That is why keeping monetary affairs in order is crucial. Frequent financial reports need reliability to grasp the financial status better [2].

Lastly, inventory management is significantly related to the three different financial statements. This means that the bigger the income earned by the business, it has a significant variation in the manner of managing the physical stocks of the company.

4. Conclusions

The study concluded that SMEs in Cauayan City most often practice recording and budgeting, which are crucial for tracking financial transactions and allocating business expenses.

Reporting and inventory management are practiced only sometimes, primarily due to the small scale of operations and limited resources of SMEs.

SMEs are seen as positively contributing to economic growth, job creation, and sustainable development through their financial management practices.

Effective financial management practices lead to improved financial performance, allowing SMEs to have a greater impact on local economies and contribute to reducing unemployment.

5. Recommendations

Based on the findings of this study on the Financial Management and Performance of Small and Medium Enterprises in the Cauayan City, the following recommendations are proposed to enhance the management practices and performance of the SMEs:

1. The Local Government Unit (LGU) of Cauayan City, in partnership with the Department of Trade and Industry, should implement policies that support the long-term survival and growth of SMEs.
2. SMEs should adopt better accounting and reporting practices, regardless of their business structure, to improve financial tracking and accountability.
3. The LGU should offer lifelong learning opportunities, such as programs and seminars, to improve the financial literacy of SMEs.
4. Government support for SMEs should focus on creating more employment opportunities and strengthening the overall economy.
5. Future researchers are encouraged to study the SME sector further to deepen understanding and promote greater support for this important sector.
6. SME owners should continuously develop their financial management practices to ensure their businesses are well-managed and sustainable.

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