

## Financial Literacy and Survival of Small and Medium Scale Enterprises

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### Abstract

*The study examined the impact of financial accounting literacy on the growth, development and survival of SMEs. The study used primary source of data obtained using a well-structured questionnaire. The sample size of the study was 90 respondents, comprising SMEs of different sectors. The Chi-square estimation tool was employed to analyse data collected. The study found that financial literacy has led to an increase on profit margins of SMEs; that financial literacy has led to an increase on sale growth of SMEs and that financial literacy has led to an increase on market share of SMEs. It was concluded that financial knowledge and attitudes influences SMEs performance. It was recommended among others that there is a need for training programs on budgeting and planning, debt management, record keeping; saving and retirement plans in schools and other institutions that seek to promote financial literacy and practice.*

*Key words: financial literacy, financial regulator, enterprise performance, and market share*

### 1. Introduction

Financial accounting literacy is a fascinating topic in both developed and emerging economies, and it has sparked a lot of interest in recent years as the financial environment has changed rapidly. Financial accounting awareness aids in the empowerment and education of investors so that they are educated about finance in a way that is important to their company and can put that knowledge to use. It is widely expected that greater financial knowledge would help overcome recent difficulties in advanced credit markets. (Bernheim & Garrett, 1996). Financial literacy prepares investors for difficult economic times by implementing risk-mitigation measures such as investing, diversifying assets, and buying insurance.

Financial accounting literacy aids decision-making processes such as timely bill payment, proper debt management, and improved credit worthiness of future borrowers to sustain livelihoods, economic growth, sound financial system and poverty reduction. It also gives you more leverage over your financial future, allows you to use financial products and services more effectively, and makes you less vulnerable to overzealous merchants or fraudulent schemes. Financial regulators are under pressure from an informed public to increase the efficiency and quality of financial services. This is because, by comparing options, asking the right questions, and negotiating more efficiently, financially literate investors put competitive pressure on financial institutions to provide more reasonably priced and transparent services. Investors should analyze and compare

financial products such as bank accounts, savings accounts, credit and loan options, payment instruments, assets, and insurance coverage in order to make the best decisions possible. (Miller, Godfrey, Levesque & Stark 2013).

Financial obstacles for Small and Medium Businesses may be exacerbated by a lack of business and management skills (SMEs). Low levels of financial literacy will make it difficult for SMEs to properly evaluate and appreciate various funding options, as well as navigate complex loan application procedures. Similarly, the lack of transparency in SMEs' accounting and financial statements makes them aggressive borrowers and therefore less appealing to lenders. SME capacity building in terms of financial statement and business plan preparation, as well as financial literacy and management training, has been shown to have a positive effect on SMEs growth. Furthermore, improving horizontal and vertical links with other SMEs and larger firms will increase SMEs' market access. (Hogarth, 2016).

However, there are several different perspectives on financial accounting literacy, which are influenced by a variety of factors. A major source of concern is SMEs' lack of understanding of the value of bookkeeping and the entity definition, causing their businesses to suffer as a result of a lack of knowledge (financial in nature) to help in forecasting against future events and expansion. There has been a long-standing issue on failure of enterprises in developing economies in the globe resulting to lack of third generation businesses in Nation like Nigeria, one of the main reasons could be lack of finance knowledge on the part of the owners and inability to design a succession plan for the future. The scarcity of accounting expertise has necessitated the conduct of this research to determine the effect of financial accounting literacy on the growth and survival of SMEs in Nigeria. In order to achieve the objective of this study, the study is organized as follows: section 2 is on literature review, section 3 is on methodology, section 4 is presentation and discussion of results while section 5 presents the conclusion and recommendations.

## **2. Literature Review**

### **2.1 Financial literacy**

Financial literacy is the education and understanding of various financial areas. This concept focuses on the ability to manage personal finance matters in an efficient manner, and it includes the knowledge of making appropriate decisions about personal finance such as invest insurance, real estate, paying for college, budgeting, retirement and tax planning (Fatoki, 2014). Financial literacy also involves the proficiency of financial principles and concepts such as financial planning, compound interest, managing debt, profitable savings techniques and the time value of money. According to Atkinson and Messy (2005), viewed financial literacy as the capacity and confidence of consumers/investors to understand financial products and concepts, as well as their ability and confidence to recognize financial risks and opportunities, make educated decisions, know where to seek support, and take other successful steps to enhance their financial well-being.

Financial illiteracy or lack of financial literacy can lead to poor financial decisions, which can have negative implications for an individual's and company's financial well-being. The Federal Government created the Financial Literacy and Education Commission, which provides resources for people who want to learn more about financial literacy (Ageyi, 2014). However, financially literate SME owner/manager is defined as someone that knows what are the most suitable financing decisions on the business performance at the various growth stages of the business; knows where to obtain the most suitable products and services; and interacts with confidence with the suppliers of these products and services (USAID, 2009).

### **2.1.1 Small and Medium Scale Enterprises Performance**

The idea of performance, as well as the concept of performance in relation to SMEs, will be discussed. Firm success or losses are two strategic results that are sometimes referred to in the literature as efficiency (Eniola & Entebang, 2015). In the management field, firm performance can be interpreted as measures of good or indifferent management (Jennings & Beaver, 1997; Sefiani & Bown, 2013), but it may occur to other reasons such as luck. The effects of a firm's performance depend on whether the firm has attained its goals or not (Davidsson, 2004).

The general performance of the organization depends on the correct management at the three levels of management (Eniola & Entebang, 2015). Performance can be characterized as the firm's ability to create acceptable outcomes and actions. However, performance seems to be conceptualized, rationalized and measured in different ways, thus making cross-comparison difficult.

There is no consensus on the definition or nature of SMEs worldwide. Different countries, institutions and individuals have put forwards various descriptions of a small business based on some parameters. Obitayo (1991) argued that the main criteria used throughout the world to describe small-scale enterprise include: number of employees, sales volume, financial strength, relative size, initial capital outlay, and independent ownership. The Federal Ministry of Industry defined medium enterprise as the one having asset value of not more than N200million with not more than 300 workers, while it defines small-scale enterprise as the one having asset value of not more than N50million, with not more than 100 workers. (Obitayo, 1991)

Small and medium scale enterprises performance involve growth as a result of expanding the sales operations or assets and usually a major strategic objective of a business. SMEs performance is common to associate improvements in firm performance with increased profitability, higher efficiency and increased output (Teruel, 2008). Extant research addressing SMEs performance has relied on accounting-based financial indicators (Vuong, 2008; Van, 2010), market-based indicators as well as combinations of both (Waweru & Kalani, 2009).

## **2.2 Empirical Review**

Lusardi, Mitchell and Curto, (2010) examined the impact of financial literacy and high cost of the borrowers. The result indicated that there is a relationship between financial literacy and low-cost borrowers. Most high-cost borrowers display very low levels of financial literacy, lack knowledge of basic financial concepts, which affect their performance level in a business.

Tamimi and Kalli (2009) examined the impact of financial literacy on financial knowledge. Their results showed that the field of individual activities affects the financial literacy level and people that invest in financial awareness have a higher level of financial literacy. The review also showed that male gender possesses higher financial literacy and income, age and education level are followed by a higher level of financial literacy.

Chepkemai (2017) investigated the impact of financial literacy training on the profitability of SMEs in Kenya's coastal region using Kwale County as a study. The study used a sample of 74 SMEs drawn from the 3 sub-counties of Kwale which included Kinang, Matuga and Msambweni. The research design used was descriptive survey methods which involve the use of questionnaire and interviews. The population of the study included SMEs who benefited from the training offered by World Bank through the Kenya Coastal Development Project in Kwale country. Simple random sampling method was used to determine the sample size. The finding of the study established that financial literacy training positively influenced the performance of SMEs and profitability. The study concluded that financial literacy affected profitability of SMEs and it recommended that financial institutions should provide training to the SMEs to build their capacity on the available financial products and how to access them. The study used

both questionnaire and interview as data collection instrument however this present study used questionnaire only to collect data from the respondents.

Njoroge (2013) assessed the relationship between financial literacy and entrepreneurial success in Nairobi County Kenya. The objective of the study was to find out whether there is a relationship between entrepreneurial success and SMEs success by interviewing a sample of seventy-nine entrepreneurs who are registered and operates in Nairobi County. The samples were randomly picked from a population of 27,485 SMEs where questions in both financial literacy and SMEs success were asked. The study concluded that there was a positive relationship between financial literacy and entrepreneurial success in Nairobi County. The study recommended that business owners and entrepreneurs need to be literate in order to succeed in their businesses.

Cherugong (2013) examined the effect of financial literacy on performance of small and medium enterprises Kenya. The researcher used a descriptive research design. A sample of 85 SMEs was selected using stratified random sampling technique. Data collected were analyzed with the aid of Statistical Package for Social Sciences (SPSS 20). The results of the study indicate that more performing SMEs employ more than three permanent employees, have been in business for more than five years, has an annual revenue growth of more than 10% and are basically financial literate and that there was a positive strong effect of financial literacy on SMEs performance.

Tuyisenge, *et.al.* (2015) investigated the role of financial literacy on loan repayment among small and medium entrepreneurs in Rwanda using Urwego Opportunity Bank as study. The research focused on 109 small and medium entrepreneurs in Urwego Opportunity Bank. A descriptive survey design was adopted in the study and questionnaire was used as the instrument of data collection. Regression analysis was used for test of hypotheses and findings of the study revealed that the quality of financial information available for financing institutions is rather poor.

Experience and knowledge are extremely important, as it provides time to recognize opportunities, develop contacts and learn how to access and to interact with funders, including bank managers and venture capitalists. Thus, entrepreneurial human capital is substantial and consequential to entrepreneurial growth. Although some studies report that only a small number of SME managers employ the resulting knowledge in a proactive way to build competitive advantage (Matlay, 2000). From the findings of prior empirics, the first, second and third hypotheses are:

*H<sub>01</sub>: Financial literacy has no significant positive impact on sales growth of SMEs*

*H<sub>02</sub>: Financial literacy has no significant positive impact on profit margin of SMEs*

*H<sub>03</sub>: There is no significant relationship between the financial literacy and market share of SMEs*

## **2.3 Theoretical Framework**

### **2.3.1 Dual –Process Theory**

The dual-process theory was propounded by Lusardi and Mitchell (2011). According to this theory, financial decisions are influenced by both intuitive and cognitive processes, implying that financial literacy cannot always result in the best financial decisions. The Dual Methodology According to financial literacy theory, people with a high degree of financial literacy's conduct is influenced by the prevalence of two thought styles: intuition (system 1) and intellect (system 2). (Lusardi & Mitchell, 2011; Glaser & Walther, 2013). Intuition is the ability to acquire knowledge without inference or the use of reason. Intuition provides views, understandings, judgments, or beliefs that cannot be empirically verified or rationally justified.

According to Taylor (1981), as cited by Chan and Park (2013), people who rely on intuition

prefer to take mental shortcuts when making decisions that are heavily affected by their emotions. A high prevalence of intuition, according to Glaser and Walther (2013), reduces the beneficial impact of financial literacy on sound investment decisions. As a consequence, increased reliance on intuition leads to less-than-optimal investment decisions.

Cognition, on the other hand, is the method of transforming, reducing, elaborating, storing, recovering, and using sensory information. Cognition is the internal mechanism of understanding, measuring, and thinking, problem solving, and making decisions (Chan & Park 2013, for example).

Individuals with a high level of cognition enjoy thinking, are analytical, are better at remembering knowledge, and are more likely to seek out new information. The dual process theory is considered relevant to this study because it shows that individuals who are high on cognition will seek out for information and are more likely to be influenced by a relevant message. This means that their decision-making skills can be boosted by financial literacy training using simple easy to understand methodologies. Moreover, use of intuition may be reduced by provision of relevant information to support decision-making through financial education since individuals tend to rely on intuition where relevant information is lacking. However optimal results may not be achieved where individuals trust their intuitions in decision making. This theory supports the review of this study and therefore the study was anchored on it.

### 3. Data and Methods

The research design used for this study is the descriptive research design. The choice of this design was premised on the researchers' inability to manipulate the variables used in the study. The research population for this study consists of owners of the SMEs in Edo State. Due to the large size of the target population, the purposive sampling technique was adopted to choose 80 (eighty) as sample size. The source of data collection is primary through the means of structured questionnaire which was designed in five Likert scale in valuing the items of questions that are relevant to aid understanding the relationship between the independent and dependent variables.

The non-parametric statistic tool was used to analysis the data collected. Chi-square was employed for data analysis because of its robustness with respect to distribution of the data. To ensure the content and face validity of the instrument, the researchers adopt a test-retest method to ensure the reliability of the research instrument

### 4. Data Analysis and Discussion of findings

**Table 1: Financial Management aspect of Financial Literacy**

|   | SA<br>F<br>(%) | A<br>F<br>(%) | UD<br>F<br>(%) | D<br>F<br>(%) | SD<br>F<br>(%) |
|---|----------------|---------------|----------------|---------------|----------------|
| I have improvement in Financial and Cash Management as a result of financial literacy                 | 33<br>(36.7)   | 19<br>(21.1)  | 25<br>(27.8)   | 10<br>(11.1)  | 3<br>(3.3)     |
| The knowledge on records keeping has improved my operations and ease of tax filing                    | 24<br>(26.7)   | 28<br>(31.1)  | 16<br>(17.8)   | 16<br>(17.8)  | 6<br>(6.7)     |
| There is a significant improvement in my financial reporting as a result of proper financial literacy | 21<br>(23.3)   | 17<br>(18.9)  | 26<br>(28.9)   | 19<br>(21.9)  | 7<br>(7.8)     |
| There is a significant improvement in my budgeting skills as a result of my financial literacy        | 32<br>(35.5)   | 15<br>(16.7)  | 17<br>(18.9)   | 16<br>(17.8)  | 10<br>(11.1)   |

**Source: Authors' Survey (2021)**

Table 1 shows that 33 (36.7%) and 19 (21.1%) of respondents strongly agreed and agreed respectively that There is improvement in Financial and Cash Management of their business as a result of financial literacy. Then were 25 (27.8%) undecided, 10 (11.1%) of the total respondents disagreed and 3(3.3%) response as to strongly disagree.

The table further shows that 24 (26.6%) and 28 (31.1%) of respondents strongly agreed and agreed respectively that the knowledge on records keeping has improved the operations and ease of tax filing. Also, 16 (17.8%) were undecided while 16 (17.8%) disagreed to the statement and 6 (6.7%) respondents strongly disagreed. The table also depicts that 21 (23.3%) and 17 (18.9%) of the respondents strongly agreed and agreed respectively that There is a significant improvement in financial reporting as a result of proper financial literacy. 26 (28.9%) of the total respondents were undecided with the statement, while 19 (21.9%) and 17(7.8%) disagreed and strongly disagreed to the statement respectively.

The table also shows that 32 (35.5%) and 15 (16.7%) of the respondents strongly agreed and agreed respectively that There is a significant improvement in budgeting skills as a result of financial literacy. 17 (18.9%) of the total respondents were undecided with the statement above while 16 (17.8%) and 10 (11.1%) disagreed and strongly disagreed to the respectively. From the analysis of table 4.2.8, we could conclude that financial management aspect of financial literacy has influence on SMEs.

**Table 2: Debt Management aspect of Financial Literacy**

|   | SA<br>F<br>(%) | A<br>F<br>(%) | UD<br>F<br>(%) | D<br>F<br>(%) | SD<br>F<br>(%) |
|---|----------------|---------------|----------------|---------------|----------------|
| Financial literacy has assisted me in accessing credit loans easily from financial institutions | 27<br>(30.0)   | 18<br>(20.0)  | 30<br>(33.3)   | 8<br>(8.9)    | 7<br>(7.8)     |
| Financial Literacy helps me to know if loan is suitable for my business                         | 23<br>(25.6)   | 16<br>(17.8)  | 23<br>(25.6)   | 18<br>(20.0)  | 10<br>(11.1)   |
| Access to loans have helped in the smooth operations and positive performance of my business    | 23<br>(25.5)   | 12<br>(13.3)  | 27<br>(20.0)   | 20<br>(22.2)  | 8<br>(8.9)     |

**Source: Authors' Survey (2021)**

Table 2 shows that 27 (30.0%) and 18 (20.0%) of respondents strongly agreed and agreed respectively that financial literacy has helped in accessing credit loans easily from financial institutions. Then were 30 (33.3%) undecided, 8(8.9%) of the total respondents disagreed and 7(7.8%) response as to strongly disagree. The table further shows that 23 (25.6%) and 16 (17.8%) of respondents strongly agreed and agreed respectively that Financial Literacy helped to know if loan is suitable for my business. Also, 23 (25.6%) were undecided while 18 (20.0%) disagreed to the statement and 10 (11.1%) respondents strongly disagreed.

The table also depicts that 23 (25.5%) and 12 (13.3%) of the respondents strongly agreed and agreed respectively that knowledge about Access to loans have helped in the smooth operations and positive performance. 27 (20.0%) of the total respondents were undecided with the statement, while 20 (22.2%) and 8 (8.9%) disagreed and strongly disagreed to the statement respectively. From the analysis of table 4.2.9, we could conclude that financial literacy has influence the debt management of SMEs.

**Table 3: Savings aspect of Financial Literacy**

|  | SA<br>F<br>(%) | A<br>F<br>(%) | UD<br>F<br>(%) | D<br>F<br>(%) | SD<br>F<br>(%) |
|--|----------------|---------------|----------------|---------------|----------------|
| Financial Literacy has helped me in proper cash management and savings | 29<br>(32.2)   | 15<br>(16.7)  | 28<br>(31.1)   | 13<br>(14.4)  | 5<br>(5.6)     |
| Financial Literacy has saved me from incurring unnecessary expenses    | 26<br>(28.9)   | 17<br>(18.9)  | 22<br>(24.4)   | 19<br>(21.1)  | 6<br>(6.7)     |

**Source: Authors' Survey (2021)**

Table 3 revealed that 29 (32.2%) and 15 (16.7%) of respondents strongly agreed and agreed respectively that Financial Literacy has helped in proper cash management and savings. Then were 28 (31.1%) undecided, 13 (14.4%) of the total respondents disagreed and 5(5.6%) response as to strongly disagree. The table further shows that 26 (28.9%) and 17(18.9%) of respondents strongly agreed and agreed respectively that Financial Literacy has helped in incurring unnecessary expenses. Also, 22 (24.4%) were undecided while 19 (21.1%) disagreed to the statement and 6 (6.7%) respondents strongly disagreed. From the analysis of table 3, we could conclude that financial literacy has influence the saving aspect of SMEs.

**Table 4: The Impact of Financial Literacy on the performance of Small-Scale Enterprises**

|  | SA<br>F<br>(%) | A<br>F<br>(%) | UD<br>F<br>(%) | D<br>F<br>(%) | SD<br>F<br>(%) |
|--|----------------|---------------|----------------|---------------|----------------|
| Financial Literacy has led to an increased profit margin in my business  | 36<br>(40.0)   | 26<br>(28.9)  | 19<br>(21.1)   | 3<br>(3.3)    | 6<br>(6.7)     |
| Financial Literacy has led to an increased sales growth in my business   | 22<br>(24.4)   | 39<br>(43.3)  | 16<br>(17.8)   | 7<br>(7.8)    | 6<br>(6.7)     |
| Financial Literacy has led to an increased market share in my business   | 29<br>(32.2)   | 28<br>(31.1)  | 14<br>(15.6)   | 14<br>(15.6)  | 5<br>(5.6)     |
| Financial Literacy has led to an increased positive and significant overall financial performance in my Business | 24<br>(26.7)   | 31<br>(34.4)  | 7<br>(7.7)     | 13<br>(14.4)  | 15<br>(16.7)   |

**Source: Researchers' Survey (2021)**

The result in Table 4 revealed that 36(40%) and 26(28.9%) of respondents strongly agreed and agreed respectively that Financial Literacy has led to an increase in profit margin. Then were 19(21.1%) undecided, 3 (3.3%) of the total respondents disagreed and 6 (6.7%) response as to strongly disagree. The table further shows that 22 (24.4%) and 39(43.3%) of respondents strongly agreed and agreed respectively that Financial Literacy has led to an increase in sales growth. Also, 16 (17.8%) were undecided while 7(7.8%) disagreed to the statement and 6 (6.7%) respondents strongly disagreed. The table also depicts that 29 (32.2%) and 28 (31.1%) of the respondents strongly agreed and agreed respectively that Financial Literacy has led to an increase in market share. 14 (15.6%) of the total respondents were undecided with the statement, while 14 (15.6%) and 5 (5.6%) disagreed and strongly disagreed to the statement respectively. The table also shows that 24 (26.7%) and 31 (34.4%) of the respondents strongly agreed and agreed respectively that financial Literacy has led to an increased positive and significant overall

financial performance. 7 (7.7%) of the total respondents were undecided with the statement above while 13 (14.4%) and 15 (16.7%) disagreed and strongly disagreed to the respectively. From the analysis of table 4, we could conclude that financial literacy has impact on the performance of Small and Medium Scale Enterprises in Edo State, Nigeria.

### **Hypotheses Testing**

The hypothesis of this research work is tested at 5% level of significance using the non-parametric chi-square test.

#### **Hypothesis 1**

Financial literacy has no significant positive impact on profit margin of SMEs.

Decision Rule: Reject  $H_0$  if  $X^2$  calculated is greater than critical table value and accept  $H_1$ . Accept  $H_0$  if  $X^2$  calculated is less than critical table value and reject  $H_1$ .

The calculated  $X^2$  is 42.1 and critical table value is valued at 5% level of confidence (9.488) using a degree of freedom of 4. We reject  $H_0$  (null hypothesis) and accept  $H_1$  (alternative hypothesis) that is financial literacy does have impact on profit margin of SMEs.

Hypothesis one revealed that financial literacy has impact on profit margin of SMEs. This implies that financial literacy has positive impact on SMEs. This finding is consistent with the study of Huston, (2017) and Glaser & Walther (2014).

#### **Hypothesis 2**

Financial literacy has no significant positive impact on sales growth of SMEs

Decision Rule: Reject  $H_0$  if  $X^2$  calculated is greater than critical table value and accept  $H_1$ . Accept  $H_0$  if  $X^2$  calculated is less than critical table value and reject  $H_1$ .

The calculated  $X^2$  is 40.3 and critical table value is valued at 5% level of confidence (9.488) using a degree of freedom of 4. We reject  $H_0$  (null hypothesis) and accept  $H_1$  (alternative hypothesis) that is financial literacy does have impact on sales growth of SMEs.

Hypothesis two revealed that financial literacy does have impact on sales growth of SMEs. This implies that financial literacy has positive impact on SMEs. This finding is consistent with the study Grohmann, Menkhoff, & Storck, (2015) and Leora, Lusardi, & Peter, (2015).

#### **Hypothesis 3**

There is no significant relationship between the financial literacy and market share of SMEs.

Decision Rule: Reject  $H_0$  if  $X^2$  calculated is greater than critical table value and accept  $H_1$ . Accept  $H_0$  if  $X^2$  calculated is less than critical table value and reject  $H_1$ .

The calculated  $X^2$  is 23.5 and critical table value is valued at 5% level of confidence (9.488) using a degree of freedom of 4. We reject  $H_0$  (null hypothesis) and accept  $H_1$  (alternative hypothesis) that is There is significant relationship between the financial literacy and market share of SMEs.

Hypothesis three revealed that financial literacy does have impact on sales growth of SMEs. There is significant relationship between the financial literacy and market. This finding is consistent with the study Moore, (2013) and Musie, (2015).



## 5. Conclusion and Recommendations

This study has attempted to assess the impact of financial literacy on the performance of small and medium scale business. This study reviewed the various forms including journal papers, articles and other relevant materials. Based on this, the study discovered that financial literacy helps to increase profit margin, sales growth and market shares in small scale enterprises in Nigeria. The problems militating against the operation of such system despite its apparent values were also examined. It was observed that although small scale enterprises may not be able to adopt systems of accounting, A number of small-scale business kept no records pertaining to their financial operations, finance, among other; while some employed professional accountants to keep proper accounting records of their business. The accounting records keeping contribute to the performance of small-scale business hence small-scale business not actually kept proper accounting records of their activities; they could be encouraged by customized adaptive systems. Based on this, the researchers made the following recommendations;

- i. There should be a training of accountants by this institution and the various professional institutes should focus more on practical means of solving accounts reporting needs of small and medium scale enterprises.
- ii. There should be a training that will help SMEs in increase of profit margin.
- iii. The government should provide adequate financial assistance, and if there is adequate financial assistance, more unemployed Nigerians can engage in small-scale businesses, allowing them to earn a living without having to search for an unavailable white-collar employment.

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