Sustainable Development for SME's by Tackling Financial Distress

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Abstract

Financial distress may be interpreted as a wake up or early bankruptcy phenomenon with regard to the financial condition faced by a company or business, also known as pre-failure or liquidation vacation conditions. Both large businesses or small business can overcome a financial distress or bankruptcy by predicting things that can cause bankruptcy by analysing existing condition of financial distress. Such bankruptcy may be caused by the company's failure to generate profit in its operational activities and the company's failure to pay off its debt. The objective of this research is to identify the main factor which causes financial distress for SME's. With this purview, the research focuses on behavioral traits that have the ability to manage finances and stay out of financial distress. Data was collected by questionnaire and distributed to each of the small and medium sized enterprises who were selected on the basis of simple random sampling.

Keywords: Financial distress, Sustainable development, SME's, bankruptcy

1. Introduction

India represents one of the world's fastest growing economies. Economic growth has been steadily accelerating in the last half decade and, most importantly, has remained very stable. This growth was driven by the Government's vigorous socio-economic policies, an influx of domestic and foreign capital, and a rise in disposal income and consumption among many other attributes. Small and Medium enterprises (SME) sector is being said as one of the key factor that is being claimed as the backbone of India's economy. Comprising of manufacturing, transportation, service industry, food processing, packaging, chemicals and IT, the SME sector has emerged as the Indian economy's most vibrant and competitive growth driver in the last few decades. This sector employs around 460 million i.e.40% of India's workforce, which is next to agriculture. Its contribution towards Indian GDP is 30% of the total GDP. Increasing population and growing urbanization have resulted in a huge rise in demands for consumption in India. This challenges the sustainability of the strong economic growth. In times when policies such as Make in India and Startup India promote manufacturing and young entrepreneurship in India, SMEs are seen as an important opportunity.

2. Literature Review

Meher, Kishor. (2018) in the research titled "Financial Sustainability of SMEs by Injecting Debt Finance" seek to assess the impact of debt financing on the financial health of SME's by taking debt finance as an explanatory variable, the study adopts quantitative approach. The determinants of financial performance taken as dependent variables are short-term financial position, long term financial position, assets turnover ratio, degree of financial leverage and profitability as financial performance brings financial sustainability to SME's. The results indicate that debt financing has a positive impact on both the short-term and long-term financial position, which indicates that SME's have gained the ability to pay current liabilities and are able to pay long term interest resulting in financial sustainability".

Bansal, Rohit & Singu, Hari Babu. (2017) in their study "Financial distress prediction of Indian companies: Future perspectives "identified the need on the basis of literature surveyed that there is a need of models which can make dynamic predictions by using dynamic variables. Identification of these dynamic variables will warn the management to take appropriate steps and decisions in advance to avoid financial distress and costs associated with business failure".

Rathod, Chirag & Ranpura, Darshan & Patel, Chirag. (2016) in their study "SMEs and Economic Growth in India: A Comparative Study", identified that the damaging factors faced by SME have been cited as low capital base, technology access difficulties, credit restriction, low access to business services, human resource efficiency constraint, low market knowledge, low lobbying ability and infrastructural constraints".

Jahur, Mohammad & Quadir, S.(2012) in their research " Financial Distress in Small and Medium Enterprises (SMES) of Bangladesh: Determinants and Remedial Measures" identified the causes of financial distress among SME's of Bangladesh, wherein they employed both financial and statistical tools to analyze the data. The study identified several potential financial distress related problem areas, such as rate adequacy, market patterns, indebtness, management capacity, financial planning etc.

Thus financial distress means stress from intimate, social and financial circumstances. Financial distress is a situation where the short-term and long-term liabilities of any company cannot be paid off. In fact, the assets of the company are not enough to settle its financial obligations. Baldwin & P Mason (1983) define it as "When a company deteriorates to the point where it is unable to fulfill its financial obligations", it is said to be in financial distress. Pindado (2005)Ward (1997) concluded that "if a corporation has negative accumulated earnings for consecutive years, merely recognized as cumulative losses and diminished results, it will be subject to a situation of financial distress".

3. Method

3.1 **Type of Research:** With the help of explanatory study hypothesis as to how financial behavior traits consist of self control, planning and patience capacity affect financial distress is undertaken.

3.2 Hypothesis

- Ho: There is no significant relationship between financial behavior and financial distress of SME's

  Ho1: There is significant relationship between financial behavior and financial distress of SME's

The first variable of the study is financial behavior. To study this behavior questions related to management, procurement, investment of funds was asked by the entrepreneurs. The second variable of the study is financial distress. To study this variable, questions related to the ability to manage critical situations of finance were asked by the entrepreneurs.

A judgmental sampling technique was used to collect the data from owners of the SMEs. A self structured method was designed to measure the relationship among the variables.

3.3 Data Analysis and Findings

The main findings of the study are discussed as follows:

Demographic characteristics of the respondent

Age	Number	Percentage
20-30	6	20
31-40	11	36.66
41-50	9	30
51 or above	4	13.33
Total	30	100

Table I: Age of the Respondent

Table I represents the age group of the owner of SMEs. From the data it is revealed that 36.66 percent of the respondents belongs to the age group of 31-40. It shows lack of interest and inability of the youngsters towards the entrepreneurship.

Education	Number	Percentage
Secondary	7	23.33
Higher secondary	16	53.33
Graduation	4	13.33
Post-graduation	3	10
Total	30	100

Table II: Education of Respondent

According to table II, out of the total respondents, 53.33 percent respondents belong to the higher secondary education which shows that entrepreneurs are managing their SMEs since years without even meeting the basic educational qualifications.

Type of Business	Number	Percentage
Manufacturing	18	60
Retail	12	40
Total	30	100

Table III: Nature of SMEs

Out of the total respondents surveyed, 60 percent of the SMEs belong to the manufacturing sector and 40 percent are from retail sector. In Rajasthan,SMEs are mainly in manufacturing and retail as compared to the other sectors.

SMEs experience	Number	Percentage
0-05 years	3	10
06-10 years	14	46.66
11 to 15 years	11	36.66
15 years of above	2	6.66
Total	30	100

Table IV: Length of SMEs

SMEs were also categorized based on experience. Out of the total SMEs surveyed, 46.66 percent of the SMEs are in the business from 06- 10 years which is highest among all the categories.

Variables	1	2
Financial behaviour (1)	-	
Financial distress (2)	*-.65*	-

Pearson's Correlation

From factual evidences, it was found that there is a negative correlation between financial behavior and financial distress. As the financial behavior of the owners of SMEs increases, financial distress decreases. Financial behavior is the ability of the owners of SMEs to manage their funds which leads to sound decision making. Financial behavior often comes with experience and SMEs having more than 5 years of experience are stronger in terms of financial behavior. Sound financial behavior enables the owners to overcome financial instability which may lead to financial loss and inability to pay their debts. Both the variables of the study are affected by number of factors which includes experience & age of SMEs, their nature, education of SMEs owners. All these factors collectively affect the financial behavior of SMEs and as a result further financial behavior influences financial distress.

4 Recommendation

The financial distress is characterized by various characteristics. SMEs as a buffer of the economic system contribute to the economy. So the most critical job of government. Apex Body, Regulatory Agencies, professional bodies is to avoid SME's from becoming financially distressed. Therefore, the following policy and strategic steps were suggested to grow non-distressed SMEs as well as to reinforce distressed SME's on all fronts in order to get them out of financially distressed circle:

- Financial Planning should be appropriate to SME's
- SME's will maintain all the financial transaction records in a device manner, In this case qualified accountants should be named to prepare the financial statements by following provisions of companies Act 2013 and the International Financial Reporting Standards adopted by IAS. This will provide correct accounting and financial information for management of SMEs for making routine as well as non-routine management decisions. This will also enable lending agencies to conduct credit risk analysis; and rating agency to carry out the rating job for the SME's.
- SMEs should implement internal audit to restore effective SME financial control
- SMEs need to have both an effective management system and skilled and skilled workforce. This should have a positive influence on the efficiency and productivity of SME's. Good culture within the company creates leadership within the organization that can track the financial distress early and thus avoid SME's from exposing themselves to financial and operational risk.

5 Conclusion and Recommendation

Thus on the basis of results obtained it can be concluded that financial behavior has a positive effect on financial distress. Hence if someone wants to avoid getting into financial distress, they can manage to do so by controlling Financial behavior traits like planning, patience and capacity of control. Everyone can come up with a better financial condition if everyone has the patience to manage their money and gain more money in future. Financial success demands that everyone know how to manage their money.

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