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SMALL & MEDIUM SCALE MARKETING ENTERPRISES IN NIGERIA AND CAPITAL INVESTMENT DECISION MAKING

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Abstract

*S*mall &Medium marketing enterprises (SMMEs) from studies play an important role in the growth, employment and development processes of the developing economies of which Nigeria is one. Capital investment is one of the major sources of identifying those projects whose return will maximize the wealth of shareholders using the appropriate technique. This study investigated the role capital investment decision making play in the growth of SMMEs in Nigeria. Theoretical approach was employed on small/medium firms budgeting, conceptual and theoretical frame work, financial management, method of investment appraisal techniques and other related factors on investment decision of small and medium scale marketing firms. This was necessitated because, apart from time constraints and resources limitation, most small business may not want to expose their decision making criteria to open discussions because they are owner managed hence, the few available past works, like journals, magazines, textbooks and appropriates websites were used as guidelines. Review showed that most small scale firms do not consider these appraisal methods as important in their capital project decisions. It was therefore suggested that academic communities should emphasize on the benefits of using these methods to Business graduates as future practitioners in commerce and industry. Studies revealed also that SMEs multitudes use very simple and traditional technologies and serve a limited market. The shortcomings of this investigation could be improved by the government breaching the gap between large and small firms by providing all needed support to SMEs,

Keywords: SMMEs, Marketing, Enterprises, Capital Investment, Decision.

Introduction

The importance of small and medium scale enterprises in Nigerian economy cannot be over emphasised. Small and medium enterprises represent the spinal cord of the economy of a country (Ramadani, 2011). SMEs have contributed reasonably towards employment, gross domestic product (GNP) and sustainable development of Nigeria. UNCTAD (2005) viewed that available evidence suggests that SMEs have played a major role in the growth and development of the leading economies in Asia. The objective of every business enterprises is the maximization of the wealth of the owners, by taking continually investment and financial decisions. Investment also known as capital budgets are projections of new outlays for land, buildings, machinery and equipment, and related incremental working capital, as well as major outlays for new products and services, expanding markets, new technology, e.t.c.

Investment decisions are long term capital assets such as plants and machinery, equipment, land and buildings etc. The major principle behind capital budgeting concerns actual cash flow that is relevant to the investment decision under consideration (Adetifa, 2005 p.264). There are various techniques available in financial management for the purpose of determining and analyzing the viability or otherwise of any investment

decision, yet, most firms disregard the use of these techniques and go ahead with intuition method. The resultant effect is business collapse or at times minimal performance. Akpala (1998) identifies attitude to work, leadership style and motivation as some of the factors that exert negative effect on organizational performance in Nigeria. Small and Medium Enterprise Development Agency of Nigeria (SMEDED) in 2008, reports that most small and medium scale businesses in Nigeria die before their fifth anniversary. In other to guide against this, SMEs should imbibe the culture of adequate financial management from inception of their businesses.

Any form of financial projection involves both an examination of past trends and specific assumptions about future behavior of revenues, cost expenses, and other receipts and payments. Past trend analysis can range from simple "eyeballing" of obvious patterns to applying a variety of statistical methods to the available data in order to establish a trend line or curve as the basis for judging future conditions. As warned by (Helfert 2001) "The mathematical elegance of statistical methods should not be allowed to supplant the effort of making realistic future assumptions about specific company investment decision and decision on market conditions, industry performance, and the national and world economic outlook affecting the likely financial performance of the business". We found that less attention is paid to these mathematical variables and financial management techniques in the investment decision in small scale enterprises (Adetifa 2005) listed information needed for capital project appraisal as; Sources of finance; cost of capital; cash flow forecast/ rate of return; rate of return on other investment avenue and methods of investment appraisal (traditional and discounted cash flow methods). In this project, efforts were made to identify those factors other than the theoretical investment appraisal techniques that are considered in taking investment decision in small/medium scale firms in Nigeria.

Objective of the study

The main objective of this study was to assess the role of capital investment decisions in the growth of small and medium scale marketing enterprises in Nigeria.

The preposition: Capital investment decision has no impact in the growth of small and medium scale marketing enterprises in Nigeria.

Literature review

Small/Medium firms budgeting: Despite the importance of capital investment to Small/Medium scale firms, most capital budgeting surveys over the past years have focused on the investment decision of large firms (Moore and Reichardt, 1983, Scott and Petty, 1984, and Bierman, 19930). An exception is (Graham and Harvey, 2001), who compare the capital budgeting practices of small and large firms. Even their small firms are quite large, however, with a revenue threshold of an equivalent of $1 billion used to separate firms by size. Indeed less than 10 percent of their sample report sales fall below $25 million. Thus, Graham and Harvey's result do not directly address the investment decision of small firms. Several reasons may account for small/medium and large firms using different criteria to evaluate projects. First, small/medium business owners may balance wealth maximization (the goal of a firm in capital budgeting theory) against other objectives such as maintaining the independence of the business (Ang, 1991, Keasey and Watson, 1993) when making investment decisions. Secondly, small business lacks the personnel resources as in large firms and therefore may not have the time to make proper investment decisions. There is

therefore a need to identify the conditions that inform investment decision of small business, hence the need for this study. This study is therefore to identify the criteria for investment decisions in small/medium scale marketing firms and compare the outcome with theoretical investment decision criteria and the effect on the performance of such enterprises. The scope of the study is centered on the investment decision techniques and their suitably to small/medium marketing business usage, and the analysis of performance of the case study over time. However, the use of the study alone may not represent the popular practice but it is hoped that it will throw light in the activities of small firms' decisions making practice and the impact on their performance. This study is hoped to provide an insight into 'other' investment decision making criteria which may not have been given significant place in financial management literature. This is particularly important when such conditions still enable the business maximize the wealth of investors in terms of return on asset and profitability.

Conceptual frame work

Variously, much has been conceptualized on Small and Medium scale enterprises depending from which perspective each author is looking at.Japan for instance, sees small enterprises as those operating with less than 300 employees and paid up capital of 100 million yen in the wholesale business and 50 employees in the retail business. (Ekpeyong & Nyang, 1992). In the USA, Britain and Canada, small scale is defined in terms of annual turnover and the number of paid employees. Britain conceives small scale with annual turnover of 2 million pounds less, with fewer than 200 paid employees. SMEs conception and definition is dynamic in character and changes with time (Olumide, 2004). It also varies among institutions and countries. The European Union (EU) as cited in (UNIDO/OECD, 2004) made a general distinction between self employment, micro, small and medium-sized businesses by defining them as; a firm with no employee is self-employed; 2-9 employee is micro business; 10-49 employees is small business; and 50-249 employees is medium-sized business.

Balunywa (2010) however argues that number of employee may not be a good indicator, especially when the company is labour intensive. This is in contrast with views of Ayanda and Laraba (2011) who upheld the crucial role of the SMEs in employment generation in Nigeria. The enterprise sector in Nigeria may be described as a dichotomy of dual structure. At one end are a few large modern capital-intensive, resource-based, import-dependent and assembly oriented enterprises, while at the other end, are multitudes of small and informal enterprise sector that use very simple and traditional technologies and serve a limited market.

Most marketing organizations in Nigeria such as Addide shops, Babcock University super markets, Yemyem in University of Lagos among others fall within one or two of the above SMEs' description. Hence this study conceptualizes on SMEs on the capital investment decisions.

Financial management

Literature suggests that most small firms do not depend mainly on the staff especially the finance and accounts staff for the preparation and analysis of financial data in their investment decision making. This may be due to the fact that the criteria for investment decision may not follow the use of investment appraisal techniques that estimate project viability, cash flows and risk. Manager and owners of small business often maintain that the financial management of their firms is different from the financial management of large firms because some large company financial practices are not necessary or

appropriate for the small firm .(Lamberson, 2009). Working capital (WC) is another aspect of financial management. It is a trading capital that is required to meet the short financial obligations of a firm. According to ALShubiri (2011) working capital refers to current assets minus current liabilities. Current assets consist of cash receivables, inventory, etc. While current liabilities comprise trade creditors, bank overdraft and other debt obligations due within one year. The concept of working capital is so important to the operation of a business especially in manufacturing and marketing sector such that its absence or inadequacy can impede the growth and survival of such business. In the opinion of Valipour, Moradi and Karimi (2012) working capital is defined as investing in current assets such as cash, short- term securitiies, accounts receivables and inventories. Working capital according to Keyinde (2011) as cited by Geoffrey and Elliot (1969) is customarily divided into two categories: Gross and Net. T he gross concept advocate that a firm should posses working capital just adequate and sufficient to meet the firm's needs. While the net concept ensures continuous liquidity of the firm, the concept advocates a finance of the working capital by permanent sources of funds e.g. shares, debenture, long term debt, preference share capital, retained earnings, etc. The net concept advocates the efficient combination of long term and short term sources of finacing working capital (Keyinde, 2011; Uremadu, Egbide and Enyi, 2012). The study generally discovered that most marketing enterprises of small and medium scale do not take the concept of WC as important unlike their large scale counterparts. Consequent upon this is low profitability.

(2009) According to Egwide, profit is the excess of revenue generated by a firm over the cost that generated it within an accounting period. If WC is not properly managed, profitability no doubt will be impeded. NorEdi and Noriza (2010) view profitability as being used as a measure for corporate performance because it evaluates the efficiency with which plant, equipment, and current asses are transformed into profit.

Theoretical framework

Related theories on business and enterprise performance are reviewed in this section for theoretical discourse.

1. Theory of the business

Druker developed this theory in 1994. This theory postulates that many businesses decline and fail because they make assumptions about the society, markets, products, customers, technology, their mission, vision, and goals among others that form the basis of fundamental business decisions which eventually become obsolete or fadeout. This theory therefore is suggestive of reengineering, benchmarking, downsizing and outsourcing, total quality management, economic value analysis in other to survive today's business challenges.

2. Contingency theory

This theory clams that the optimal course of action is dependent upon the internal and external situations.The management literature offers a variety of established contingency framework (Zeithaml, varadarajan and zeithaml, 1988) . This approach has its root in general systems theory and the open system perspectives (Von Bertalanffy, 1951, Anderson, 1957). The open system sees the complex organization as a set of interdependent parts that, taken together, constitute a whole which, in turn is interdependent with some larger environment. Interaction between elements within the organization and between it and its environment result in adaptation and equifinality.

Thompson (1967) integrated these root concepts into a concrete framework that now represents a cornerstone of the contingency theory.

3. Firm performance evaluation approach

There exist quite a number of theoretical frameworks for evaluating firm's performance and effectiveness in relation to resource usage. The frameworks explore different approaches which include the goal approach, system resource among others.

4. The Goal and Systematic Resource Approaches

The goal approach emphasizes measuring firm performance in terms of financial measures, and directs owner-managers to focus attention on financial performance such as profits, revenues, returns on investment, returns on sales and returns on equity. While the systems approach assesses the ability of an organization obtaining its resources, the goal approach measures the extent an organization attains its financial goals. The most common system resource measures used by the SMEs include number of employees, annual turnover, market share and revenue per employee (Mohr and Spokeman, 1994)

5. Investment decision

The ultimate aim of any investment decision is to realise adequate returns on investment. Hence the firm must invest in working capital as well as in fixed assets to operate on a day to day basis, meeting her operational needs from such investment of resources. As pointed out however, by (Akinsulire, 2002) 'the continued existence of any company is not predicated on it's investment on short term basis but rather on its long term investment strategies". Therefore, business would continue to invest both on short-term and long-term basis if they are to remain.

Investment in whatever form is a decision that has to be made. The ability to analyze and make capital investment decision allows you as the owner or manager of a business to ensure that your limited resources are allocated to the project or projects that will best achieve your strategic goals (hence they are also sometimes referred to as strategic investment decisions) (Yamusa, Adelusi & Ademola, 2011). Such decisions could relate to capital investment such as the construction of a new factory, development of a new website, commitment to a new marketing campaign, the acquisition of a business or establishing new outlet in the case of our subject matter. Basic financial management theory expect that such investment decisions should be based on the outcome of appraisal techniques such as Payback Period, Accounting rate of return, Profitability Index, Internal Rate of Returns and Net Present Value to mention but a few.

(Crickett 2007) has this to say; identifying the need for investment can be problematic in most business because strategic planning is rarely carried out and when it is carried out, it is independent of any budgeting process. This separation of budgeting and planning can have an effect on business needs to include resource allocation in its strategic planning process. However generating ideas for strategic investment involves a level of risk and an investment of time on behalf of the proposal. Therefore, unless a business creates a culture that encourages and rewards staff for putting forward proposals, the business will miss many strategic investment opportunities.

Methods of Investment Appraisal Techniques

i. Gut-feel (intuition) techniques:

While the use of gut-feel is concentration in the least sophisticated of small firms, it is also widely used by firms that make primarily replacement investment. A firm may have limited options when it replaces equipment, and estimating future cash flows (i.e. incremental maintenance costs or efficiency gains) for each option might be difficult. For example, if a firm must replace a delivery truck, it may be difficult for the firm to

estimate difference in the future annual operating costs of two replacement vehicles under consideration. Moreover, if an investment is necessary for the firm's survival (and the owner is committed to maintaining the business as a going concern), the maximization of firm value may not be the business owner's primary objective. Instead, the owner may simply look for the alternative investment decision that has promising return at a reasonable cost. Thus, it is not surprising to find the small scale business owners use relatively unsophisticated methods of analysis to evaluate replacement option. Gut feel is used extensively by firms in the service industry. Although some service firms make substantial capital expenditures, the investments of many service firms might be limited to business vehicles or office equipment. A firm's primary considerations when evaluating this type of purchase decision may be cost, reliability, and product features. Structuring a discounted cash flow analysis of these investments can be difficult.

ii. Payback period: Payback period conveys important economic information in at least some circumstances. For example, the payback period can be rational project evaluation tool for small firms facing capital constraints (i.e firm that do not operate in the perfect financial markets envisioned by capital budgeting theory). In this case, projects that return cash quickly could benefit a firm by easing future cash flow constraints. The use of accounting rate of return increases with firms' growth rates; it is significantly higher than the sample mean for firm entering new lines of business. Each of these characteristics can indicate high borrowing needs. The accounting rate of return is thus especially important if a firm must provide banks with periodic financial statements, or is required to comply with loan covenants based on financial statement ratios.

(iii). Discounted cash flow analysis: The most theoretically correct method- discounted cash flow analysis- is the primary investment evaluation method. Not surprising, owners with advanced professional degrees are most likely to use this method; normally, project's value should be estimated using a discounted cash flow (DCF) valuation, and the opportunity with the highest value, as measures by the resultant net present value (NPV) to determine their selection and implementation. This requires estimating the size and timing of all of the incremental cash flows resulting from the project. These future cash flows are then discounted to determine their present value (Adetifa, 2005). These present values are then summed, and this sum net of the initial investment outlay is the NPV (Net Present Value). The NPV is greatly influenced by the discount rate. Thus selecting the proper discount rate- the project "hurdle rate"- is critical to making the right decision. The hurdle rate is the minimum acceptable return on an investment. i.e the project appropriate discount rate. The hurdle rate should reflect the riskiness of the investment, typically measured by volatility of cash flows, and must take into account of the financing mix. Managers usually use models such as the CAPM or the APT to estimate a discount rate appropriate for a particular project, and use the weighted average cost of capital (WACC) to reflect the financing mix selected. But excluding the finance and accounts professionals from such decision making may deprive the firm the use of the techniques.

As it is shown when interpreting the performance of a business one must make a clear distinction between accounting results and economic results. The former are based on generally accepted accounting principles (GAAP), under which all publicly held businesses are required to record their transactions, and repot their financial position and operating results. The latter represent a translation of these according data and results

into a basic cash-in cash-out framework, which is used to establish the ultimate test of economic performance and value creation. However, as pointed out by (Helfert, 2001) both types of results depend on sound management of every aspect of the company, expcet that cash-flow based principles and tools give much more direct decision support and economic meaning to performance evaluation and value creation. Both sets of measures and tools have their place in business analysis, depending on the circumstance of their use. Over the past two decades there has been a growing shift in the direction of cash-flow based principles and measures, inflation-adjusted and applied across time and geographic boundaries. We believe this to be a sound development for better decision making and investment analysis. There is no doubt therefore that factors other than financial play some roles in investment decision of small/medium firms.

Some of the major determinant factors investing in new small outlets are listed below;

1. Location and the targeted customer: Here the management felt that the location of an outlet should be convenient to the targeted customers in terms of accessibility with vehicular traffic.

2. Affordability of products by targeted customer The concern here is weather the products are affordable amongst the targeted customer in terms of ability to pay for all the various products that will be offered by the proposed outlet.

3. Financial commitment (Initial outlay): though, this factor ought to be among the most important investment decision, in fact, investment decision can be indifferent to the initial outlay where appraisal techniques proof that the cash inflow project will exceed the initial outlay and so add to the value of the firm. The most popular among such investment appraisal methods are the Net present Value and the Internal Rate of Returns. Others may consider payback Period where time factor is a concern.

4. Conditions attached to the acquisition of the landed property: The conditions attached to the acquisition of the landed property play a prominent role in the investment decision of indigenous fast food operators as the more favorable the terms and conditions for acquiring the property, the higher the desire to have them all other factors being equal.

5. Perceived level of Competition in the Locality: Being the first to establish an outlet can be perceived to be very advantageous in some cases and as such may not suffer much in terms of competition. It is believed that such advantage would have provided the opportunity to develop the taste of clientele; hence the fear of existing outlet may drive away competition. Though in some cases where patronage is high, competition is relevant.

6. Access by Customers to the outlet and their safety: The ability of the customers to drive in and out without encountering much traffic congestion and the security of the environment is also an encouraging factor in the establishment of an outlet. This is particularly important as it is assumed that most users of fast food centers are car users and apart from their safety, access to free traffic is also an advantage and greatly influences patronage. It can be seen that apart from the initial outlay of the project, the regular investment criteria has less emphasis in the decision making process of small scale business.

Methodology

To investigate the objective and preposition of this study, theoretical approach using secondary data was adopted. Most of the SMMEs businesses are owner managed and

they are conservative reviewing information about their organizations and themselves. However, available data were reviewed from texts, journals, internets etc. Data collected were reviewed and based on that, conclusion and recommendations were made.

Summary/Conclusion

It was observed that the conception and definition of SMEs is dynamic in character and changes with time, and varies among institutions and countries. However, the basic definition parameters are same. Most of the SMEs businesses do not operate in the perfect capital markets that capital investment theory assumes for reasons of other factors as listed above. Many of the investment that small firms make cannot easily be evaluated using the discounted cash flow techniques recommended by capital budgeting theory. Many investment by small firms are not discretionary (a firm either makes a specific investment or it goes out of business), and future cash flows can be distortive. SMEs contribute to the growth of the Asian economies GDP, employment and other socio economic development. Most small & medium scale marketing enterprises in Nigeria use very simple and traditional technologies and serve limited market.

As stated by Daniels and Scott (2006), when future cash flows cannot be easily estimated, discounted cash flow analysis may not provide a reliable estimate of a project's contribution. Most of the firms investigated do not apply the basic investment appraisal methods known in financial management literature and the application of working capital management is giving little or no attention leading to low profitability.

For these reasons, small firms face capital budgeting challenges that differ from those faced by larger firms. Thus, it is possible that optimal capital budgeting methods for large and small firms may differ. However, a fully integrated capital budgeting theory-identifying the conditions under which discounted cash flow analysis is appropriate has yet to be developed.

Recommendation

Based on the research findings, we recommend the following;

1. Small and medium scale marketing enterprises are being encouraged to make capital investment decision a priority.
2. They should imbibe the methods of investment appraisal techniques in their dealings.
3. The concept of financial management, working capital and profitability should be taking seriously by SMMEs for increased performance and sustainability.
4. The Nigerian government should breach the wide gap between the large firms and the small/medium enterprises by intensifying effort in the provision of soft loans, conducive business environments, occasional training on investment decisions and financial managements techniques.
5. There should be other methods of evaluating investment decision by small and medium scale enterprises. We therefore implore the assistance of researchers and other cademicians to investigatethe appropriate method.

This is because, for any economy to succeed, especially after the kind of financial crises witnessed few years ago, the SMEs must be the driving force as they have the capabilities to expand and create employment opportunities thereby creating wealth in a massive way.

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