



Faculty of Economics, University of Niš, 16 October 2015

International Scientific Conference

**CHALLENGES IN BUSINESS AND ECONOMICS:
GROWTH, COMPETITIVENESS AND INNOVATIONS**

**EFFECTS OF IMPLEMENTATION OF THE
STRATEGIC FINANCIAL PLANNING
FOR SMEs IN REPUBLIC OF MACEDONIA**

Meri Boshkoska*

***Abstract:** SMEs are experiencing problems related to lack of funds in the current operations, which directly affects the power of companies to pay their obligations within the designated period of time. The reason for this situation arises as a result of the absence of financial management in SMEs which directly affects the failure of these companies. The purpose of this paper is to analyze the role of financial management and to identify the challenges of strategic financial planning for the survival and development of SMEs. This paper is expected to make a significant contribution to the existing literature by analyzing the challenges and effects of strategic financial planning in Macedonian SMEs and the impact of the implementation of this concept on the performance of SMEs. Additionally, the paper could cause academic interest in future development research.*

***Key words:** Small and medium enterprises, financial management, strategic financial planning, SFP practice.*

1. Introduction

Access to finance is identified as a key element for small and medium enterprises (SMEs) to succeed in their efforts to achieve the productivity, competitiveness, job creation and to contribute to poverty reduction in developing countries. Without finance, SMEs will not be capable to absorb new technologies neither can improve their competitiveness.

The relevance of this issue is highly pronounced in developing countries, and represents the latest trend in financial management in SMEs in Macedonia.

Financial theory and practice are occupied issues such as: preserving capital, maintaining liquidity, bankruptcy, and so on. The 1950s were marked by paying attention to the analytical approach to the process of financial decision making. Today, the emphasis on financial management is facing toward company where the manager brings

* Faculty of Economics Prilep, Republic of Macedonia; ✉ meribb@yahoo.com
UDC 334.012.63/.64

difficult financial decisions under the influence of external and internal factors by using the strategic planning (Block, S., and Hirt, G., 2008, p.163).

The practice of managing the SMEs shows that despite the identified need for the application of the strategic planning process in business management, managers/owners of these enterprises lack the “know – how” of key elements and methods of strategic management, especially for planning financial operations with a strategic approach.

Topics that treat issues of liquidity management can be found in the existing literature, inventory, cash flow, pro forma financial statements and more. But only a small number of publications focused on the financial problems of SMEs combined with methods and techniques of strategic planning.

Strategic financial management, and in this frame the strategic financial planning is one of the key managerial topics of SMEs which deserves to significant attention in terms of survival and growth of SMEs.

The aim of this report is to analyze the key purpose of fiscal management and financial strategic planning and to recognize the effects of the application of this process in fiscal management in SMEs.

The first part of the paper presents the role and importance of SMEs in the Macedonian economy and the problems these companies face in this sector in terms of influential factors in the external and internal environment. The analysis of the specific conditions in the external environment provides information about the possibilities and limitations in closer and broader business environment that are inputs in the process of strategic planning.

The second section of the paper explains the basic components of strategic financial management in order to interpret the structure and purposes of the managerial philosophy. The focus is on the problem of providing external financial sources which justifies the need for the formulation of alternative strategies in the selection of the most favorable source of funds.

The third section of the paper explains the central position and the role of financial management in SMEs. This section presents the different approaches in explaining the structure and objectives of financial management from several authors. In this part, a model of financial management for SMEs is presented that cannot be identified combined with influential environmental factors.

Therefore, the fourth section is an attempt to present a strategic approach to financial management. The focus is on the planning process of operational financial performance where a key role is the analysis of external and internal environment, formulating alternative goals and strategies in the structure of working capital, implementation of the selected strategy and control. Strategic approach to financial planning helps in solving the financial problems of SMEs and provides knowledge and understanding of the business environment and its effect on the financial decision.

2. The Importance of Small and Medium Enterprises and Business Environment

SMEs represent the basis of the economy in each country. These companies have a high share in GDP, contribute to the job creation and employment as well as encourage entrepreneurship and innovation. SMEs are drivers of growth of the Macedonian economy. In Macedonia, these enterprises have great importance in terms of their representation in the total number of enterprises, the number of open job positions, participation in the gross domestic product, etc. Statistical indicators for 2010 showed that on SMEs account 99.8% of the entire number of enterprises and 77% of the total number of employees are employed in this sector. The significance of these companies for growth of the Macedonian economy is evident in their share in the gross domestic product of a country which is 60.6% compared to large companies, whose share amounted to 39, 4% in 2010. The percentages, mentioned previously, point out the economic and social opportunities of this sector.

Namely, with small investments and government support can influence the situation on the labor market by creating new jobs which in turn affect the solving of the problem of unemployment that contributes to using social effects in the country. Also, SMEs can reduce import dependency of the certain raw materials through the conclusion of cooperation agreements with large companies. The possibility of flexibility that possess such businesses in changing and dynamic environment provides quick adjustment to other more profitable activities.

Employees in small and medium enterprises have the entrepreneurial skills and they are prone to innovations in production of products and services. Good management increases their importance in terms of improving productivity, increasing efficiency in using the resources available locally, increasing competitiveness. But despite this knowledge of the significance of these companies for the Macedonian economy, they grow up slightly and rise slowly. Why is that? The answer to this question is answered in the characteristics of the factors and conditions in the business environment in which this sector operates.

In the previous period, in the SME's business environment in Macedonia efforts have been made in order to improve the working conditions. For instance, the government has invested in the improvement of infrastructure in adopting legal measures for tax incentives, provide credit lines with favorable credit terms with the European Investment Bank, but it allocates little money in the budget to support the growth and development of SMEs through programs of entrepreneurship, innovation and competitiveness development. After consideration of the magnitude of the problem of debt and liabilities payment of the firms, the government adopted a Law on financial discipline that does not solve the problem entirely.

In terms of tax policy it is worth highlighting that SMEs have a significant amount of costs arising from the obligation to pay taxes. The financial pressures by the state through taxes and other fees, and strict inspection penalties negatively affect the financial stability of the companies and undermining their weak liquidity. The lack of funds in enterprises has caused the delay in payment of obligations by state institutions. In conditions where SMEs cannot collect its receivables from state institutions and their customers, is inevitable the emergence of illiquidity in the business sector. If a client cannot pay their obligations to the supplier, then the supplier cannot pay its obligations to its

suppliers and to employees. It spreads like a domino effect and plunges the whole economy in a liquidity gap.

In the Financial Stability Report of the Republic of Macedonia in 2013 the National Bank of Macedonia (NBRM) states that in such conditions, banks do not want to risk and refrain from giving loans to the private sector. They still consider this sector as risky that produces non-performing loans which points to higher risks for the financial stability of banks. Companies are being forced to borrow, even under unfavorable conditions for their work and risk their accounts to be blocked thereby create conditions for going into bankruptcy. According to the Central Bank the total indebtedness of the corporate sector accounted for about 2/3 of GDP in 2013 arising from the debt that the corporate sector has to foreign creditors, in which the worst performances recorded in the largest group - small entities. These conditions cause a strong negative impact on entrepreneurial initiatives in Macedonia which manifests as a change in the total number of newly established small firms. In 2013 the number of newly established companies and sole proprietors decreased by 3.4% compared to 2012. If we add an increasing number of companies which are under bankruptcy procedure, it can be concluded that the number of registered companies in this sector decline. According to data from the Central Register of the Republic of Macedonia, the number of legal entities with blocked accounts grows and in 2013 more than 31% of the total number of registered legal entities have their accounts blocked.

In the SME's business environment, consumers are a significant component which influences on the enterprises' financial capability. Because of their capacity for timely payment of their obligations the possibility of the funds release depend on the funds that are tied up in outstanding claims, as such does not bear any contribution. The weak liquidity position of SMEs is a result of the number of days that are needed for payment of their claims. An interview, conducted by me to more than 30 Macedonian companies, showed that these enterprises need more than four months to gather up their claims and even more for the payment of their obligations. This leads to the conclusion that the turnover of receivables is low because the companies are not able to effectively use funds for their basic activity.

In order to improve the payment of accounts receivable and payment of liabilities to suppliers the Law for financial discipline is incorporated in our country at the end of 2013. The main objective of this law is the timely fulfillment of monetary obligations and guidance to managers of companies to pay greater attention to the benefits of the application of techniques in managing receivables and inventories, managing cash flows and etc. This Law provided deadlines for fulfilling cash obligations between companies. Thus, the maximum contractual deadline for the fulfillment of obligations is 60 days and by a written agreement between the parties maximum 120 days. In the Law it is written that there is a right of the creditor in an untimely payment by the debtor to turn on a total of 50 euros. These provisions apply to all public enterprises and state institutions. The effects of the application of this law that began to be implemented from 01.01.2014 cannot yet be assessed realistically. If we consider the response of the surveyed enterprises consisting in incomplete solving the problem of monetary obligations, it can be concluded that the Law only delayed collection of receivables within the deadlines. The surveyed enterprises have complained about long deadlines as well as by the fact that they finance a purchase with their own money. The indicated conditions in the external environment of SMEs imply a need for application of financial management with strategic features that will take into account impact of the business environment into the financial decisions making.

Effects of Implementation of the Strategic Financial Planning for SMEs in Republic of Macedonia

3. Strategic Financial Management

According to Hitt, Ireland and Heskisson (2000), strategic management is a set of commitments, decisions and activities that are required for an enterprise to achieve competitive advantage and above-average profits. The strategic management process is based on three components: a strategic input elements, strategic activities and results. (Hitt, Ireland and Heskisson, 2000, p. 8). Strategic inputs are provided by the analysis of external and internal environment and they are necessary for strategic activities that addressed the formulation and implementation of strategic decisions. Strategic results are favorable strategic achievements of carefully formulated strategies and their implementation. Dynamic by its nature, the process of strategic management includes the following elements: scanning and monitoring of the environment, strategy formulation, strategy implementation, monitoring and evaluation. Companies use strategic management to create "clear feeling" about their vision and mission, which helps to determine the strategic orientation as precondition for strategic decision making.

Considering the fact that SMEs work in a variable environment, the use of strategic management helps them to understand the external and internal environment more easily. With this process, SMEs determines their vision, mission and strategic objectives, and strategic plans for a certain period of time. The strategic behavior of SMEs involving specific strategic tools such as analysis of opportunities and constraints in the external environment and analysis of the strengths and weaknesses in the internal environment of the company (the SWOT analysis). SMEs are characterized by flexibility that ensures adjustment to the environmental changing conditions and to the needs of shareholders. From this point of view, SMEs are forced to apply strategic management to ensure the necessary strategic flexibility that provides the ability to respond to multiple demands and opportunities in the dynamic and competitive environment in the sector of small and medium businesses.

In the transition economies, as the Macedonian, the introduction of market economic conditions has raised numerous problems and opened up issues pertaining to ways of managing the businesses. In the 90s of the last century, the scientific thought in the country was focused on research of the management practice, and in such framework on the strategic management of medium and large enterprises that have completed the privatization process. The results of these studies show that there are many problems that cause bad governance in the new market environment.

The survey implemented within the research project "Feasibility study for continuing management education" that was realized by the Faculty of Economics in Prilep, highlight the problems that managers are facing in SMEs. The research has shown that it is surprising how high the extent to which businesses lack a general perspective on strategic planning in the new market conditions. Most of the surveyed managers (60%) have stated that they plan budgets or develop annual financial plans based on the projected sales volume. Only 5% of managers surveyed said that they applied an integrated management approach, in terms of the range of external influences and internal skills and weaknesses of the company.

Foreign literature of this period underlines the need for greater adaptation of small firms to "High competitive uncertainty" (Careter, 1990). It is interesting that the previous survey identifies that managers showed insufficient competencies for strategic

management, explaining that in a dynamic and unstable economic conditions they refrain from planning and assessment of the future business situation and results.

In the last decade of the last century, in Macedonia the formation of small businesses is intensified and distinguished by specific features, such as: personal characteristics of the owners / managers of SMEs, ethical values, business experience, a specific competitive behavior, focus on the business environment and etc. Research has shown that the participation of SMEs in the total number of enterprises in Macedonia is as follows: (Stojanovska, 2014)

Table 1. Participation of SMEs in the total number of enterprises in Macedonia

Numbers of companies	2006	2007	2008	2009	2010
SMEs	49999	51064	53156	58288	61794
Over 250 employees	152	92	95	128	131
Total	50151	51156	53248	58416	61925

Source: Stojanovska, E (2014), “The importance of SMEs for reducing unemployment in the small and open economies - the case of Macedonia”, master's thesis, FAMIS, 2014. p. 179

Having in mind the vital importance of SMEs for the Macedonian economy, the SMEs are facing major challenges such as: insufficient “know – how” on strategic management, the absence of new technology, constant insolvency of SMEs, insufficient amount of capital to start up, high tax charges and other bureaucratic problems.

Financial problems are common to the majority of Macedonian SMEs. This problem arises primarily from delayed collection of receivables, from restrained lending to this sector by commercial banks, which is an important factor for improving the lower technological level and low investment in new technology. Despite the unfavorable banking conditions, however, most companies refer to commercial banks when they need additional funds, although banks are not the only ones available to companies. Namely, SMEs can come with the necessary funds through other alternative sources of funding, such as:

- An lease agreement
- Trade credits
- Factoring
- Issuance of shares
- Issuance of bonds
- A network of business angels and etc.

Data from the survey that is implemented over 119 companies from different countries by Kuntchev, Ramalho, Meza and Yang (2013, p.18) confirm the fact that SMEs are more likely to be credit constrained than large companies. Also, this study provides information that companies often use alternative modes of financing for working capital and fixed assets. They have classified the variety of external financing sources of fixed assets into four categories: equity finance, formal debt finance, trade finance, and informal source of credit. In all regions, in which the survey was conducted, the use of formal debt is relatively high, but much less SMEs use this type of financing than large firms. With the exception of South Asia, SMEs use trade credits and other informal sources to finance their activities.

Effects of Implementation of the Strategic Financial Plannig for SMEs in Republic of Macedonia

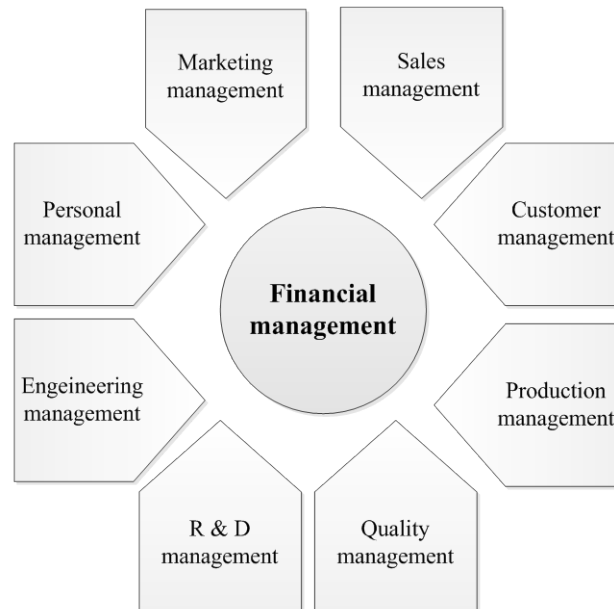
In research that we have conducted in 30 SMEs in the Republic of Macedonia, all companies stressed out that the main problems are insufficient amount of income or insufficient amount of funds from the sale of products and services. They have indicated that the difficulties in collection of trade receivables are the main reason for this problem. Despite the declaration that they regularly are planning the cash flows in the company, however, the effects of this lack.

This situation causes an inability to meet its commitments to creditors and employees. The main reason for this problem is restrained lending by commercial banks. The banks consider that the sector of small and medium businesses is still risky to finance due to their reduced ability to pay obligations and low capacity to absorb new debt. Also, the problem is the absence of knowledge of the owner for application of the strategic approach in the company's management and limited knowledge of finance and accounting. Owners of SMEs restrain from hiring experts in this area to reduce the high costs and so plaguing business and threaten the survival of businesses.

4. Financial Management of the SMEs

According to research by Nguyen (2001) financial management is one of the several functional areas of management, but it's key to the success of any small business. Figure 1 presents the central role of financial management in relation to other specific areas of business management.

Figure 1. The central position and role of financial management



Source: Nguyen, Minh. (2001), "Financial management and profitability of small and medium enterprises, DBA thesis, Southern Cross University, Lismore, NSW, p.68.

Meri Boshkoska

Lect. Ispas and Prof. Simion (2010, p.1) emphasize that the main objective of financial management consists in maximizing the value of the company. Financial management should answer the following questions:

- In which assets and projects the company should invest?
- What is the best form of financing such investments?
- How to implement the distribution of the profit?

The role of financial management is to provide methods and techniques by which an adequate analysis can be made and the most profitable investment can be chosen, and on the other hand to find the best way to finance investment.

The stated primary goal of financial management can be analyzed in more detail also in terms of: profitability and liquidity (Nguyen, M., 2001, p.70):

- Management of profitability means maintaining or increasing profit by monitoring the cost of capital, pricing and sales volume.
- The management of liquidity means that the company pays on time its obligations such as salaries, taxes, loans, etc. The adequate liquidity management minimizes inactive cash, which can be profitably invested.

Nguyen (2001, p.73) emphasizes that many researchers have a different approach in explaining the specific areas of financial management, but he summarized as follows:

- Current asset or working capital management
- Funding management
- Financial budgeting and planning
- Fixed asset or long-lived asset management
- Leverage and capital structure
- Financial analysis and evaluating performance of the business and
- Profit distribution.

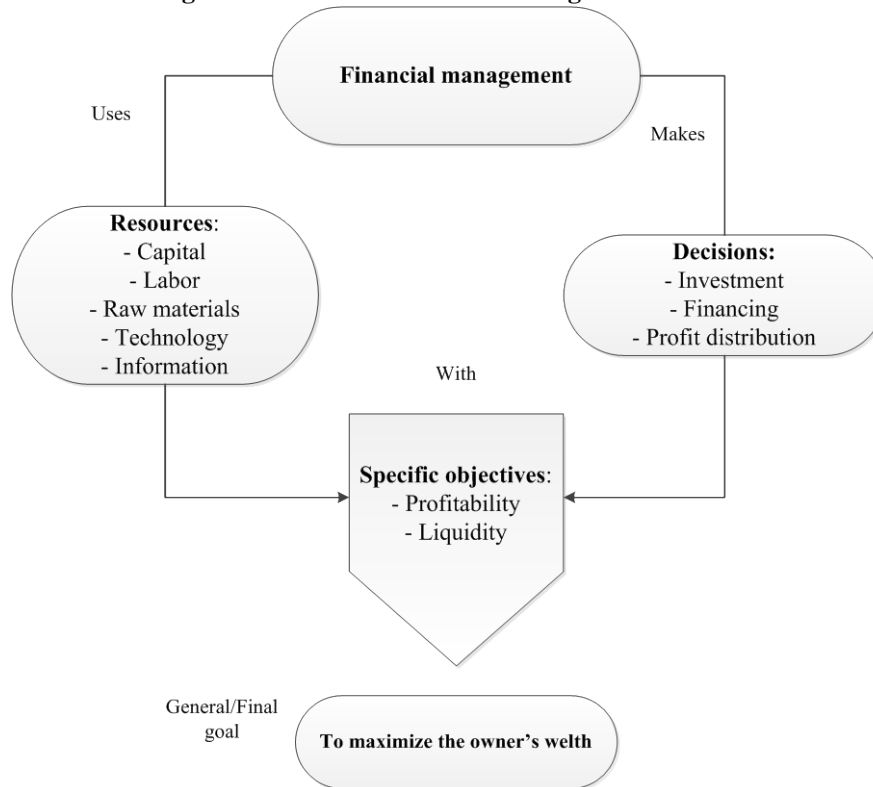
Figure 2 represents a model of financial management for small businesses in which the connection between the goals and decisions of financial management is presented.

From this model it can be concluded that management uses financial resources for making optimal decisions for investment, financing and distribution of profits in order to achieve profitability and liquidity of the company. The achievement of specific goals also means realization of the main objective of financial management - maximizing the company's value.

As outlined in the previous section, one of the key challenges for SMEs is managing the company's finances under conditions of an influential environment. The financial managers or managers/owners need knowledge and understanding of the relationship of strategic management and finance. Strategic Management provides inputs for formulation of strategic decisions (mission, vision, objectives and strategies) as follows: fiscal system of the country, the commercial banking system, monetary policy. Economic variables such as interest rate and taxes, inflation and deflation, employment, GDP and many others should be in the spotlight of financial managers and fit into the pattern of decision making in the financial area. (Block, S., Hirt, G., 2008, p.95).

**Effects of Implementation of the Strategic Financial Plannig for SMEs
in Republic of Macedonia**

Figure 2. A model of financial management



Source: Nguyen, Minh. (2001), “Financial management and profitability of small and medium enterprises, DBA thesis, Southern Cross University, Lismore, NSW, p.74.

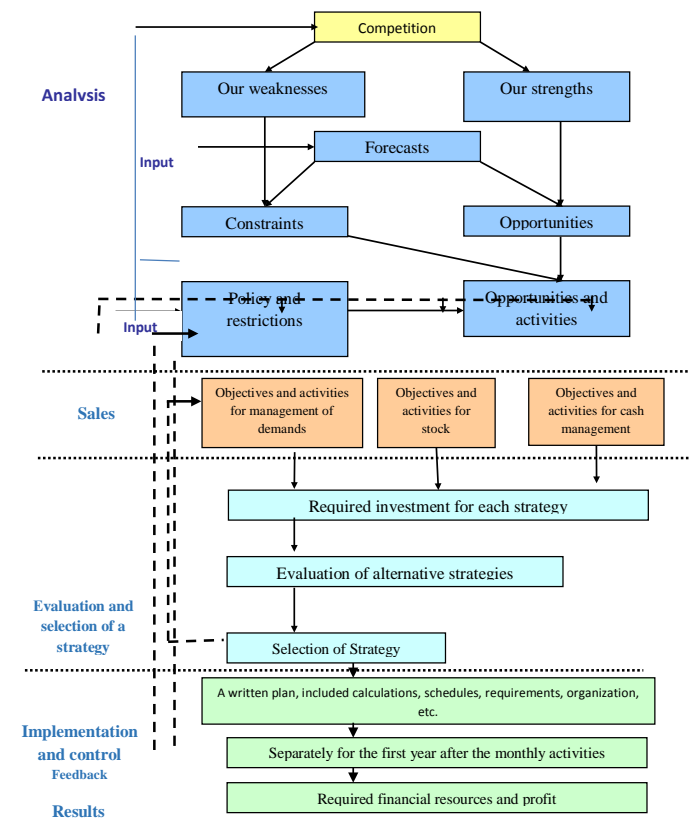
Nowadays managers/owners of SMEs make difficult decisions, such as which aims to choose and how to accomplish them, while combining the impact of external and internal environment over the process of strategic planning and decision making. In order to efficiently and effectively manage finances, they are responsible to provide funding through a selection of the best mix of alternative funding sources. In order to achieve the objectives the managers need to allocate the current and fixed assets in accordance with the profitability and risk of the company. (Panovska, Boshkoska, 2010, p.219)

Managing finances have been implemented, among other, by planning the future that is difficult, especially in the newly created environment after the change of the social system in Macedonia and frequent unpredictable political - legal and economic changes in the business environment. However, SMEs managed to get through this kind of difficulties thereby maintaining their importance for the Macedonian economy. In these strategic efforts, financial planning system that is presented below in the next section, could help for successfully addressing the dynamic and complex changes in the environment of SMEs.

5. System of Financial Planning with Strategic Approach

System of financial planning with strategic approach provides valuable information for financial managers. This system of financial management encourages strategic thinking about the developments of different business segments. The successful operation of the system depends on the relationship and cooperation between the management of marketing and finance that have responsibility to develop strategies the implementation of which will contribute to achieving the objectives of the company. Also, “know-how” and good practice in the field of finance is needed. In this regard, managers/ owners of SMEs should attend seminars and other forms of training. In this kind of training the elements of the financial planning with strategic approach are analyzed and the content and form of written action plans are explained. The system contains the strategic process stages, such as: analysis of external and internal environment, strategy formulation, strategy selection and implementation and evaluation of the results. The scheme of the financial planning with strategic approach is shown in Figure 3.

Figure 3. Scheme of the planning process: operational financial planning with strategic approach



Source: The scheme is taken and adjusted appropriately from: Panovska, V and Boshkoska, M (2010), *Planning and decision making*, Bitola: FAMIS, p.30)

Effects of Implementation of the Strategic Financial Planning for SMEs in Republic of Macedonia

As it can be seen from the system, it is externally oriented financial planning with a strategic approach that applies, above all, to short-term adjustment of the financial capacity of the company. Continuity in the functioning of the system is ensured by application of activities such as: analysis of customers and sales, evaluation of alternative strategies in the area of working capital, accounts receivable, cash flows and stock, selection of appropriate strategies for the segments of the working capital, the allocation of resources and developing a plan of undertaking appropriate action and control which allows implementation of selected strategies. The system provides detailed information that is quantitatively expressed and is related to the scope of the anticipated sale, the amount of the expected profit, the amount of necessary investments and etc. Thus defined future achievements include guidelines for dynamic management of working capital and for undertaking specific activities as well as answers to questions related to finance, such as: what, how, when, who?

The effects of strategic financial planning will be felt not only in the financial sector but, also in other sectors with which there is a direct financial connection. For this to occur, the planning system should be based on information obtained by previous development of a pro forma financial statements (income statement, balance sheet and cash budget). Based on the planned statements company may reconsider future volumes of working capital (accounts receivable, inventory, cash and liabilities, lending, credit terms, etc. (Block, S., Hirt, G., 2008, p.93).

Systematic approach of the financial planning effects, a predetermined plan of sale, specified plan of production with planned resources, estimated future costs and profits. Integrated planning of the sales and finance contributes to the determination of appropriate amounts of stock, real prediction of receivables and payables, and profit and cash flow will be within the company goal.

Such planning results will be realistic with the necessary know-how and commitment of responsible managers in SMEs, primarily by planning of the Financial Statements.

Based on the prediction of these reports guidelines are planned (goals, strategies and action plans) for managing segments of the working capital. Control of the implementation ways of previous decisions provides feedback on specific actions in the strategic planning process in order to achieve the intended results.

6. Conclusion

In terms of changing business environment success of SMEs depends, among other things, by the use of the strategic management process. With its use SMEs can easier and more efficient set their goals, mission and strategic plans. The system of financial planning with strategic approach helps financial managers in the implementation of strategic financial plans.

Through exploring the main purpose of our paper we can summarize up that strategic planning is a formal system where there is a precise schedule of activities covering the segments of key financial performance of the company. Strategic approach

in management helps in problem solving when SMEs attempts to adjust and adapt to dynamic business environment.

References

1. Block, S and Hirt, G (2008), *Foundations of financial management*, McGraw-Hill; 12 edition.
2. Hitt, M.A, Ireland, R.D and Heskisson, R.E (2000), “*Strategic management competition and globalization*”, South Western College, Tomson Learning.
3. Central Registry of Republic of Macedonia, <https://www.crm.com.mk/DS/> (5.3.2015)
4. Ispas, R., Simion, D (2010) The financial management of the Small and Medium Sized Companies in Romania, University of Craiova, Faculty of Economics and Business Administration, *Journal Annals of Computational Economics*, Vol.2, Issue 38.
5. Kuntchev, V, Ramalho, R, Rodreiguez-Meza, J. and Yang, Judy (2013), What Have We Learned from the Enterprise Surveys Regarding Access to Credit By SMEs?, *World Bank Policy Research Working Paper No. 6670: 1-37*.
6. Law on financial discipline, Official Gazette of the Republic Macedonia, No. 187, 12.30.2013, Skopje.
7. NBRM (2014), Извештај за финансиската стабилност на Р.М за 2013 година, Skopje, Republic of Macedonia.
8. Nguyen, Minh. (2001), Financial management and profitability of small and medium enterprises, DBA thesis, Southern Cross University, Lismore, NSW.
9. Panovska, V and Boshkoska, M (2010), *Planning and decision making*, Bitola: FAMIS.
10. Stojanovska, E (2014), “The importance of SMEs for reducing unemployment in the small and open economies - the case of Macedonia”, master's thesis, FAMIS, 2014.
11. Tempus Phare Programme (1997/98), “Feasibility study for continuing management education”, Faculty of Economics – Prilep.