DETERMINANTS OF FINANCIAL LITERACY OF MICRO ENTREPRENEURS IN DAVAO CITY

William T. Sucuahi
College of Accounting Education, University of Mindanao
Davao City, Philippines

Abstract

The study determined the financial literacy of the selected micro entrepreneurs in Davao City. A total of 100 micro-entrepreneurs participated in the study. On the whole, the level of financial literacy of the micro-entrepreneurs were moderate indicating a not so impressive financial management of their resource. To obtain the determinants of financial literacy, multiple regression analysis was employed which revealed a significant influence of educational attainment on the financial literacy. The result however showed that gender cannot predict the financial literacy level among micro entrepreneurs.

Keywords: Financial Literacy, Micro Entrepreneurs, Descriptive, Philippines

1. INTRODUCTION

Various research has long highlighted the importance of financial literacy in developing persons towards financial stability. In fact, a lot of studies were conducted to determine the financial literacy of different individuals. Previous studies focus determines the financial literacy among students (Borodich, Deplazes, Kardash, & Kovzik, 2010), stock market investors (Rooj, Lusardi & Alessie, 2007), employees (Fornero & Monticone, 2011) and general population (Plakalovic, N., 2012). These studies explore the financial literacy of micro entrepreneurs and determine what explains the variation on the level of their financial literacy.

Micro enterprises contributed significantly in the economic development because these types of enterprises create a bridge between a margin of purchase ability of the greater number of the population and the affordability of the products made available to the consuming public. Frempong (2009) even highlighted the important characteristic role of the micro-entrepreneurs as a provider of affordable goods and services for the public and at the same time creating a large proportion of jobs. Given that the micro entrepreneurs have significantly shaped the economic activity in the countryside, a low financial skill might lead into an adverse impact in the future of the business.

This significant role of the micro-enterprises can be well-harnessed and sustained through a fine and precise financial management of the entrepreneurs themselves. Brown, Berman, Saunders & Beresford (2006) subscribed to the general principle of good business through financial literacy. Good business leads to competitiveness in the globalized community (Borodich et al., 2010). Lack or no financial literacy, as Niederauer (2010) cautioned, would lead to shut down of the business. Thus, a good financial foundation of the entrepreneurs is also a significant barometer of the success and growth of the enterprises in a competitive business environment.

1.1 Micro entrepreneurs and financial literacy

No less than Greenspan (2002) described the means to acquire assets which include home ownership, savings and micro entrepreneurship particularly. Micro entrepreneurship has gained global prominence while shapes local economies.

Although with woofing contribution to the economy, the micro entrepreneurs are still beset with the troubles of financial management. The strategies employed to address this concern are incorporating entrepreneurship in the formal educational programs (Klein, Evans and Todd, 2009), intensive training on financial literacy (Bates and Servon, 1998) in order to make individuals arrived at informed judgments on the use of money to become more informed consumers, producers and investors (Jacob, 2002)

The cost of lack of financial literacy leads to financial indecisiveness (Lusardi, 2009), and is commonly found among women with low education (Lusardi, 2008). Indicatively, a low financial management would lead to problematic cases (Bell and Lerman, 2005) like spending beyond regular means.

1.2 Measuring financial literacy

Financial literacy topics such as record keeping, budgeting, personal finance and savings were viewed to be more important to lower-income individuals. This suggests that financial educators should not only teach how to save or ways to save, but also the why's to save (Rhine and Comeau, 2000). In this study the researcher used these four topics to measure the financial literacy of micro entrepreneurs.

Record keeping is a fundamental skill a business person must possess. It is the source of important information vital to critical decision-making, and responsible for minimizing risks (Gray, Sebstad, Cohen and Stack, 2009). This measure of financial literacy suggests the effective record systems considered to be critical in business operation since business owners cannot rely on their memory to summarize all transactions of the day.

Savings is another component which serves as economic security (Braunsten and Welch, 2002) and also for accumulation of wealth (Gokhale, 2000) for an improved living standard. However, micro entrepreneurs are lack of necessary discipline and willingness in advancing their business skill including saving ethics (Karides, 2005).

The financing skill, the third measure of financial literacy, is the ability to obtain capital from outside sources with minimal cost and payoff obligation. Interestingly, Assibey (2010) found out that most micro entrepreneurs are illiterate with respect to business financing. Without knowing that their obligation is getting bigger because of interest and high debts will lead to business reversal (Worthington, 2004).

Budgeting, on the other hand, refers to the expenditure planning and cash flow analysis (Uddin, Chowdhury and Zakir, 2009) which is very important to the success of the business operation and processes (Bragg and Burton, 2006). However, Torres (2008) found that small business owners are not concerned about budgeting; their concern is more of the cash flow.

Quite interestingly, financial literacy differs between men and women; males are more knowledgeable financially than females (Al Tamimi and Kalli, 2009). Also, those who have low financial literacy have low education (Lusardi, 2008).

2. METHOD

A total of 100 micro entrepreneurs in Davao City was randomly selected. These micro entrepreneurs are owners of the small “sari-sari store” (*makeshift, variety store)*, beauty salon, fish vendors, eatery, and auto repair shop owners.

The respondents were given a survey questionnaire that takes 5-point Likert type (Always, Often, Sometimes, Seldom and Never).

A regression technique was employed in determining the financial literacy of the entrepreneurs. The financial literacy was taken as the dependent variable and the sex (male or female) and the education of the respondents were used as explanatory variables.

The equation is thus given as $y = \beta_0 + \beta_1 sex_i + \beta_2 educ_i + \varepsilon_i$ where y is the level of financial literacy, β_s as the parameters, sex which is multichotomouslue (male or female), and $educ$ as the educational attainment which takes multichotomous values (high school, college level, and college graduate).

3. RESULT AND DISCUSSION

Presented in table 1 is the descriptive statistics of the profile of the respondents. It was found that there were more female entrepreneurs (65 percent) compared to males (35 percent). It could be readily explained that a greater number of females are engaged in enterprising works than males who are doing regular jobs. With their current occupation as household managers rearing the children while taking time for entrepreneurial activities would lead into a trade-off between family support and entrepreneurial focus. Enterprise engagements of the female entrepreneurs would be limited, and the focus shall be beamed on the cash flow management as the Torres (2008) study described as meat and mean.

Table 1 Profile of respondents

Sex	Frequency	%
Female	65	65
Male	35	35
Total	100	100

Table 2 presented the educational attainment of the respondents. It was found that a majority of the micro entrepreneurs were in the college students or at least in college level. A previous study found out a similar characteristic between businessman and college students that is why college students today are expected to have an entrepreneurial mindset (Kauffman Foundation, 2009).

Table 2 Educational Attainment

Education	Frequency	%
High School Graduate	29	29
College Level	39	39
College Graduate	32	32
Total	100	100

Table 3 displays the summary of the level of financial literacy of micro entrepreneurs. The result revealed that majority of the micro entrepreneurs is not financially literate (*mean* = 3.06). The lack of financial education could be one of the factor (Anthes, 2004). The other reason might time constraint. Since business requires their presence always they might not be able to acquire the necessary financial education.

Table 3 Summary in the Level of Financial Literacy of Micro Entrepreneurs

Item	Min	Max	Mean	Std. Dev.
Record Keeping	1.00	5.00	3.10	1.16
Saving	1.00	4.60	3.02	0.82
Financing	1.00	5.00	3.13	1.07
Budgeting	1.00	5.00	3.00	1.09
Overall	1.00	4.75	3.06	0.82

Table 3 also shows the mean score of the four financial literacy indicators. Micro entrepreneurs financial literacy is consistently moderate in terms of record keeping (*mean*=3.10), saving (*mean*=3.02), financing (*mean*=3.13) and budgeting (*mean*=3.00). Further discussion on these results will be discussed below:

3.1 Record Keeping

Business owners had recorded all revenues and expenditures based on the documents gathered during interview. However, majority of the respondents were still using notebooks and piece of paper in recording their business transactions. The used of appropriate book of accounts such as journals and ledgers was not observed all the time during collection of data. Rutherford, McMullen and Oswald (2001) explained that it is possible that the small business owner keep records, but not in a formal manner.

In addition, separation of business records from personal records was slightly observed. The separation of these two records will help the business owners split business profit from personal profit. On the other hand, majority of respondent did not summarize their records. This task helps them be aware of the result of their business transaction.

3.2 Savings

Micro entrepreneurs are quite literate in monitoring their sales over the expenditure most of the time. They understand that in order to save they should have surplus at least. However, the respondents were not consistently set aside funds for future expenses. It was not manifested all the time that they were planning to have a ready money for their unexpected expenses through savings.

It was also found out that majority of the business owners did not deposit their extra money in the bank or invest in cooperative this is because they are not setting a target percentage out of their surplus in savings. What they knew is whatever money they have after deducting all personal expenses that will be the savings for them. Jacob, Hudson and Bush (2000) emphasized that many lower-income persons are capable and have desire to save but have trouble in doing so for purely economic reasons.

Majority of the micro entrepreneurs are not considering investing into other business opportunity using their savings. They would rather use other source of fund such as loan than to use their extra money. According to Karides (2005) micro entrepreneurs must invest out of their income for things is not permanent.

3.3 Financing

Micro entrepreneurs are highly literate in paying their loan balance on time. They are aware about the consequence in not paying the loan. They knew that not paying on time will result in paying penalties and other surcharges.

However, micro entrepreneurs are not much literate in separating the payment of their business loans from personal loan using their business money. Accounting principles assert that business transaction should be separated from the owner's transaction and this principle is fundamental and it applies to all types of organization.

It was also noted that majority of the business owners prefer to borrow short-term loan from Indian national lender than to borrow from financial institution such as banks, lending companies and credit card companies. This finding supports the observation of Leiber (2010) that only 20 percent of the short-term credit for the small businesses comes from the bank. In relation with this, the result also shows that business owners are not much concern on interest rate. They are more concern about the approval of the loan.

3.4 Budgeting

With respect to controlling their business spending micro entrepreneurs are moderately literate. They were not consistent in planning about when to spend and what to spend in their business. Literacy on making written plan for the next month sales and business spending were both moderate. This means that business owners sometime make a written budget and sometimes not at all. These written plans are important for monitoring purposes but were not able to do this on regular basis. The budgets were also not regularly monitored.

In terms of financial budgeting, the financial literacy of micro entrepreneurs was not manifested all the time. One of the evidence is the respondents were not computing the payback period for their capital expenditure.

Based on the findings above, business owners are not prepared to manage their business properly. Jacob (2002) found that acquiring financial knowledge is a critical financial management tool. It is a tool for ensuring that not only the privileged few have the knowledge and ability to effectively build assets, manage their debt, and avoid being misled, exploited or cheated by the plethora of aggressively marketed financial products that are now available. However, acquiring these business skills is less important to them based on the result. What they know about business is purely selling their products. Other factors are not important as long as consumers will buy their products.

3.5 Determinants of financial literacy

Presented in Table 4 is the parameter estimate of the model using the ordinary least squares estimate in doing regression analysis. Two variables was use in predicting the financial literacy of micro entrepreneurs.

Table 4 Financial literacy determinants

Variable	*B*	*Std.*	*t-value*	*p-value*

		Error		
Gender	-0.188	0.164	-1.142	0.256
Educational Attainment	4.03	0.097	4.131	0.00

The result shows women have lower level of financial literacy than male (*B* = -0.188). However, the difference is not significant with *p-value* of 0.256 which is higher than the significant level of 0.05. This means that gender cannot predict the financial literacy level of micro entrepreneurs. This finding did not support previous studies (Al Tamimi and Kalli, 2009; Lusardi, 2008).

The educational attainment is significantly related to its level of financial literacy (*p-value* = 0.00). The result explained that micro entrepreneurs with at least college level have higher financial literacy than of the lower education. Hence, it affirms the theory of Lusardi (2008) that financial illiteracy is widespread people who have low education.

4. CONCLUSION

The study was able to determine the strengths of the micro-entrepreneurs in sustaining their businesses. Although as a whole, the entrepreneurs were not sophisticated in record-keeping, saving, financing and budgeting; they were as well not unpolished in utilizing their skills.

It was found also, using regression analysis that education is a factor that would increase financial superiority of the entrepreneurs but not with their gender.

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