International Journal of Education and Evaluation (IJEE) E-ISSN 2489-0073 P-ISSN 2695-1940
Vol 9. No. 6 2023 www.iiardjournals.org

Effect of Risk Assessment Practices on the Financial Performance of Small and Medium Scale Enterprises (SMES) in Anambra State

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DOI: 10.56201/ijee.v9.no6.2023.pg41.50

Abstract

The study sought to ascertain the influence of risk assessment procedures on the financial performance of Anambra State's small and medium-sized companies (SMEs). Two research questions were developed, and one hypothesis was evaluated at a 0.05 level of significance. A correlational design was used in the study. The study's population included 2,895 managers of SMEs in Anambra State. A stratified sampling strategy was used to pick the sample. Thirty percent of small and medium-sized entrepreneurs were picked at random from each stratum, yielding an 868-person sample size. Three experts validated the two questionnaires used to gather data. A pilot test was done on 20 managers of SMEs in Enugu State to examine the dependability of the instruments. The Cronbach Alpha reliability technique was used, and the total reliability coefficient for internal consistency was 0.82, suggesting that the study was reliable. The Cronbach Alpha reliability technique was used to assess the data for each instrument cluster, providing values of 0.78 and 0.85 for clusters 1 and 2, respectively. Pearson's Product Moment Correlation and Multiple Regression were used to analyze the data. According to the findings, risk identification and risk analysis have a beneficial impact on the financial performance of SMEs in Anambra State. Furthermore, a substantial association was discovered between risk assessment techniques and the financial success of the state's SMEs. Based on these findings, several recommendations were made, including the suggestion that top management of SMEs should develop a risk assessment framework tailored to their business size, type, and financial capacity

***Keywords**: Risk Assessment, Risk Analysis, Risk Identification, SMEs, Financial Performance*

Introduction

The economic growth and development of a country depend on the ability of its small and medium-sized businesses to thrive. This idea has led to the recognition that Small and Medium-Scale Enterprises (SMEs) are the backbone of the economy. According to Gbandi and Amissah (2014), small and medium-sized firms play a crucial role in driving economic development in both developed and developing nations. SMEs are known for their dedication to innovation and their potential to stimulate growth. In an economy, SMEs perform various functions, such as creating jobs, promoting rural development, empowering youth, contributing to national income and growth, facilitating the spread and development of adaptive technology, and fostering balanced regional growth.

In recent years, SMEs have emerged as the key source of job creation in Nigeria, notably in Anambra State. SMEs account for roughly 97% of all firms in Nigeria and provide an average of 50% to employment and industrial production (Abubakar, Imran, & Abba, 2020). SMEs have become identified with the local populace in Anambra State. The people of Anambra State are known for their love of commerce and entrepreneurship, as seen by the large number of small and medium-sized businesses distributed throughout the state's rural and urban districts. The existence of these SMEs has not only boosted economic activity but has also increased the state's income base. As Mikugi and Baguda (2021) point out, this is precisely why SMEs are seen as the driving force behind economic growth and technical innovation.

Micro, Small, and Medium Enterprises (MSMEs) in Nigeria get little attention and assistance, despite their critical role in the country's economic growth. Despite the good economic conditions, this lack of concentration is evident in the minimal contributions of these firms to Anambra State's production base. SMEs in Anambra State suffer a variety of internal and global economic concerns, including uneven government policies and poor company risk management. As a result, business development is constrained, there is a high risk of business failure, and there is a considerable death rate among SMEs, resulting in worker layoffs and increasing unemployment. These data corroborate Okoli and Okeke's (2019) discovery that Anambra State has one of the highest unemployment rates in the South East Zone, at 21.3%, above the national average of 21.1%. According to Okoli and Okeke's research, these businesses have failed to meet their goals of creating jobs and money. This circumstance exemplifies Anambra State's SMEs' low financial performance.

Certain criteria are essential for a company's success, according to Gorgievski, Ascalon, and Stephan (2011). Profit, growth, and innovation, according to Gorgievski, Ascalon, and Stephan, are the top three key criteria for SMEs. These variables are most likely associated to wealth increase. Growth and profitability are the two most widely cited performance measures in the entrepreneurship and small business literature, according to Gorgievski, Ascalon, and Stephan (2011). According to Stoner in Mbuva, Rambo, and Oketch (2018), financial success is the ability to maintain operational effectiveness, profit creation, and positive changes in SME growth, as well as continuous responsiveness to opportunities and threats in the immediate environment. This can be seen in the sales growth rate, cash flows, returns associated with a common stock investment, the profit margin in gross terms, the profit margin in net terms, the net profit to revenue coefficient, the returns to total investment ratio, and the ability to facilitate project growth (Mbuva et al, 2018). According to Mbuva et al, the financial performance of SMEs is dependent on their ability to recognize risk efficiently.

Risk is the possibility of injury or any other adverse occurrence brought on by vulnerabilities on the inside or outside; it may be prevented by adopting preventative actions. Risk and uncertainty are usually associated since the occurrence may or may not happen (Okoli & Okeke, 2019). It is a key aspect of business since enterprises cannot function without taking risks, and enterprises grow by taking risks. Risk is related to opportunities and risks that might adversely affect a course of action or anticipated result. The term "risk assessment" refers to the entire process of identifying hazards and risk factors that could potentially cause harm (hazard identification); analyzing and evaluating the risk connected to that hazard (risk analysis, and risk evaluation); and selecting the most appropriate measures to eliminate the hazard or control the risk in cases where the hazard cannot be eliminated (risk control) (Mbuva, et al., 2018). In a similar vein, Heldman (2010) suggested in Boubala that risk assessment should pay particular attention to the following five areas: Identifying and documenting risks; evaluating and classifying risks; managing risks; maintaining risk management and putting controls in place; and performing risk evaluations and audits.

Risk assessment is the process of analyzing factors that might potentially hinder the accomplishment of SME objectives. Risk assessment is based on whether organizational goals and objectives are accomplished. SMES are able to actively investigate all relevant risks that they are exposed to thanks to the risk assessment process (Iopev & Kwanum, 2012). Smit and Watkins (2012) stated that SMEs are better equipped to maximize their resources by incorporating risk assessment into SME operations, enabling firms to transform an expensive activity into an activity that may produce a positive return. However, among SMEs in Anambra State, there is no actual data to back up this claim. This study, therefore, intends to ascertain the effect of risk assessment practices on the financial performance of small and medium-scale enterprises in Anambra State.

Statement of the Problem

The majority of small enterprises fail within a short period of time, despite the government's and other stakeholders' attempts to encourage sustainable SMEs as a method of attaining economic growth and development. According to Utomi in Ifekwem, Oghojafor, and Kuye (2011), few early wealthy families (SME entrepreneurs) have been able to maintain the family business for a lengthy period of time. According to Utomi, a lot of the ventures have failed as a result of handing over business management to a family member who is unable of doing an in-depth assessment of business risk. This problem affects the majority of SMEs in Nigeria, particularly those in the state of Anambra. This is the outcome of SME owners' and management's dissatisfaction with the methods used to evaluate business risk.

A prevalent characteristic of SMEs in Anambra State appears to be a lack of funding. Due to their modest size and weak financial foundation, SMEs struggle to compete successfully with large enterprises. These generally put businesses in adverse strategic situations since they lack the financial backing needed to withstand such competition, which includes skilled and experienced individuals, adequate competence, funds, and additional resources for survival. These lessen the company's chances of survival and raise its sensitivity to serious risks.

The problem with this study is that certain managers of small and medium-sized businesses in the state of Anambra are dealing with a deluge of financial issues and responsibilities. These issues and liabilities have limited the ability of SMEs' in the State to boost development, decrease poverty, produce wealth, and create jobs. Although the primary reasons for their failure do not appear to be clearly demonstrated, actual observations show that managers of small and medium-sized firms do not appear to be sufficiently using acceptable risk assessment techniques in their company operations. The extent to which this is true, however, can only be determined by an empirical investigation, as the researcher intended.

Purpose of the Study

The main purpose of the study was to determine the effect of risk assessment practices on the financial performance of SMEs in Anambra State. Specifically, the study ascertained:

1. The correlation between risk identification practices and the financial performance of small and medium scale enterprises in Anambra State.
2. The correlation between risk identification practices and the financial performance of small and medium scale enterprises in Anambra State.

Research Questions

The following research questions guided the study

1. What is the correlation between risk identification practices and the financial performance of small and medium-scale enterprises in Anambra State?
2. What is the correlation between risk analysis practices and the financial performance of small and medium-scale enterprises in Anambra State?

Hypothesis

The hypothesis was tested at a 0.05 level of significance:

H_o: There is no significant correlation between risk assessment practices and the financial performance of SMEs in Anambra State.

Conceptual Framework

Independent Variable **Dependent Variable**

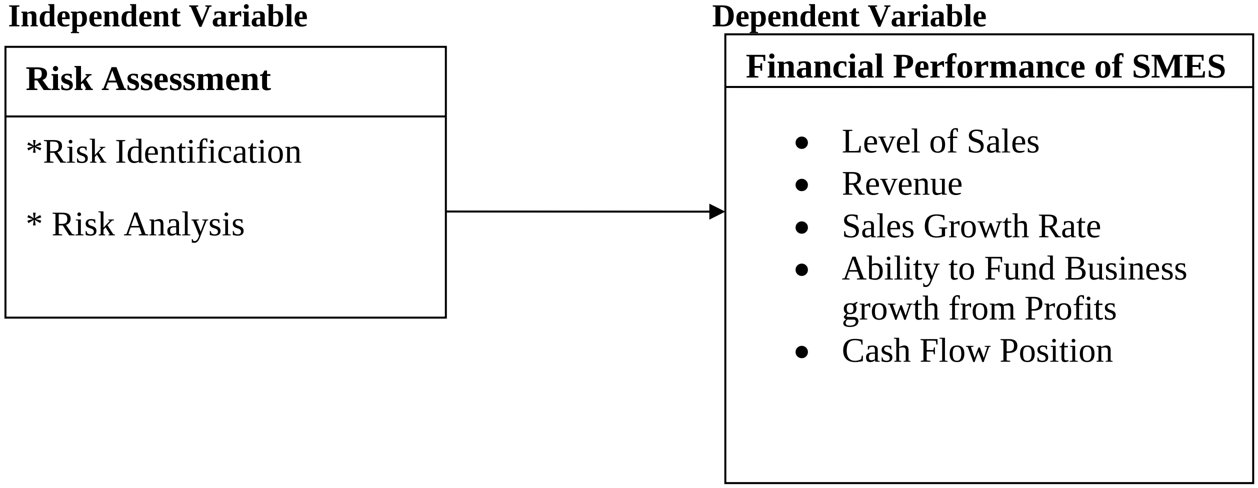

Figure 1: Conceptual Framework for the Relationship between risk assessment and Financial Performance of SMEs

Theoretical Underpinning

Agency theory

Agency theory was first proposed by Smith and Stulz in 1985. It claims that an agency relationship is established when individuals or groups (referred to as principals) hire another person (referred to as the agent) to do a task on their behalf. In this system, the agent has decision-making authority. An agency relationship is commonly represented as the relationship between an employer and an employee. An organization (principal) and a lobbyist (agent), a state (principal) and its ambassador (agent), constituents (principal) and their elected representative (agent), shareholders (principal) and a CEO are some further instances. Managers' views regarding taking risk and hedging in the field of managing risks have been seen to be impacted by agency issues. The agency theory is relevant to the present study because it shows the effect of the financial structures of a firm on the propensity to which it adopts risk assessment practices. This theory will help the researcher understand the effect of risk assessment practices on the financial performance of SMEs in Anambra State.

Empirical Studies

Mikugi and Bagudu (2021) examined a framework of risk analysis and the performance of small and medium enterprises. The methodology adopted was through conceptual analysis and literature review. Relevant books and journals on risk, risk identification, assessment and management were used for findings. The study revealed that the extent of efforts required for risk management depends on the complexity of the operational activities and the scale of the business, therefore risk management for a business of any size relates to systematic assessment and strategic response to threats. The paper suggested that there is a need for proper risk analysis by SMEs to achieve better risk management and business performance. SMEs should put in place measures for timely risk identification and effective risk mitigation to ensure that their financial performance is not impacted negatively. Risk management frameworks such as Enterprise Risk Management which conform to international best practice should be put in place by SME owners.

Okoli and Okeke (2019) ascertained the extent owners of Small and Medium Enterprises adopt suitable risk management practices for institutional collaborations for business success in Anambra state. The descriptive survey design was adopted for the study. The population comprised 2502 owners of SMEs registered with Anambra State Ministry of Commerce, Industry and Technology. A sample of 750 owners was drawn through a stratified random sampling technique. One research question guided the study and one null hypothesis was tested at a 0.05 level of significance. A validated structured questionnaire with a reliability coefficient of 0.76 was used to collect data for the study. Mean and standard deviation were used to answer the research questions while ANOVA was used to test the null hypothesis. The findings of the study revealed that the adoption of suitable risk management practices for business success was low among owners of SMEs in Anambra state. The findings further revealed that years of experience of the SME owners did not significantly affect their mean ratings on the extent they adopt suitable risk management practices in their businesses. It was concluded that there was a need for collaborations between the Association of Owners of SMEs and higher educational institutions through training for the acquisition of skills on the identified risk management practices that were not suitably adopted by owners of SMEs in their businesses for success. It was recommended among others that governments at all levels should make training on risk management practices in the electronic world compulsory among owners of SMEs through workshops, seminars and conferences; and as a requisite for the provision and approval of loans to SMEs. This is to ensure the effective use of resources provided for success of their businesses.

Mbuva, Rambo and Oketch (2018) determine the extent to which risk assessment influences the performance of SME projects in Machakos County. The study applied a pragmatism philosophical approach and descriptive survey research design. It tested the hypothesis at a 95% confidence level which stated that risk assessment does not significantly influence the performance of small and medium enterprise projects in Machakos County. The study used a multiple regression model against a sample size of 265 selected from a population of 5311 small and medium enterprise projects in Machakos County using a stratified and convenience sampling approach as guided by the Yamane (1967) formula. A structured questionnaire was used to collect data whereby drop and pick approach was used. The study finding revealed that the majority of the risk assessment components were positively supported by the respondents and their response mean was above 3.50, the composite mean. Inferential statistics depicted that risk identification, prioritization and managing change significantly influenced financial performance with β=.102(p=0.016) and β=.092(p=0.012) respectively whereas organizational goals and objectives had insignificant influence with β=.031(p=0.366). Further, risk identification and prioritization significantly influenced non-financial performance with β=.104(p=0.017) whereas organizational goals and objectives and managing change had insignificant influence with β=.020(p=0.574) and β=.054(p=0.184) respectively. Management of SME projects should ensure the significant contribution by risk identification and prioritization towards performance, in general, is upheld with further endeavours to improve on the risk assessment components which have an insignificant impact on performance.

Methodology

The design adopted in this study was the correlational design. The study was carried out in Anambra State of Nigeria. The population of the study comprised 2895 managers of small and medium-scale enterprises in Anambra State who were registered with the State Ministry of Commerce, Industry and Technology as of January 2022. The sample was drawn from 2895 registered SMEs in Anambra State using stratified random sampling. In the process, four strata were formed based on types of business activities (Agro-allied, General Business Services, Manufacturing and Construction). Thirty per cent of each of small and medium-scale entrepreneurs were drawn through randomization from each stratum. Thus, the sample of the study comprised 868 small-scale enterprise managers. Two instruments were used to collect data for the study. The first instrument is titled "Risk Assessment Practices Questionnaire (RAPQ)," it contains 18 item statements spread over two sections, A and B. Section A contains 10 items on risk identification practices while Section B contains 8 items on Risk Analysis Practices. The second instrument is titled "Financial Performance of Small and Medium Scale Enterprises Questionnaire (FPSMSEQ)." The questionnaire contains 6 items on the financial performance of SMEs. The instruments were validated by three experts in the Department of Accounting, Chukwuemeka Odumegwu Ojukwu University, Igbariam.

A trial test was conducted on 20 managers of SMEs in Enugu State. The application of the Cronbach Alpha reliability method on the obtained data yielded a general reliability coefficient of 0.82 for internal consistency which was deemed reliable for the study. Since the instrument is in clusters, the researcher again applied the Cronbach Alpha reliability method in analyzing the data for each cluster. This yielded coefficient values of 0.78 and 0.85 for clusters 1 and 2 respectively.

The researcher administered copies of the instrument personally with the aid of six research assistants who were briefed by the researcher on the purpose of the research, the response pattern and the subject of the study. Direct delivery and retrieval method was employed in the administration of the instrument to minimize wastage and achieve a high return rate. Out of the 876 copies of the questionnaire administered, 682 were properly filled and successfully retrieved. These 682 copies which represent an overall return rate of 78% were deemed adequate for the study and thus used for data analysis. Pearson Product Moment Correlation was used to answer research questions. The coefficient "r" obtained was used to ascertain how each of the independent variables correlates with the dependent variable. Similarly, multiple regression was used to test the hypothesis. Multiple regression was used to ascertain the interactive relationship among the variables of interest and also to determine the r^2 and adjusted r^2.

Results

Research Question 1

What is the correlation between risk identification practices and the financial performance of small and medium-scale enterprises in Anambra State?

Table 1: Pearson's Correlation between Risk Identification Practices and Financial Performance of SMEs

Variables	N	Risk Identification	Financial Performance of SMEs	Decision
Risk Identification	682	1	.710**	High Positive Correlation
Financial Performance of SMEs	682	.710**	1	

According to data in Table 1, Pearson's correlation coefficient is r = 0.71. This demonstrates that risk identification procedures and the financial success of small and medium-sized businesses in Anambra State are highly positively correlated. This suggests that SMEs' financial performance would improve if they used risk detection procedures. As a result, risk detection procedures and the financial success of small and medium-sized businesses in Anambra State have a strong positive link.

Research Question 2

What is the correlation between risk analysis practices and the financial performance of small and medium-scale enterprises in Anambra State?

Table 2: Pearson's Correlation between Risk Analysis Practices and the Financial Performance of SMEs

Variables	N	Risk Analysis	Financial Performance of SMEs	Decision
Risk Analysis	682	1	.820**	High Positive Correlation
Financial Performance of SMEs	682	.820**	1	

According to data in Table 2, Pearson's correlation coefficient is r = 0.82. This demonstrates that risk analysis procedures and the financial success of small and medium-sized businesses in Anambra State are highly positively correlated. This suggests that SMEs' financial performance would improve if they used risk analysis procedures. As a result, there is a strong positive association between the use of risk analysis and the financial success of small and medium-sized businesses in Anambra State.

Hypothesis

H_o: There is no significant correlation between risk assessment practices and the financial performance of SMEs in Anambra State.

Table 3: Summary of Regression Analysis on the Correlation between Risk Assessment Practices and the Financial Performance of SMEs

	R	R Square	F	p-value	Decision
Model	.791[a]	0.556	7.82	0.00	Significant

Predictors: (Constant), Risk Identification and Risk Analysis

Dependents: Financial Performance of SMEs

Data in Table 3 The result of the analysis of variance shows that the F-value of 7.82. The p-value of 0.000 is less than the alpha value of 0.05. This means that there is a significant correlation between risk assessment practices (risk identification and risk analysis) and the financial performance of small and medium-scale enterprises in Anambra State. There, the null hypothesis was rejected.

Discussion

Results showed a positive relationship between risk identification procedures and the financial success of small and medium-sized businesses in Anambra State. This result suggests that SMEs would see growth in their company operations if they use meticulous risk detection techniques. This is in line with the findings of Mbuva, Rambo, and Oketch (2018), who claimed that risk identification procedures had a big impact on SMEs' financial performance. According to Okoli and Okeke (2019), risk identification techniques are a crucial part of risk management practices that have a big influence on the financial performance of SMEs

Additionally, research results showed that risk analysis procedures have a big impact on how well small and medium-sized businesses in Anambra State do financially. This result suggests that applying risk analysis techniques will greatly enhance SMEs' financial performance. This is in line with Mikugi and Bagudu's (2021) research, which said that enhancing the financial performance of SMEs requires risk analysis as a crucial element of risk management. Further, Mikugi and Bagudu recommended that SMEs use strategies for prompt risk assessment and efficient risk mitigation to protect their financial performance. In the same vein, Mbuva, et al (2018) noted that management of SME projects should ensure the significant contribution by risk identification and prioritization towards performance, in general, is upheld with further endeavours to improve on the risk assessment components which have an insignificant impact on performance. Further findings revealed that there is a significant correlation between risk assessment practices and the financial performance of SMEs in Anambra State. This is in agreement with the findings of Okoli and Okeke (2019) and Mbuva, et al (2018) who found that there is a significant correlation between risk assessment practices and the financial performance of SMEs in Anambra State.

Conclusion

The researcher concludes based on the findings of the study that risk assessment practices positively influence the financial performance of SMEs in Anambra State. The application of sound risk assessment practices like risk identification and risk analysis would positively influence the financial performance of SMEs. It is therefore expedient that managers of SMEs take into consideration the potential of the adoption of risk assessment on their business financial performance.

Recommendations

The researcher makes the following recommendations based on the findings of the study:

1. Top management of SMEs should ensure that they map out a risk assessment framework that would suit their business size, type and financial capacity.
2. Managers of SMEs should ensure that they conduct periodic risk identification in their businesses to determine risk inherent and external to their business survival.
3. Risk analysts should be invited to determine the types of risks the business is exposed to and the measures for controlling the risks.

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