INTERVENING EFFECT OF FINANCIAL MANAGEMENT ON THE RELATIONSHIP BETWEEN CAPITAL STRUCTURE AND PERFORMANCE OF SMALL AND MEDIUM SCALE ENTERPRISES IN BENUE STATE, NIGERIA.

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Abstract

The main objective of the study was to investigate the intervening effect of financial management on the relationship between capital structure and firm performance of small and medium scale enterprises (SME) in Benue state, Nigeria, focusing on twenty SME in Benue state registered with corporate affairs commission from 2019-2023 using ex-post facto research design. The variables used were short term- debt (STD) and long- term debt (LTD) for capital structure and return on assets (ROA) as proxy for firm performance. Regression analysis, using random effects model, as determined by hausman specification test was used for data analysis using STATA 20. Findings were that, there exists a positive and significant effect of short- term debt while there was a negative and insignificant relationship between long- term debt on return on assets. However, on intervening with financial management, the coefficients of margin of contributions of short- term debt and long- term debt on firm performance became significantly enhanced. Based on the results, the study recommended, among others that, firm owners and managers should ensure that the processes of sourcing for funds either for expansion or investment purposes of SME must submit completely to the relevant financial provisions. Government and regulatory agencies should put in place stringent laws to compel firms to embrace financial management principles and defaulting firms should be sanctioned appropriately.

Keywords: Capital, Structure, firm performance, Financial, Management

1 Introduction

The capital structure of firms has been a major subject for academic study in the corporate finance world. This is because financing decision is one of the core business decisions business managers make Abese (2023). It goes without saying that this may not be unconnected with the role finance plays in the life of every business. How to obtain funds for investment activities or to finance their operations is therefore the concern of financial managers. The proportion of debt to equity is a strategic choice of corporate managers. As early as 1945, Chudson carried out extensive research into this area by asking the question. In what way does the structure of assets and liabilities of a given concern reflect the-kind of industry in which a concern is

engaged, the concern's size and level of profitability? Chudson's research question has implied that there might be a relationship between the capital structures practiced by a firm with effect on its performance (Akter, 2021).

Interestingly, firms are often concerned with when to raise additional fund, where to raise it. how much to raise and how much is required from a particular source or from each of the alternative sources. In making financing decisions, firms are expected to be conscious of the costs and contributions of each of the sources to the realization of their desire to prosper, survive, expand and to make profit. In order to accomplish their goals, be they profit or wealth maximization, businesses strive to obtain resources at minimum cost and utilize them efficiently and effectively. Thus, all other things being considered, firms would act rationally by opting for a source or sources of fund capable of yielding higher profit and enhancing their values (Abese, 2023). This implies that a carefully planned capital structure, that is, the financing mix of a business, which basically consists of equity and debt, is beneficial to a firm, particularly for its survival and the enhancement of its value. Therefore, in financing decisions, firms are concerned with the evaluation of the determinants of their financing mix with a view to achieving an appropriate or optimal capital structure.

Small and medium scale enterprises (SME) no doubt play a significant role in the Nigerian economy. They engage in productive activities to the real sector of the economy. Capital structure in SME is made up of short-term debt, retained profits and long-term debts. In addition, capital also represents a source of funds along with deposits and borrowings which is regulated by the capital adequacy requirements.

In performing their roles, SME are expected to choose and adjust their financing mix in fibred to maximize the value of the firm and ensure their operations are not either highly geared or too lowly geared to achieve optimum capital structure. As a caution Okwolli (2022) advised that a firm may have the policy of not borrowing at all (which is very unusual) or to borrow the maximum amount available in the market at the lowest rate of interest, borrow up to some fixed degree of leverage, borrow until the interest coverage reaches some minimum acceptable level or borrow the maximum amount available but limited by what the market is willing to accept.

The determination of appropriate capital requirement and sources of raising funds are of great importance. This is because as earlier mentioned, finance represents the livewire of all business. The lack of adequate capital has always been identified as one the major causes of business failure and no exception to SME. According to Umoh (2020), the unprecedented

financial crises affecting SME in Benue state are mainly as a result of insufficient or capital structure mix.

Sequel to the above, there is need to intensify more research efforts in this area in Benue state which underscore the essence of this research efforts.

Small and medium scale enterprises (SME) play important role in the economic development of Nigeria. The importance of capital structure to corporate financial stability, growth and adequate returns cannot be overemphasized especially in the midst of recent global financial crisis. Yet, these vital issues of capital structure and its effect on financial performance of SME are under researched In Benue state (Abdul, 2017). Closely align with this problem is the fact that previous attempts on capital structure were focused more on listed firms in the non financial sectors leaving out the SME's. In addition, even the research conducted in this sector has produced mixed result. Meanwhile many SMEs continue to underperform leading to take-overs, mergers and consolidation policies to outright collapse in some cases due to inappropriate capital structure decisions made not based on empirically verified evidence (Umoh, 2017). This unfortunate scenario of incessant collapse of SME in Benue state due to lack of appropriate empirically verified information about capital structure mix has led to the impoverishment of Benue citizens with its attendant implication on the economy of the state generally. It is sequel to the above identified problems that this research effort is initiated using financial management as an intervening variable which is used in situations where results of investigations in a specific area continue to be inconclusive or mixed. It is hoped that, the result of this research will provide empirically verified information to the managers and owners of SME about the correct capital structure mix for enhanced performance. The main objectives are to determine the relationship between short term debt and firm performance of SME in Benue state, Nigeria; To establish the relationship between long term debt and firm performance of SME in Benue state, Nigeria; To determine the intervening effect of financial management on the relationship between capital structure and firm performance of SME in Benue state, Nigeria.

2 Literature Review-

2.1 Concept of capital structure

The concept of capital structure is viewed by scholars from different perspectives. According to Akinsurile (2021), capital structure is described as the components of debts and equity, used by a company to finance its operations, and which usually consist of ordinary share capital, preference share capital and debt capital. In the same vein, Kurfi (2024) posisted that, capital structure deals with the question of what happens to the total valuation of the firm and its cost of capital when the ratio of debt to equity or degree of leverage is varied. In other words, capital structure is a mixed of equity and debt. Equity is taken to mean ordinary shares plus retained earnings while debt is taken to mean all fixed interest bearing stock.

Pandey (2021) opined that, capital structure is the proportionate relationship between debt and equity financing of firms. According to him, financial managers of individual firms are saddled with the responsibility of determining the right proportion.

To Akter (2021) capital structure is the permanent financing of the firm represented by long-term debt, preferred stock and net worth. Similarly, Bourke (2021) posits that, capital structure is the mix of a firm's permanent long-term financing represented by debt, preferred stock, and common stock equity. From the above discussion, it is clear that capital structure combines mainly equity and long-term debt. To him, a business concern can go for different levels of the mixture of equity, debt and other financial facilities with equity having the emphasis on maximizing the firm's market value. Capital structure refers to the various financing options of the asset by a firm and it affects the performance of such a firm.

In the views of Abdul (2017)], a firm's capital structure refers to the mix of its financial liabilities. As financial capital is an uncertain but critical resource for all firms, suppliers of finance are able to exert control over firms. Debt and equity are the two major classes of liabilities, with debt holders and equity holders representing the two types of investors in the firm. Each of these is associated with different levels of risk, benefits, and control. It is the way the corporation finances its assets through some combination of equity, debt, or hybrid securities. A firm's capital structure is then a composition or structures of its liabilities, a mix of a company's long-term debt, specific short-term debt, common equity and preferred equity. The capital structure is how a firm finances its overall operations and growth by using different sources of funds. Debt comes in the form of bond issues or long-term notes payable, while equity is classified as common stock, preferred stock or retained earnings. According to Abdul (2017), the consensus is that leverage increases with fixed assets, non-debt tax shields,

investment opportunities, and firm size, and decreases with volatility, advertising expenditure, the probability of bankruptcy, profitability, and uniqueness of the product.

Myers (1984) in his study which developed the pecking order theory identifies that the capital structure of firm range from internal financing to external financing. The internal financing is made up of largely retained earnings while the external financing includes debt financing and equity financing. In similar fashion, Amidu (2024) and Kim (2023) concured that the capital nature of a firm ranges from internal finance, which include retained earnings to external finances, that is, debt and equity.

Akter (2021) identified a more comprehensive capital structure composition, based on their study of Australian small and medium scale businesses capital structure behavior. Consequently, they identified that a company's capital structure should include the following; reinvested profits (retained earnings), short-term debt financing like trade credit, long-term debt financing like debentures and long term debts among others, new equity capital injections from existing owners and new equity capital from un-invested parties like outside investors and venture capitalists.

2.2 Concept of firm performance

A firm's performance is of importance to investors, stakeholders and the economy at large. Investors are interested in the returns for their investment. A business that is performing well can bring better reward to their investors. Performance of a firm can increase the income of its staff, rendering quality product or services to its customers and creating more goodwill in the environment it operates. A company that has good performance can generate more returns which can lead to future opportunities that can in turn create employment and increase the wealth of people. According to Segun (2021), a company's performance is its ability to achieve its target objectives from its available resources. Schmit (2021) viewed a firm's performance as the result of a company's assessment or strategy on how well a company accomplished its goals and objectives. Firm performance provides a deductive measure of how well a company can use assets from business operations to generate revenue.

2.3 Concept of financial management

Financial management is described as the process of planning, organizing, directing and control

ling the financial activities of an organization. According to Kurfi (2024), financial management means, the activity concerned with the planning, raising, controlling and administering of funds used in the business. It is concerned with the procurement and utilization of funds in the proper manner. Financial activities deal with not only the procurement and utilization of funds but also with the assessing of needs for funds, raising required finance, capital budgeting, distribution of surplus and financial controls. Padey (2021) has viewed financial management as an integral part of overall management rather than as one specially concerned with funds raising operations. To Umoh (2020), financial management has to do with procurement of funds and their effective utilization in the business.

Financial management is critical to any company, whether small or big. It is like the lifeline of the business. It is also a vital activity that must be performed in any organization. However, financial management entails the process of planning, organizing, monitoring and also controlling the financial resources of an organization. The idea for doing such is to be able to achieve the vision or goals of the company at the stipulated time frame.

To Tunde (2022), financial management is a regular practice in a business environment. It involves managing a company's financial resources to ensure there is little or no wastage. It controls every single thing regarding the company's financial activities which includes the procurement of funds, use of funds, payments, accounting, risk assessment and other things that are related to finances.

In other words, the use of business funds matters. It's the reason financial management is like the engine room of the company and can affect every other department if not handled properly. So in order to eliminate any form of barrier that may hinder the growth of the business, firms must ensure that the right financial management mechanism is put in place.

In this broader view, the central issue of financial policy is the wise use of funds and the central process involved is a rational matching of the advantage of potential uses against the cost of alternative potential sources so as to achieve the broad financial goals which an enterprise sets for itself. In addition to raising funds, financial management is directly concerned with production, marketing and other functions within an enterprise whenever decisions are made about the acquisition or distribution of funds.

2.2 Empirical Review

Amidu (2023) carried out a study on the sensitivity of performance to capital structure on selected companies in Nigeria. The study used Earnings before Interest and Taxes (EBIT), Earning Per Share (EPS) and Dividend Per Share (DPS) as measures of performance; and Degree of Operating Leverage (DOL), Degree of Financial Leverage (DFL) as measures of leverage. Ordinary least square model was used to estimate the regression equation and the results showed positive associations between debt ratio, firm size and growth, while asset tangibility, risk, corporate tax and profitability regularly related to debt ratio.

Pandey (2021) explained the relationship between capital structure and market structure; and capital structure and profitability. The results suggest that capital structure and market structure have cubic relationship that at lower and high range of Tobia Q ratio firms are using high debt; and at medium range, they use less debt. This is due to agency costs and bankruptcy costs because when firms take more debts there are chances of bankruptcy because the firms might not be able to repay the debts in future. Regarding relationship between profitability and capital structure they conclude that there is a saucer-shape relationship between capital structure and profitability because of the interplay of agency costs, costs of external financing and the interest rate and tax shield.

Schmit (2021) conducted investigation on the relationship between capital structure and performance of Malaysian Construction sector. The result revealed a mixed relationship between the variables investigated. While for the big companies, the result showed a positive relationship between ROC and DEMV on one hand; and EPS and LDC on the other hand. Never the less, a negative relationship was reported between EPS and DC. Meanwhile, for medium size companies, a positive relationship was reported between OM and LDCE. However, a negative relationship was reported between EPS and DC in small size companies

Christopher, Schafer and Talavera (2006) in their study find that there exists strong effect of short-term and long-term debts on profitability. According to them, the organization which prefers financing through long-term debts has low profitability and on the alternative, if a firm uses short- term financing, it earns more profits. In this particular study in which their data covered 1988 to 2000 period, they were able to prove a hypothesis that firms using short-term debt financing are relatively more profitable than the firms using long-term debts. This view tends to favour commercial banks' sources and uses of funds. Demand deposit liabilities are short-term sources of funds to banks and through various short-term channels banks lend short-term funds to rake in huge profits (Luckett, 1984).

3 Research Methodology

3.1 Research Design

An ex-post facto research design was adopted. The ex-post facto (or causal comparative) research design attempts to explore causes that affect relationship where causes already exists and looks backward to explain why. Ex-post facto research design involves ascertaining the impact of past factors on the present happenings or event. Since this study sought to estimate effect of capital structure (past factors) on performance of SME, the choice of this research design is apt.

3.2 Population and Sampling Design

The population of this research work comprised of twenty SME registered with corporate affairs commission in Benue state. Purposive sampling method was used to select SME that have complete financial records to be investigated.

3.3 Data Collection Method

Data was extracted from the audited annual financial reports of the sampled SME for five years (2019-2023).

3.4 Data Analysis

The method of data analysis used in this study is the regression method. This is because of the following reasons; the computational procedure is fairly simple as compared with other econometric technique, regression technique has been used in a wide range of economic relationship with satisfactory coefficients; and it is an essential component of most other econometric techniques.

4. Results and Discussions

Table 1 Summary of Hausman specification test

Variable	P-value
ROA	0.9179

Source STATA Output

Table 2 Summary of random effect regression result for ROA

Variables	**Coefficient**	**Z.value**	**P.value**
LTD	-0.034	-1.500	0.133
STD	0.156	2.960	0.004
F Statistics			0.000
R. Squared			0.480

Source: STATA Output

Table 3 Intervened Random Effect Regression Result of the Effect of Capital Structure on ROA

Variables	coefficient	z.value	p.value
FM	0.299	0.110	0.003
FM*LTD	0.004	0.130	0.000
FM*STD	0.006	2.900	0.001

Source: STATA Output

The results of the random effect regression for the panel data for each of the performance measures and for the full sample of observations for the period 2019 to 2023 are displayed in Table 1 to 3. It is instructive to note that, the hausman specification tests performed show P-value 0.9179 for Table 1. This indicates that, the random effect model was most appropriate for the estimation.

The random effect regression results in Table 2 revealed that, long term debt (LTD) had a coefficient value of – 0.034 and p- value of 0.133 which indicates that LTD has negative and insignificant relationship with return on assets (ROA). Short term debt (STD) had coefficient of 0.156 and a p- value of 0.004 which indicates a positive and significant relationship with ROA. The F statistics value was 0.0000 which indicates that the model was fit. The implication of this is that the estimated equation can be relied upon in making valid inference about the influence of the explanatory variables on the performance of Nigerian firms.

The intervened result in Table 3 indicates that financial management (FM) which is the intervening variable had a coefficient of 0.299 and a p- value of 0.003. The intervened long term debt (FM*LTD) has a coefficient value of 0.004 while the p- value was 0.000. The intervened short term debt (FM*STD) has a coefficient value of 0.006 and a p- value of 0.001.

The reasons for these findings may be due to the followings;

Financial Management involves controlling the financial activities of an organization such as procurement of funds, utilization of funds, accounting, payments, risk assessment and every other thing related to money. It therefore means that when firms adopt this practice in their operations their performance will likely be enhanced.

Proper budgeting of an organization's finance provides quality fuel and regular service to ensure efficient functioning. If finances are not properly dealt with in an organization as budgeted, it will face barriers that may have severe repercussions on its growth and development. This is part of financial management.

Sound financial planning may also be a good reason. Finance is the life-blood of business and there must be a continuous flow of funds in and out of a business enterprise. Money makes the wheels of business run smoothly. Sound plans with respect to capital structure decisions, efficient production system and excellent marketing network are all hampered in the absence of an adequate and timely supply of funds.

A large business firm has to raise funds from several sources and has to utilize those funds in alternative investment opportunities. In order to ensure the most judicious utilization of funds and to provide a reasonable rate of return on the investment, sound financial policies and programs are required. Unwise financing can drive a business into bankruptcy just as easily as a poor product, inept marketing or high production costs. Portfolio investment analysis, which is a component of financial management, is therefore critical if such investments are to be profitable and enhance firm performance.

Choice of investment by firms based on comparative advantage may also be a reason for the positive and significant intervening effect of FM on the relationship between capital structure and firm performance. Financial management provides information about differential advantage in the market place. This information is critical to guide managers to make informed capital structure decision. (How much funds is needed, where to source and where to invest). The success of a business enterprise is largely determined by the way its capital funds are raised, utilized and disbursed. In the modern money-using economy, the importance of finance has increased further due to increasing scale of operations and capital intensive techniques of production and distribution.

Good organization of the firm's finances which is another function of financial management may be another reason. In fact, finance is the bright thread running through all business activity. It influences and limits the activities of marketing, production, purchasing and personnel management. The success of a business is measured largely in financial terms. The efficient organization of the finance function which capital structure decisions are critical is thus vital to the successful functioning of every business enterprise.

The results are in tandem with the submission of Padey [10], who said that for firms to ensure good performance they must plan, organize, control and monitor funds raised by firms for investment purposes irrespective of the sources of the funds. Umoh [12] in agreement also asserted that, funds meant for financing firms that are not planned for, deployed according to plan, monitored and controlled will likely not produce the expected good results.

Based on these findings, the null hypothesis which states that financial management has no significant intervening effect on the relationship between capital structure and performance of SMEs in Benue State could not be accepted.

5. Conclusion and Recommendations

5.1 Conclusion

Based on the result of data analysis and discussion, the study concluded that there is a negative and insignificant relationship between long term debt and the proxy of performance (used in this study) indicating that, the use of long-term debt as a source of firm financing without adequate financial control measures can negatively affect firm performance.

The study also concluded that there is a positive and significant relationship between short term debt and the proxy of performance (used in this study) indicating that, the use of short term debt as a source of firm financing can positively affect firm performance.

The study has also concluded that, financial management has a positive and significant intervening effect on the relationship between capital structure and performance of SMEs in Benue state. The result indicates that, irrespective of whether the capital structure component is long term debt or short-term debt provided that the process of sourcing for such funds and subsequent investment are planned, organized, coordinated, controlled, and monitored, the firm will likely experience improved performance.

5.2 Recommendations

Based on the findings of this study, the following recommendations are suggested to different stakeholders who are involved in the existence of SMEs in Benue state. Long term debt as a source of financing negatively impacted firm performance but the effect became positive when mediated with financial management. Owners and managers of firms should note that, long term debt itself does not hamper firm performance. However, if the process of securing the debt and subsequent investment is not planned, organized, well-coordinated, controlled and monitored such loans secured may not likely enhance firm performance.

Short term debt as a form of financing was positively related to performance with or without mediation with financial management. Owners, managers and would be investors should focus more on this source as a form of firm financing because of the positive and significant impact it has on firm performance.

Since long term debt and short term debt had a positive and significant effect on firm performance when intervened with financial management, it is highly recommended that, firms must strictly comply with financial rules and regulations(financial management) when securing loans, offering shares to the public for subscription, engaging in portfolio investment analysis as well as development of debt management policies.When this is done, it is likely irrespective of whether the source of financing is long term debt or short term debt, it is going to affect performance positively in the operations of small and medium scale enterprises in Benue state all things being equal.

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