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DOES FINANCIAL LITERACY MEDIATE THE RELATIONSHIP BETWEEN FINANCIAL BEHAVIOR AND PERFORMANCE OF SMES CONCERNING THE IMPLEMENTATION OF A CASHLESS POLICY IN NIGERIA?

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ABSTRACT

This research investigates how financial literacy (FL) influences the connection between financial behavior (FB) and Small and Medium enterprises (SMEs) performance. The study selected 255 SMEs engaged in manufacturing, agro-allied activities, trading, education, and transportation in Lagos State, Nigeria. Data analysis was performed by structural equation modeling using the STATA version 15. The result reveals that FL is linked to positive FB and SMEs performance. Evidence also demonstrates that both FL and FB are powerful indicators of SMEs performance. Moreover, the study reveals that FL has a partial mediating effect on the relationship between FB and SMEs performance. In conclusion, this research suggests that FL serves as a fundamental foundation in shaping FB, which in turn encourages online banking activities and enhances financial and investment decision-making. Therefore, policymakers should therefore prioritize the implementation of comprehensive financial education programs specifically tailored to small business owners. These programs develop their understanding of financial knowledge, tools, and techniques to help them make informed decisions and effectively manage their finances.

Keywords: - FL, FB, SMEs, Performance, Online operation Decision-making.

INTRODUCTION

Recently, there has been increasing global interest in examining the FL and FB of SME managers and CEOs (Odewale, Owolabi & Odeku, 2019; Izedonmi & Osabuohien, 2016). Especially in Nigeria, with the introduction of the cashless policy by the Central Bank of Nigeria (CBN), these aspects are essential for small business owners. The main aim of the cashless policy is to train small business owners in the use of electronic payment systems and reduce their reliance on cash transactions. Uba (2020) says the introduction of a cashless policy in Nigeria has brought various benefits to the country's financial system, including increased transparency, efficiency, and convenience. According to the CBN (2012), the cashless policy was implemented to promote electronic transactions and decrease dependence on cash. However, as with any significant policy change, it brings about challenges, particularly for SMEs. These challenges are worsened by the lack of financial knowledge and inadequate financial practices among SME operators and owners. Ajibade et al. (2021) found evidence indicating that many SMEs in Nigeria face difficulties in accessing essential electronic payment infrastructure like point-of-sale (POS) terminals and card payment systems. This lack of access hinders their ability to accept electronic payments from customers, thereby limiting their revenue streams and potential for growth.

Similarly, Uba (2020) observes that numerous SME operators and owners in Nigeria encounter technological obstacles and have limited digital skills, making it challenging for them to effectively adopt and utilize electronic payment systems. This lack of technical proficiency hampers their capacity to manage electronic transactions and creates inefficiencies in their day-to-day operations. Likewise, Lawal and Salihu (2020) confirm that many SMEs have insufficient knowledge about the advantages and functionality of electronic payment methods, which deters their willingness to adopt such systems. This unfavorable situation has hindered SMEs from achieving financial inclusion and growth. Sajuyigbe et al. (2021) lament that over 80% of SMEs in Nigeria experience financial exclusion, leading to premature closure. Additionally, the World Bank (2018) reports that around 2 million SME owners, especially in Nigeria, are not connected to banks. Odetayo, Sajuyigbe, and Adeyemi (2020) express concern that this lack of banking culture among SME operators is a result of insufficient financial literacy and financial practices. Karadag (2015) also confirms that the lack of FL and FB among SME operators has a negative impact on the ability of SMEs to grow and achieve sustainable results. This implies that the decline of SMEs in Nigeria is primarily due to the syndrome of financial exclusion.

Financial experts and researchers have recognized the importance of FL for SME owners. It serves as a valuable tool to equip them with the necessary knowledge and skills to understand how the Cashless Policy will impact their businesses. By enhancing their FL, SME owners can grasp the advantages of adopting electronic payment systems and anticipate the challenges that may arise during the transition (CBN, 2012). Ghosh, and Mondal (2020) have shown that a high level of FL is linked to both financial inclusion and the financial performance of SMEs. Previous studies have also highlighted the significant role of FB in influencing the success of SMEs. How SMEs manage their finances, make financial decisions, and allocate financial resources can have a substantial impact on their overall performance and long-term sustainability (Chowdhury et al., 2019; Gizycki, 2021).

FL and FB have been extensively studied in both developed and developing countries. However, there is currently a lack of research exploring the mediating effect of FL on the relationship between FB and SMEs performance, specifically in the context of the implementation of a cashless policy in Nigeria. This study aims to fill this gap in the existing literature and provide valuable insights for SME owners and policymakers in their pursuit of Sustainable Development Goals by 2030.

THEORETICAL FRAMEWORK

Previous research links many theories such as Behavioral Finance Theory, Social Learning Theory, and Rational Choice Theory to financial literacy, financial behavior and SMEs performance (Sajuyigbe et al., 2021; Odetayo, Sajuyigbe, & Adeyemi, 2020; Khadijah & Wan, 2019; Uba, 2020). However, the fundamental theory explored in this study is Behavioral Finance Theory because the theory provides valuable perspectives on the factors that impact financial behavior and the role of financial literacy in decision-making (Chavali, Mohanraj, & Ahmed, 2021). Behavioral finance theory challenges the conventional assumption of rationality in economic theory and introduces psychological principles to explain deviations from rational decision-making (Chepkemoni, 2017). Arifin (2017) states that behavioral finance combines principles from psychology and economics to comprehend how individuals make financial choices, acknowledging that people's behavior is not always rational and can be influenced by cognitive biases and emotions (Gathergood, 2012). This theory carries significant implications for FL, FB, and SMEs performance.

Khadijah and Wan (2019) argue that behavioral finance theory offers insights into real-world financial behavior by investigating deviations from rationality, enabling policymakers, financial institutions, and individuals to develop strategies that mitigate the adverse effects of behavioral biases. For instance, numerous small and medium-sized enterprise (SME) owners face obstacles related to technology and lack proficiency in digital skills. This poses a challenge for them to effectively adopt and utilize electronic payment systems (Uba, 2020). Lawal and Salihu (2020) corroborate this by stating that many SMEs lack knowledge about the benefits and functionality of electronic payment methods, which hinders their willingness to embrace such systems. Consequently, this theory emphasizes the importance of providing financial skills to SME owners regarding the usage of electronic payment platforms and understanding the advantages and functionality that drive financial inclusion and enhance SME performance. Likewise, Chavali, Mohanraj, and Ahmed (2021) demonstrate that SMEs, given the involvement of owners and managers in decision-making, are particularly vulnerable to behavioral biases.

Behavioral finance theory can therefore help understand the challenges facing small businesses and provide strategies for improving their performance through FL and FB. Hasibuan, Lubis, and Walad (2017) caution that behavioral finance theory sheds light on how financial literacy and financial behavior empower SME owners to engage in online business, utilizing the technological infrastructure of the digital era to create opportunities. Klychova et al. (2018) also confirm that behavioral finance theory serves as a platform through which financial literacy and financial behavior educate SME owners on performing online business and banking transactions, such as checking account balances and making online payments.

CONCEPT OF CASHLESS POLICY IN NIGERIA

The cashless policy was first introduced by Nigeria's CBN in 2012 with the aim of reducing cash transactions and promoting online businesses and banking systems. The directive encourages individuals and businesses to adopt e-banking and other electronic channels for financial transactions (CBN, 2021). The concept behind the cashless policy is to create a more efficient, secure and transparent payment system in Nigeria. The policy aims to address issues such as the high cost of handling cash, the security risks associated with cash transactions, and the prevalence of counterfeit money by reducing reliance on cash (CBN, 2021). The policy also aims to formalize the economy by promoting financial inclusion and reducing the size of the informal sector (Ojo & Omankhanlen, 2020). The implementation of the cashless policy and redesign of the Naira in Nigeria have presented various difficulties for SMEs. These difficulties encompass a range of issues such as limited digital infrastructure, high costs associated with digital payments, low customer uptake, concerns regarding counterfeit transactions, and the need to adjust cash flow management (Ayo, 2020). According to Adeoti, Adeoti, and Fasina (2018), numerous SMEs, particularly those situated in rural areas, face challenges due to the absence of reliable internet connectivity and digital payment systems. This lack of access inhibits their ability to smoothly transition to cashless transactions. Similarly, Oni and Daniel (2018) discovered that SMEs often encounter transaction fees and charges when utilizing digital payment platforms. These additional costs can erode profit margins, particularly for businesses with limited transaction volumes. Ojo and Omankhanlen (2020) also note that the acceptance and adoption of digital payment methods by customers are crucial for many SMEs. However, a significant obstacle arises from some customers' reluctance to embrace cashless transactions.

SMEs must tackle these challenges to effectively navigate the changing financial landscape and take advantage of the benefits offered by digital transactions in the long term. Research indicates that financial literacy and behavior play crucial roles in guiding SMEs towards electronic payment systems, which offer faster and more efficient transactions compared to cash-based methods. This allows SMEs to receive payments instantly, reducing the time spent on cash counting and verification. Consequently, they can focus on other aspects of their business and enhance overall operational efficiency. Supporting this claim, Olagunju (2019) demonstrates that the cashless policy promotes financial inclusion by encouraging the use of bank accounts and electronic payment systems. SMEs that previously relied solely on cash can now access a broader range of financial services, including credit facilities, savings accounts, and insurance products. This enables SMEs to expand their operations, invest in growth, and improve their financial stability (Olayemi & Omoye, 2017). Mordi (2021) expresses concern over SMEs' preference for cash transactions and reluctance to embrace account operations. Meanwhile, according to CBN (2021), the SMEs sector is among the primary beneficiaries of the cashless policy in Nigeria. Cash transactions carry inherent security risks, such as theft, loss, and counterfeit currency. By adopting electronic payment methods, SMEs can minimize these risks and create a safer business environment. Electronic transactions leave a digital trail, ensuring transparency and accountability, which acts as a deterrent against fraudulent activities (CBN, 2021). Similarly, Oni and Daniel (2018) confirm that cash-based transactions often involve additional expenses such as cash handling fees, transportation costs, and security measures. By reducing reliance on cash, SMEs can save money on these operational costs. Moreover, electronic payment systems can offer competitive transaction fees, making them a cost-effective choice for SMEs (CBN, 2021).

EMPIRICAL REVIEW AND HYPOTHESES DEVELOPMENT

FINANCIAL BEHAVIOUR

Financial behavior pertains to the manner in which individuals or entities conduct themselves in relation to their economic activities, such as saving, spending, investing, and borrowing. It encompasses both the cognitive aspects, including beliefs, attitudes, and knowledge, as well as the behavioral aspects, which involve actual actions and choices when managing finances. This concept is particularly important in the context of SMEs, as they play a key role in restructuring the economy and job creation in many countries. Understanding the financial behavior of SMEs is crucial for assessing their financial well-being, performance, and long-term viability. Extensive knowledge about financial behavior can offer strategic advantages to SME owners by helping them avoid mental mistakes and errors, as highlighted by Kostini and Raharja (2019). Likewise, Kiyosaki (2012) asserts that SME owners possessing financial skills demonstrate better financial behavior and effectively manage their financial resources, leading to improved financial performance. Similarly, Ong, Wong, and Teo (2020) reaffirm that SME owners with cognitive abilities consistently handle their finances to achieve predetermined goals and meet expected expenses.

Numerous studies have confirmed that the FB of SMEs has a significant impact on their performance. The way SMEs manage their finances, make financial choices, and utilize financial resources plays a crucial role in determining their overall performance and long-term sustainability. Laraba, and Sani (2021) demonstrate that financial behavior serves as an indicator of financial inclusion and contributes to better financial performance for SMEs. Cai and Liu (2018) also argues that financial behavior serves as a foundation for effectively managing cash flow, which influences the growth opportunities for investments in SMEs. Additionally, Vonkova et al (2020)'s research shows that financial behavior, specifically the effective management of financial risks such as interest rate, exchange rate, and credit risks, significantly affects the financial performance of SMEs. Lussier et al. (2017) further illustrate that SMEs exhibiting prudent financial behavior by carefully evaluating and selecting appropriate financing options (debt or equity) based on their specific needs and risk profile are more likely to achieve better performance outcomes. Khadijah, and Wan (2019) also attest that financial behavior, including regular financial reporting and analysis, provides SMEs with valuable insights into their financial position, profitability, and efficiency, enabling informed decision-making and improved performance. Finally, Hasibuan et al. (2017) confirms that financial behavior empowers SME owners and managers to make informed financial decisions, leading to enhanced financial performance.

MEDIATING FACTOR OF FINANCIAL LITERACY

Financial literacy is the understanding and awareness of the various financial principles and skills necessary to make successful, informed financial decisions. It encompasses the ability to manage personal finances, comprehend the complexities of financial products and services, and evaluate the potential risks and benefits associated with financial choices (Ajibade, Olawumi, & Abiodun, 2021). In recent times, the importance of FL has increased due to market advancements, economic and policy shifts, such as the adoption of a cashless policy and the introduction of a new currency design in Nigeria. These changes have posed challenges for SMEs, including cash shortages, the impact of e-payment trends, limited access to finance, and difficulties in obtaining capital and investments (Lawal, & Salihu, 2020).

Enhancing FL can address these identified problems. Laraba, and Sani (2021)

argue that FL plays a crucial role in promoting financial well-being and empowerment for both individuals and businesses. Cai, and Liu, (2018) provide evidence that FL serves as a foundation for financial behavior that leads to improved financial and investment decisions. Ratnawati et al. (2021) conducted a study that demonstrates a direct link between FL, FB, and SMEs' performance. Similarly, Makdissi et al. (2020) highlight the significant association between financial knowledge and skills with FB and SMEs' performance. Thi, Mien, and Thao (2015) find that FL acts as a catalyst for the FB and performance of SMEs. Arifin (2017) supports this view, showing a significant relationship between FL, FB, and SME performance. Strömbäck et al. (2017) confirm that FL serves as a driving force behind FB and SMEs' performance.

Tang and Baker (2016) conducted a study that verifies the connection between FL, FB, and SMEs' performance. Sayinzoga et al. (2016) reaffirm that FL acts as a driving force for FB and SMEs' performance. Similarly, Xiao et al. (2008) emphasize that small and medium-sized enterprise (SME) owners who possess a range of financial abilities demonstrate favorable financial practices. These include effectively managing budgets, saving money, utilizing online banking services, making informed financial decisions, skillfully handling cash, and engaging in investment activities. As a result, these SME owners achieve strong financial performance.

CONCEPTUAL FRAMEWORK FOR THE STUDY

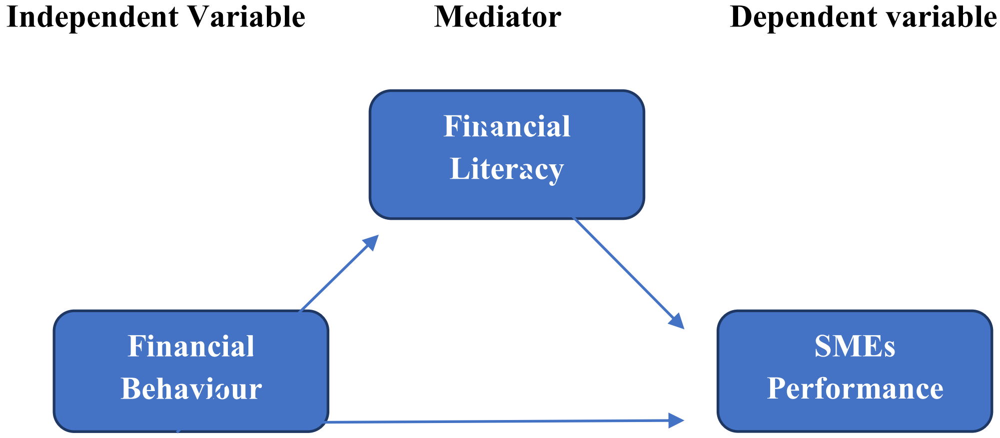

Figure 1: Conceptual Model

Based on the literature review, the following hypotheses were emerged (see Figure 1)

H_1: FB has a significant association with FL

H_2: FB has a significant association with SMEs performance

H_3: FL has a significant association with SMEs performance

H_4: FL mediates between FB and SMEs performance

METHODOLOGY

RESPONDENTS

A total of 255 questionnaires were distributed to small and medium-sized enterprises (SMEs) involved in various sectors such as manufacturing, agro-allied, trading, education, and transportation in Lagos State, Nigeria. The choice of Lagos State was based on its status as the state with the highest number of registered SMEs in the country. The survey was conducted in person, targeting randomly selected SME owners, with the assistance of three researchers to ensure timely attention and response from participants. This approach allowed researchers to pose follow-up questions and gather additional information. The data indicates that a majority of the respondents belonged to the 25-35 age group, followed by the 36-45, 46-55, and 56+ age groups, accounting for 36%, 32%, 20%, and 12% respectively. This suggests that most SME owners within the selected sample are young and energetic, capable of making significant contributions to economic growth and development. The results also indicate that approximately 44.9% of the sampled SMEs are engaged in manufacturing, 10% in agro-allied activities, 30% in trading, 19% in education, and 30.3% in transportation. This highlights that the manufacturing and trading subsectors have the largest representation. Analyzing the results further, it is revealed that 24% of the respondents held B.Sc/HND degrees, 30% had ND/NCE certificates, and 46% possessed a secondary school certificate. Hence, the majority of the respondents had some level of formal education, indicating their ability to competently answer the survey questions.

DESCRIPTION OF THE RESEARCH INSTRUMENTS

The questionnaires used for participants from selected small and medium-sized enterprises (SMEs) in Lagos State, Nigeria, were structured and consisted of three scales: the financial literacy scale (FLS), the financial behavior scale (FBS), and the SMEs performance scale (SPS). A 5-point Likert scale was employed for all measurements in the questionnaires, ranging from 1 (strongly disagree) to 5 (strongly agree).

The Financial Literacy Scale (FLS) was developed and validated by Ratnawati et al. (2021) and comprised five items. Example items included understanding the concept of compound interest, accurately calculating the return on investment for various financial products, and having knowledge about different investment options in the market. The author reported a Kaiser-Meyer-Olkin (KMO) value of 0.781, a principal component value eigenvalue of 2.679, and a variance percentage of 92.56%. These results indicate that the exploratory factor analysis confirmed the consistency of the FLS construct.

The Financial Behavior Scale (FBS) was created and validated by Kostini and Raharja (2019) and consisted of six items. Sample items included regularly tracking and managing expenses, setting financial goals and creating budgets to achieve them, and saving a portion of income regularly for emergencies or future needs. The author reported a KMO value of 0.847, a principal component value eigenvalue of 3.608, and a variance percentage of 72.34%. These findings suggest that the exploratory factor analysis confirmed the consistency of the FBS construct.

The SMEs Performance Scale (SPS) was developed and validated by Izedonmi, and Osabuohien, (2016) and consisted of six items. Example items included experiencing consistent revenue growth in the business over the past year, effectively managing cash flow to meet operational needs, and monitoring key financial ratios (e.g., profitability, liquidity) to assess the financial health of the business. The authors reported a KMO value of 0.644, a principal component value eigenvalue of 1.878, and a variance percentage of 61.89%. These results indicate that the exploratory factor analysis confirmed the consistency of the SPS construct.

Method of Data analysis: Structure Equation Modeling was used to analyze the data using STATA version 15.

RESULTS AND DISCUSSION

Table 1: **Results of the Structural Equation Model with SMEs Performance**

Explanatory Variable	Responses variables	β-value	t-value	p-value	[95% Conf. Interval]	
SPS	FBS	.766	11.74	0.000	.6383286	.8941389
	_cons	1.077	3.70	0.000	.5064851	1.649359

Source: Prepared by the authors (2023)

Table 1 depicts the result of the structural model for the independent variable (FB) and the dependent variable (SMEs performance). There is evidence that the beta values for FB and SPS are 1.077 and 0.766, respectively. We substituted the beta values obtained from the structural equation model into the hypothetical model to obtain:

$$SPS = 1.077 + 0.766_{FBS} \quad \text{………………………(i)}$$

Equation i connotes that a 1 unit change in SMEs performance results in a 1.076% positive change in the FB. This indicates that the more influential predictor of SMEs performance is FB. The calculated t-scores and associated significance probabilities are 3.70(p=0.00) and 11.74 (p=0.00) for constant and FB respectively. SMEs performance is positively and significantly associated with FB. This means that FB is an indicator of SMEs performance. The study aligns with previous studies that FB is an effective management of financial risks such as interest rate, exchange rate, and credit risks, significantly affects the financial performance of SMEs (Kostini & Raharja, 2019; Kiyosaki, 2012; McMahon, 2015).

Table 2: Results of Structural equation modelling with mediator.

Relationship between variables	Estimates	S.E	t-value	p-value	Hypo thesis	Remark
Direct Model						
FLS <- FBS	.766	.065	11.74	0.000	H_1	Confirmed
SPS <- FLS	.603	.090	6.67	0.000	H_2	Confirmed
SPS <- FBS	.193	.091	2.12	0.034	H_3	Confirmed
Indirect Model						
SPS <-FLS <-FBS	.462	.079	5.80	0.000	H_4	Partially supported

Table 2 illustrates that there is a positive correlation between FB and FL, with a beta-value of 0.766 and a t-value of 11.74. Additionally, the t-value of 0.000 indicates that the association between FB and FL is statistically significant. This suggests that FL serves as a platform for demonstrating FB. This finding is consistent with previous research that suggests FL is an indicator of FB (Kostini & Raharja, 2019; Kiyosaki, 2012; Makdissi et al., 2020). Furthermore, the beta-value of 0.603 and the t-value of 6.67 indicate a positive relationship between FL and SMEs performance.

The t-value of 0.000 further confirms the significance of this relationship. Consequently, FL emerges as a strong predictor of SMEs performance. There is also evidence to suggest that FB predicts SMEs performance, with a beta-value of 0.193, a t-value of 2.12, and a t-value of 0.000. The results of the indirect effect analysis reveal that when FL is introduced, the beta-value increases from 0.193 to 0.462, and the t-value increases from

2.12 to 5.80, while the p-value decreases from 0.034 to 0.000. This indicates that FL partially mediates the relationship between FB and SMEs performance. This finding aligns with the guidelines proposed by Kenny and Baron (2003), which state that when the independent variable predicts the dependent variable and the mediator also predicts the dependent variable, partial mediation occurs.

The implication of these findings is that FL provides a foundation for FB, leading to improved financial and investment decisions (Hira, 2012). This study supports the perspective of Thi, Mien, and Thao (2015) that FL acts as a catalyst for the FB and performance of SMEs. Arifin (2017) also supports this view in another study, demonstrating a significant relationship between FL, FB, and SME performance. Additionally, Strömbäck et al. (2017) confirm that FL serves as a driving force behind FB and SMEs' performance.

CONCLUSION

This research investigates how financial literacy influences the connection between financial behavior and the performance of small and medium-sized enterprises (SMEs). A group of SMEs engaged in manufacturing, agro-allied activities, trading, education, and transportation in Lagos State, Nigeria were selected for this study, the number of respondents was 255. Data analysis was performed by structural equation modeling using the STATA version 15. The analysis indicates that financial literacy is linked to positive financial behavior and improved performance of SMEs. The results demonstrate that both financial literacy and financial behavior are powerful indicators of SMEs performance. Moreover, the study reveals that financial literacy plays a partial mediating role between financial behavior and SMEs performance. In conclusion, this research suggests that financial literacy serves as a fundamental element in shaping financial behavior, which in turn encourages online banking activities and enhances financial and investment decision-making.

POLICY IMPLICATIONS

Financial literacy and behavior play a key role in the success and sustainability of SMEs. Policymakers should therefore prioritize the development and implementation of comprehensive financial education programs specifically tailored to small business owners. These programs develop their understanding of financial concepts, tools, and techniques to help them make informed decisions and effectively manage their finances. Governments should provide appropriate resources and support to small and medium development agencies and financial institutions to improve their ability to provide financial literacy programs, guidance and access to financing options. Strengthening theses agencies support will enable them to better assist SME owners in improving their financial behavior and overall business performance. Also, policymakers should continuously evaluate the effectiveness of financial literacy initiatives and monitor the financial behavior of SME owners. Regular assessment allows policymakers to identify gaps and areas of improvement, adjust existing policies, and develop new strategies to enhance financial literacy and behavior among SMEs. This aims to encourage collaborations among banks, microfinance institutions, and small and medium enterprises (SMEs) in order to create tailored financial offerings, including accessible loans, adaptable repayment choices, and effective strategies for managing risks. These customized products are designed specifically to address the distinct requirements of SMEs.

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