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A SYSTEMATIC LITERATURE REVIEW ON FINANCIAL CAPABILITY OF SMALL AND MEDIUM ENTREPRENEURS

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ABSTRACT
The lack of financial capability has become a contemporary issue around the globe. Currently there is a high level of individual indebtedness, an increasing trend of complexity in the financial market, rapidly changing financial landscape, and increased individual responsibility, specifically the growing need of financial capability. The main objective of this study is to critically evaluate the literature on financial capability. The study identified different aspects and different measures of financial capability, levels of financial capability of small and medium entrepreneurs, consequences of financial incapability and methods of improving financial capability. The study revealed financial capability can be improved from tailor-made training programs and workshops. Also, it is necessary to follow up the individual's acts and their behavior to identify whether their performances changed according to the advice given. Finally, the financially capable individual has the capacity to participate more effectively in society and contribute significantly to the economic growth of the country.
Key words: Financial Capability, Financial Knowledge, Financial Literacy

1. Introduction

In the current context, different studies use the terms "Knowledge", "Literacy" and "Capability" interchangeably. However, each term has a unique meaning (Huston, 2010). The financial capability concept originated from financial literacy. One of the oldest records on personal finance education, introduced in 1737 by Benjamin Franklin in his annual almanac, mentions financial advice as "A penny saved is two pence clear" under the title of "Hints for Those That Would Be Rich". Also, there is evidence received on financial literacy in 1787, with a letter from John Adams to Thomas Jefferson using the term (Adams, 1787). In the 19th century, money management was as important a topic as it is today, and records show that early attempts at financial education started during this period. Supporting that, there is an article published in 1849, by James Gilbart, a manager for London and County Bank who moonlighted as a personal finance author, on "Ten Minutes Advice about Keeping a Banker" which discussed advantages of opening a bank account and described the process. James Gilbart published more articles to educate society on banking and its benefits (Lou Haverty, 2019). The financial literacy term was officially taught since 20th century. Lou Haverty, a Chartered Financial Analyst started a site, "Financial Analyst Insider", to provide established extension programs and provide funds for research. However, the financial literacy term was populated since 1914 (Smith-Lever, 1914). He conducted researches and educated the society on useful and practical information and personal finance. During that era, financial literacy was taught in different terms as home economics. Under home economics, the terms of household finances, family finances and consumer economics were delivered.

The first research on personal finance was done in 1920 by Hazel Kyrk and Lowry and is a foundation of consumer economics and family economics. The first study on consumer behavior and household behavior was done by Margaret Reid, a professor of home economics during the 20th century. Starting from the 21st century, financial literacy plays a vital role in every economy and most countries have financial education systems, mainly concentrated on tracking expenses, budgeting, saving smartly and building wealth. Most of the countries identified without financial literacy education systems are the countries exposed to financial risk (Kirkwood, 2017).

With the economic development, people expand the confidence and strategic attitude on financial system to have long-term financial health. Hence, the financial literacy concept was not sufficient to achieve their long-term financial needs and as a result, the impotency of the financial capability concept arose as a broader aspect. The financial capability concept was initially defined as a "set of knowledge, attitudes, habits, and confidence in one's ability to control one's finances that a consumer needs to build his or her financial wellbeing" (EVERFI, 2018). The current study reviewed the literature on different aspects of financial capability in developed countries, financial capability of small and medium entrepreneurs, and different factors used to measure financial capability. The evaluation was carried out in terms of financial management competency, socio demographics, self-efficacy, financial resources and financial sophistication as factors of financial capability.

Financial Knowledge

Set of fundamental skills required to read and write, may assist with understanding contract terms and basic financial activities such as budgeting, and helps with financial decision making (Huston, 2010) (Coonan, 2004).

Financial Literacy

Consumers knowledge and confident financial performance regarding budgeting, spending, borrowing and investing (ANZ, 2005) are always decided based on financial knowledge. Individual's ability to obtain, understand and evaluate the relevant information necessary to make decisions with an awareness of financial consequence (Mason, 2000). Also, ability to make informed judgments and take effective decisions regarding the use and management of money (Noctor, 1992).

Financial Capability

In current economic context, financial capability has become an emerging concept (FINRA & Investor Education Foundation, 2009). The Basic Skills Agency on behalf of the Financial Services Authority in United Kingdom conducted a baseline survey of financial capability to express the distribution of financial capability and to look for groups of people with similar skills (Atkinson A. M., 2006). The concept of financial capability expresses individual knowledge and skills to understand their financial circumstances along with the motivation to take action (Treasury HM, 2007). Another concept is the perception of consumers' behavior regarding financial matters, consisting of four financial domains: managing money; planning ahead; choosing the most suitable financial debt instruments and products; and staying informed by seeking information (Atkinson A. M., 2007). Financial capability is a macro term associated with knowledge, skills, attitudes and behavior of the individual. The financially capable individuals can make budgets, manage money effectively assess risk and returns and effectively assign insurance and protections and take informed financial decisions and have a wider ethical, social, political and environmental dimensions of finances (Noctor, 1992).

Research Objectives

The main objective of this paper is to critically evaluate the literature on financial capability. The study identified the different aspects of the financial capability, different measures of financial capability, the level of financial capability of small and medium entrepreneurs, the consequences of financial incapability, and the methods of improving the financial capability to help the policy makers to actively fill this missing gap and ultimately achieve economic development.

2. Research Methodology

The study employed a discussion-based approach where the previous work on financial capability of different segments in the society and small and medium entrepreneurs, their behavior in terms of financial activities, and the business results, were thoroughly analyzed and critically evaluated.

3. Literature Review

Different aspects of financial capability in developed countries

Financial management competency as a factor of financial capability

In a study done in Italy, the financial capability of Italian households were based on planned spending behavior, budgeting, financial decision making and cash management controls (Monticone, 2010). In addition, savings is a key behavior of the financial capability, affected by various institutional savings products, the offering of incentives, financial education and facilitation (Beverly, 1999), (Han, 2009) and (Cohart, 2016). According to a study done in the UK, financial capability of adults depends on knowledge and understanding, skills and confidence and attitudes (Basic Skills Agency, 2004). In behavioral terms, financial capability has 4 separate aspects as; managing money, planning ahead, making choices and getting help (University of Bristol, 2006). In a study on UK employment, abilities, understanding, competence, knowledge and motivations were identified as key factors of financial capability (Egdell, 2010). The author expressed that more capable individuals are able to deal productively with the day to day management of finances; plan ahead; efficiently select financial products and understand these products; know where, and how, to seek financial advice, and have the motivation to efficiently manage finances and effect change. (The World Bank, 2013) expressed financial capability as individuals' internal capacity, to contain financial literacy, skills, attitudes, select financial products, rational behavior and fulfill financial needs from the products available in the financial market. According to the (World Bank, 2015) "Financial capability means that individuals have the internal capacity to act in their best financial interest, given socioeconomic and environmental conditions, which can play an important role in constraining or facilitating individual financial capability". However knowledge of financial services is not a component of financial capability in developed countries, since they have more knowledge and they have problems with the lower levels of access to financial services (Kempson E. P., 2013).

Socio demographics as a factor of financial capability

In a study done in UAE, the financial capability of UAE-national investors depends on demographic factors such as income, education, occupation and the level of financial knowledge (Hassan Al-Tamini, 2009). The financial services providers introduced different products to different people according to their geographical locations (Atkinson A. M., 2007) (Remund, 2010). In a study done in Australia, there is a positive linear relationship between financial literacy and socio demographic factors with participants who were of low education, unemployed, unskilled, earning less than $20,000 per annum with a savings level under $5,000, single, young (18–24 years old) or older (over 70 years) having lower levels of financial literacy (ANZ, 2003), (ANZ, 2005). (Kempson E.,

2005) has identified three areas of financial capability that influence behavior: (a) knowledge and understanding, (b) skills, and (c) confidence and attitudes. With regards to gender, (Mahdavi, 2012) expressed that even well-educated women have low financial literacy. The literature suggests that background factors have an impact on an individual's financial capability. Suffice it to say that an educated, employed male living in an urban area will be more financially capable than his peers (Kimball, 2006), (Klapper L., 2011), especially if his parents were educated (Lusardi, 2010).

Self-efficacy as a factor of financial capability

Self–efficacy is an important psychological factor that influences our thoughts, emotions, actions, motivation and overall human behaviors to measure financial capability (Jing Jian Xiao, 2013). Past studies evidenced financial self-efficacy as a key factor of financial capability (Victoria Vyvyan, 2014), (Atkinson A. S., 2006). According to (Bandura, 1982), "Perceived self-efficacy is concerned with judgments of how well one can execute courses of action required to deal with prospective situations". Self-efficacy is incorporated in the theory of planned behavior as an important determinant of human behavior and perceived control (Ajzen, 1991). Self-efficacy is also a measure of the belief in the individual's own ability to complete tasks and reach goals and high self-efficacy behavior has a positive relationship with the domain of making ends meet and with the ability to keep track of finances (Ormrod, 2006). There is a positive relationship between financial capability and self-efficacy (Gyarmati D. L., 2014). Financial self-efficacy has a positive impact on the personal financial management behavior (Muhammad Ali Jibran Qamar, 2016). Individual financial efficacy was found to have a strong positive association with financial well-being (Vosloo, 2014). Higher financial self-efficacy is associated with less financial issues (i.e. more control over individual finances) (Lapp, 2010). Perceived behavioral control (which includes financial efficacy) was found to have a positive association with good financial practices (Xiao J. T., 2011). Studies carried out in Australia expressed that financial capability has a link with budgeting skills which will control spending, resulting in reduced personal debt levels as it helps consumers to differentiate between their needs and wants (Coonan, 2004), and the possible consequences of overspending (Brougham, 2011).

Financial sophistication as a factor of financial capability

Financial sophistication is the financial capability of an individual to avoid making investment mistakes (Hilgert, 2003). The high level of financial sophistication leads to efficient money management. Financial sophistication improves the portfolio returns and the incentive to substitute consumption interests (Padula, 2013). Less sophisticated individuals hold under-diversified portfolios (Calvet L, 2009) or stay away from the stock market entirely (Van

Rooij, 2007) (Huberman, 2005). The same studies expressed that individuals with high financial sophistication have more desire to invest in stock market. The high level of financial literacy increases financial sophistication and boosts the accumulation of wealth (Rooij V. M., 2008). The richer, better educated households tend to be better diversified (Blume, 1975); (Calvet, 2007); (Goetzmann, 2008); (Vissing-Jorgensen, 2003), display less inertia (Agnew, 2003), (Bilias, 2008), and have a weaker disposition to hold losing stocks and sell winning stocks (Calvet L. E., 2009); (Dhar, 2006) than other households. The more financially sophisticated households invest more efficiently (Calvet, 2007). In past studies, financial sophistication was measured by using wealth, income, education and financial experience (Calvet, 2007), (Calvet L, 2009).

Financial resources as a factor of financial capability

The financially capable individual has better capability of managing their money and money management involves being well organized and keeping control over financial resources (Kempson E., 2005). Various studies use managing money as a key factor of financial capability and if a person was not able to manage their money day to day, then no matter how good they were at planning ahead, choosing and using products, or seeking advice, they would not be able to make the best use of their financial resources (Atkinson A., 2006), (Atkinson A. M., 2007), (Financial Services Authority, 2006). Resources can be either human or material in nature. The human resources within the family system are the skills, abilities and knowledge of individual family members. Tangible goods, savings, and investments represent the material resources of the family (Deacon R E, 1988). Financial capability is a construct that goes beyond financial literacy, referring not just to knowledge or understanding of financial concepts, but to how people manage their resources and make financial decisions (FINRA Investor Education Foundation, 2009). In both higher and lower financial capability groups, the most relied upon financial resources in the case of an emergency was existing savings and credit cards (Sanja Ajzerle, 2013). Individuals typically benefit from having larger, less dense, and more diverse networks as these can leverage a wider range of resources (Gyarmati D. L., 2014). Those with the least resources are particularly at risk of serious consequences due to a lack of financial capability and if someone's capability goes beyond their access to resources and utility give ability to make appropriate financial choices (Sen, 1998), (Egdell R. M., 2010). Adequate possession of financial resources gives more financial satisfaction (Hira, 1998). Also previous studies revealed, the level of available resources have an impact on financial behavior, as consumers with less available resources may fail to meet all of their financial obligations, or lack the means to save (Aizcorbe, 2003); (Hilgert, 2003). Achievement of higher number of financial resources increase financial capability of the individual.

In summary, past studies considered financial capability based on the individuals' knowledge and understanding, skills, confidence and attitudes, financial literacy, internal capacity, and rational financial behaviors. Past literature identifies individuals under 45 years, who are married or living with a partner, unemployed, have low income, live in rented accommodation, have recently had children, have low levels of education, and are women (do not stay informed), as having a low level of financial capability (Atkinson A. M., 2007), (Thoresen, 2008), (Egdell, 2010),. (Noctor, 1992) and (University of Bristol, 2006).

Financial Capability of Small and Medium Entrepreneurs

Small and Medium businesses are the backbone of every economy. The business success of the small and medium entrepreneurs is associated with the ability to manage their financial matters (Husniyati Ali, 2017). In the business operation, entrepreneurs always make decisions of acquisition, allocation and utilization of financial resources. To obtain sustainable development in the competitive market, financial capability plays an important role. The (Banking Association of South Africa, 2014) defined the financially literate SME as one "which: (i) has an adequate level of personal entrepreneurial competencies, personal finance skills, and business management skills; has an appropriate level of understanding of functional financial management systems; (ii) has an appropriate level of understanding of SME life-cycle funding and other financial services needs and options and knows where and how to source and negotiate those funding and service requirements; (iii) understands and can manage financial risks or seek relevant advice to man-age such risks; (iv) understands legal, regulatory and tax issues as they relate to financial matters; (v) understands the range of legal re-courses it can resort to when necessary, and namely, in case of bankruptcy or other situations of financial distress." (The United States Agency for International Development, 2014) explained the financial literacy of the SME owners/ managers as "someone who knows what are the most suitable financing and financial management options for his/her business at the various growth stages of his/her business; knows where to obtain the most suitable products and services; and interacts with confidence with the suppliers of these products and services. He/she is familiar with the legal and regulatory framework and his/her rights and recourse options."

In developing countries like South Africa, access to finance is a major issue faced by entrepreneurs (Herrington, 2009). The financial literacy and capability can improve access to finance of the entrepreneurs (Wise, 2013), reduce the chances of loans falling into arrears (Kotze, 2008) and enhance the performance of the business (Bruhn, 2011).

In Sri Lanka, Small and Medium enterprises represent more than 75% of the registered enterprises and the contribution from the sector to GDP is 52% (Ministry of Industry and Commerce, 2018). The constraints on growth of Small and Medium Entrepreneurs are still not resolved and out of all challenges, the main constraint is access to adequate and timely financing on competitive terms and fulfilling the working capital and expansion requirements of the business (Premaratna, 2017), (Amaradiwakara, 2017), (National Policy Framework for SME Developement, 2015), (Daily FT, 2015), (Rathnasiri, 2015) . Notwithstanding every one of the aggravations, the biggest reason for this development is lack of financial capability (Amaradiwakara, 2017), (Sri Lanka Economic Association – Annual Sessions, 2017). According to the recent literature, compared to income poverty, lack of financial management competency, inadequate financial knowledge and financial incapability significantly increase the financial stress of the Small and Medium Entrepreneurs (Marmot, 2004), (Wilkinson, 2005). In Sri Lanka, there are very few studies on the financial capability of the small and medium entrepreneurs.

Measures of financial capability

There is no universal standard method to measure financial capability (Cole, 2008). However different studies use different items to measure financial capability. (See Table 1.)

The consequences of financial incapability

The lack of financial capability can lead to an inability to make conversant decisions (Norvilitis J. M., 2006). This happens due to poor financial selection with high financial cost (Monticone, 2010). Individuals with a lack of financial knowledge and weak financial management do not understand the gravity of the accumulating credit and may be at risk of becoming over indebted adults (Perry, 2005). The study of (Egdell, 2010) stated that individuals may have poor financial management skills, and lack of financial management leads to increasing debt and the problem get worse with some individuals cutting back on essentials in order to meet their repayments (Gillespie, 2009). Unemployment is a direct cause for the lack of financial capability and individuals who are working can also suffer the consequences of a lack of financial capability as financial stress has been linked to absenteeism from work (Kim J. S., 2006), (Kim J. a., 2003). Lower income individuals save only for special reasons and utilize all savings (Kempson, 2000). Individuals may be experiencing high levels of stress and anxiety due to the lack of capability (Lenton, 2008), (Taylor, 2009), and individuals with low income, always turn to doorstep lending or even loan sharks and they do not maintain any savings and most of the time they default on other commitments to repay these high interest loans without questioning (Atkinson A. , 2005), (Randall, 2006). Older

Table 1: Financial capability measures

Study Population	Author	Financial capability measures
Individuals	(Kempson E. C., 2005), (The World Bank, 2013), (World Bank, 2015), (Basic Skills Agency, 2004), (University of Bristol, 2006), (Atkinson A. M., 2006), (Collard, 2012), (Jang, 2015)	Knowledge and understanding, Skills, and Confidence and attitudes, Financial literacy, Skills, Attitudes, Select financial products, Rational behavior and Fulfill financial needs from the products available in the financial market, Financial Resources, Environmental factors, Social factors, Financial behavior, Managing money, Planning ahead, Choosing products and Staying informed, Making ends meet, Keeping track of money, Motivation, Opportunity, Financial management competency.
Tenants	(Hopkins, 2008)	Budgeting skills, Paying the rent and Setting up a home, Opening and using a bank account, Savings, Borrowings and understanding welfare rights issues.
Italian households	(Monticone, 2010), (Taylor, 2011)	Planned spending, Budgeting, Financial decision making, Cash management controls and Level of personal wealth accumulation, Way of managing money, control of finances, making appropriate financial decisions, understanding how to manage credit and debt and identifying appropriate products and services
Scotland Employees	(Egdell, 2010)	Abilities, Understanding, Competence, Knowledge and Motivations
Consumers	(Jing Jian Xiao, 2013)	Perceived financial capability, Financial literacy, and Financial behavior
Financial Counselors in Australia	(Vyvyan, 2014)	Self-esteem and Self-belief

individuals are more financially capable (Financial Services Authority, 2006) and individual social networks directly and indirectly affect their financial decisions (Kempson, 2000), (Meadows, 2004). According the study done by (Fitch, 2007) on debt and mental health, 25% of the individuals are suffering mental illness due to the problem of debt. Studies also expressed the development of financial capability as directly connected with the change of individual's behavior (Mandell, 2007), (Dixon, 2006), (De Meza D., 2008), (Oehler, 2008). A past study done by (Lea, 1995) on psychological factors in consumer debt in United Kingdom found that poor financial management was overcommitted with personal debt. Also, financially incapable people face difficulties on selecting appropriate financial products for their requirements and they don't have an idea of getting advice. Hence they caught for bad practices and mis-selling (National Association of Citizens Advice Bureaux, 2001).

4. Conclusion and Recommendations

According to the systematic review of the existing literature, financial capability supports entrepreneurs to manage the day to day financial situation of the organization, create successful background to plan ahead, give efficiency to manage financial products, furnish knowledge to seek financial advices and creates a foundation to manage the financial position of the business effectively and efficiently. As transpired from the existing findings, the majority of the entrepreneurs who lack financial capability, are mostly at risk. Overall, the literature expressed that the lack of financial capability results in lower financial management, inability to make conversant decisions, high levels of financial stress, no retirement savings or planning (Clark GL, 2009), mental illness due to the problem of debt (Lenton, 2008); (Taylor, 2009), absenteeism from work (Kim, 2003), (Kimball, 2006), entering into a financial arrangement they cannot maintain (Randall et al., 2006), not being able to cope with unexpected changes (Financial Services Authority, 2006), and an increase in older people's risk of being victims of financial abuse (Crosby, 2007). Finally, improving an entrepreneurs' financial capability can enable them to participate more in the society and contribute significantly to economic growth.

To overcome the above constraints, past studies highlight financial management competency and financial sophistication as factors of financial capability, and suggest the inclusion of financial education programs in the primary and secondary school curriculum (Granville, 2009), delivery of financial literacy feedings during the different stages of life and tailor-made training programs to motivate individuals to enhance financial capability (Jones, 2006), (Social and Enterprise Development Innovations;, 2004), (McCormick, 2005). Past studies recommend training as the best method to develop the financial capability of individuals. Practically, different approaches need to cater for the different segments in the society. According to the study done by (Collard, 2012), to enhance the financial capability of the tenants, the training needed to be organized as one to one sessions rather than group sessions and at their place rather than gathered to different places or personal contact – cold calling by telephone. Printed materials and local area promotions are not effective other than the above tailor-made trainings. Similar findings justified by the study done by (Collard, 2012) stated, different segments of society has to use different techniques to enhance financial capability. Also past studies done on socio demographics and financial resources as factors of financial capability suggested, the financial capability were wider with the organizing of workshops and follow up of individuals to check whether their behavior changed according to the advice on making a commitment (CFEB, 2010). Improving an individual's financial capability can enable them to participate more fully in society and help to reduce poverty (University of Bristol, 2006). The study done by (Vyvyan, 2014) recommended that those developing financial capability programs should address behavioral and contextual factors rather than concentrating purely on literacy. Studies done on self-efficacy as a factor of financial capability suggested that financial capability can be improved thorough developing self-efficacy by applying flexible plans to manage expectations about success and accepting failure positively, watching similar people succeed or hearing success stories, developing model experiences and increasing happiness and taking advice to reduce stress (Bandura, 1982), (Dixon, 2006).

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