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Does Book-Keeping Contribute Toward High Failure Rate of Business During First Year of Operation?

A Case of South Africa

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Abstract

The high failure rate of businesses during the first year of operation is a well-documented phenomenon globally, with South Africa being no exception. This research investigates the role of book-keeping practices in contributing to this high failure rate among South African small and medium-sized enterprises (SMEs). By examining the relationship between financial management, particularly bookkeeping, and business sustainability, the study aims to determine whether inadequate or poor bookkeeping practices are significant factors in the early demise of businesses. The population size that was targeted consisted of 311672 small businesses that were registered with the CIPC in South Africa during the first quarter of 2023 and were no more than a year old. To sample a population with a 0.1 per cent chance of selection and to remove bias, essential random sampling was employed using Excel Quantitative Management (QM). Consistent with similar studies, a sample size of the study was 150 new SMEs. Data was collected through semi-structured interviews with SMEs owners. The findings reveal a strong correlation between poor bookkeeping practices and business failure, highlighting the need for enhanced financial literacy and the adoption of effective bookkeeping systems. This study investigated lack of bookkeeping practices contributes to the high failure rate of business during the first year of operation.

Keywords

Inadequacy accessibility of capital, Statement of financial position, Income statement, Cash flow statement, Liquidity constraints, Competitiveness

INTRODUCTION

Lack of financial expertise causes businesses in South Africa's first year of operation to fall short of meeting the demands of stakeholders, including creditors, borrowers, and customers. Moschella, Boulianne & Magnan (2023) indicate financial knowledge is a factor in poor cash management, loan defaults by South African businesses in the first year of operation, and low business liquidity. Given limited financial resources, a barrier to a business's survival is the inability to develop financial strategies in the first year of operation that will increase liquidity. Furthermore, difficulties in creating and analysing financial statements and maintaining financial records are difficult because of a lack of bookkeeping practices expertise. Monitoring cash inflows and outflows is crucial for business management, particularly for businesses with limited funding, according to Adian, Doumbia, Gregory, Ragoussis, Reddy & Timmis (2020), who describe bookkeeping practices as the repository for documents pertaining to financial transitions in enterprises. Moreover, Peprah, Abdulai & Agyemang-Duah (2020) highlight the inadequacy of record management as detrimental to business owners' ability to determine profit in the first year of operation in South Africa. Imo & Chukwu (2022) point out that maintaining accurate and timely accounting records is essential to expressing a transparent financial picture of the company and determining success or failure. In South Africa, bookkeeping practices is crucial to a business’s survival in the first year of existence, highlights Zahrah Buyong (2020). According to Imo & Chukwu (2022), the degree of accounting knowledge and abilities is crucial for business owners in South Africa to develop solid bookkeeping practices throughout the first year of operation. Record management is crucial for proper managerial decision-making, consistency, impartiality, ongoing learning and development, efficient risk management, and the competitiveness of businesses in South Africa during the first year of operation, asserts Dimitriou (2020). The main topics of the study from the standpoint of business expansion and sustainability are the lack of bookkeeping practices contributing to the high failure rate of business during the first year of operation, the challenge of obtaining funding, and the advantages of financial literacy.

LITERATURE

For South African businesses operating in the first year, bookkeeping practices refers to generating and/or keeping track of financial records of business activities. Bullock (2021) defines bookkeeping practices trachoma as simple to use, intelligible, trustworthy, precise, consistent, and built to provide information quickly. Imo & Chukwu (2022) state bookkeeping practices aid in record analysis, monitoring, creating paperwork required for taxation, and evaluating businesses' financial status in the first year in South Africa. In the initial year of operation, South African businesses can leverage bookkeeping practices as a basis for growth, competitiveness, and sustainability. Record management is a critical ability for businesses in the first year of operation, according to Zahrah Buyong (2020). In South Africa, is necessary to identify, store, and protect critical business records and administer all recorded business transactions. The process of having essential documents as proof and references for the business in the first year of operation in South Africa is another. Bullock (2021) notes that bookkeeping practices is a performance indicator in South Africa and is significant in determining a business's profitability in the first year of operation.

Theoretical Literature

Maintaining financial records, such as bookkeeping, is essential to business administration. To prepare and show financial accounts, bookkeeping involves identifying transactions, classifying, summarizing, storing, protecting, reporting, and maintaining financial records.

Benefits of record management

Gjokaj, Kopeva, Krasniqi & Nagy (2021) indicate that record management also includes the following: a general journal, a nominal ledger, a petty cash book, a cash receipt book, a purchases day book or purchases journal, a cheque payment book, a debtors' ledger, and a creditors' ledger. Zahrah Buyong (2020) explains in his article on the sales day book or sales journal that the sales record is the most essential document in the business because it is acknowledged as the reason for the business's existence and survival during the first year of operation. Tracking all customer transactions, including credit and cash sales, is made possible by keeping a sales day book or sales journal. In the first year of business in South Africa, the cash receipt book is an essential document for tracking the available cash for the business. Business owners can measure received cash flow against cash paid by keeping track of bank account activities using a cash receipt book. In the initial year of the business, South African business owners evaluate the liquidity and accessibility of financial resources for everyday operations based on the documented transactions in the business bank account. Additionally, Dimitriou (2020) asserts that cash receipt books help South African business owners keep regular tabs on the revenue and expenses throughout the first year of operation. All business transactions for walk-in consumers are documented in the purchases daybook or purchases journal by issuing a till slip or cash register receipt. In South Africa, the purchases day book, also known as the purchases journal, and the cash receipt book are typically used concurrently because they both employ a similar method to document business transactions during the first year of operation. Similar to a cash receipt book, a cheque payment book can be used to document business transactions. The debtors' ledger applies to South African businesses with credit facilities for clients and is in the first year of operation. The debtors ' ledger documents all credit sales and amounts owed to borrowers. In South Africa, debtors' ledger helps business owners track the assets and cash flows throughout the first year of operation. In South Africa, the creditors' ledger documents the business's liabilities throughout the first year of operation, including credit purchases for products and services. Businesses in the first year of operation in South Africa with suppliers' credit facilities can use creditors' ledger records. Tinits & Fey (2022) and Dvoulet, Srhoj & Pantea (2021) assert that the administration of record management for businesses during the first year of operation is contingent upon obtaining invoices, bank teller records, and receipts. These records are further documented in subsidiary books, specifically the day books for purchases and sales. Furthermore, all obtained documents have to be entered into several ledgers, including the debtor, creditor, and general ledgers. These ledgers are then verified by trial balances and final financial reports (statements of comprehensive income and financial condition).

Reporting framework

To determine the financial competitiveness of the business in the first year of operation in South Africa, Oosthuizen, Van Vuuren & Botha (2020) highlight that record management is an essential tool for developing financial reporting, such as a statement of financial position, statement of comprehensive income, and cash flow projection. In South Africa, the insufficiencies of financial statements eliminate information asymmetry among financial institutions and foster positive relationships with creditors during the initial year of operation. According to Caruso (2020) and Udoh & Okon (2021), the statement of financial position records the monetary measurements of the resources used, such as the business's assets and the sources of financial resources (owners' equity or liabilities) that were used to finance the business during founding year in South Africa. A statement of financial position represents a snapshot of the business's financial situation and is prepared at a certain point in time, according to Fadil & St-Pierre (2021). The creation of a statement of financial position documents three components, namely assets, liabilities, and owner's equity, as asserted by Renaldo & Sevendy (2023); to guarantee a return on investment, assets are things that businesses hold and have a monetary value. Debtors, shares, and cash are current assets; fixed assets include plant, property, and equipment. There is no replication of any change in market value in the costs and monetary worth of all registered assets. Liabilities are short-term commercial debts that must be paid back within a year. These debts include salary, stock, and other expenses incurred by the business during the first year of operation in South Africa. Mortgages, bonds, and equipment leases with medium- to long-term payments are examples of long-term liabilities. Owners' equity, which represents the value of a business in the first year of operation in South Africa, is calculated as total assets minus total liabilities. Owner equity typically results from the owner's personal investment in the business and from the business's gains or losses. An insolvent business is indicated by a negative owner's equity, which shows that obligations exceed assets. Balagobei (2020) indicates that the income statement documents the business's financial performance and profitability, encompassing all revenue and expenses throughout the initial year of operation in South Africa. Mehdiyev (2024) articulates the creation of a statement of comprehensive revenue comprises three elements: a trading account, an expense summary, and non-trading income. The trading account reflects the gross profit calculation after deducting the cost of products sold from the revenue received. The detailed breakdown of expenses incurred in producing revenue is recorded in the second section of the comprehensive income statement. In the first year of business, establishment, administration, finance charges, and other overheads are included in the summary of expenses recorded in South Africa. In the first year of business operation in South Africa, non-trading income captures additional income from the sale of an asset or investments made by the business.

Financial statements

According to Najera Ruiz & Collazzo (2021), business income is mainly pertinent to a specific period, so it's critical that the comprehensive income records statement accurately reflects this period. South Africa must prepare a statement of comprehensive income every month to monitor and appropriately manage business difficulties, given the volatility of business owners in the first year of operation. Two restrictions on the declaration of comprehensive revenue for business owners in the first year of operation are pointed out by Escaloni & Mareque (2021). An accrual basis is commonly used to create a statement of comprehensive income, which indicates that revenue and expenses must be recorded at the time of the transaction, preferably with cash payments. In the first year of operation, South African business owners must know that the profit shown in the comprehensive income statement does not always correspond to the amount of cash received, as cash is typically invested primarily in stock and debtors. The second restriction is significant discrepancies between net profit and taxable income, and the comprehensive income statement is unsuitable for income tax computation. As per Ahinful, Boakye & Osei Bempah (2023), the creation of a statement of financial position and a statement of comprehensive income aids South African business owners in the initial year of operation by documenting the financial outcomes of the operations and the financial status at a specific moment in time. While creating these records is crucial for companies in the first year of operation in South Africa, they do not necessarily reflect the owner's understanding of the business's financial situation. Zizi, Oudgou & El Moudden (2020) indicate the cash flow statement, which comprises operating, investing, and financing operations, is added to the statement of financial position and the statement of comprehensive income. By maintaining cash flow statements, businesses in South Africa can avoid overinvesting or overtrading during the first year of existence, which could lead to insolvency. In South Africa, a cash flow statement helps entrepreneurs in the first year of operation by converting profits into cash flow items through working capital activities and retrogressive non-cash flow items. Both Hoti & Krasniqi (2022) and Escaloni & Mareque (2021) emphasise the importance of the cash flow statement in guiding by showcasing the cash inflows and outflows that occurred during the reporting period and the net outcome's impact on the cash resources of South African businesses in the first year of operation.

Empirical Review

The accuracy of bookkeeping procedures and the timely reporting of accounting data to express a transparent financial business position determine the success or failure of the enterprise. Escaloni & Mareque (2021) indicate insufficient bookkeeping procedures during a business's first year of operation in South Africa create barriers that harm the business's competitiveness and performance. Najera Ruiz & Collazzo (2021), emphasises that lower educational attainment, a lack of business management experience, insufficient staffing, and a lack of business expertise are the main causes of South Africa's poor first-year bookkeeping procedures knowledge. Caruso (2020) states poor bookkeeping procedures lead to resource mismanagement and poor cash management, both of which have increased the number of South African businesses that fail within the first year of operation. Mehdiyev (2024) points out that insufficient bookkeeping procedures make it difficult for business owners in South Africa to distinguish between business and personal transactions during the first year of operation. They have also been known to use company assets for personal gain. Renaldo & Sevendy (2023) highlight might be difficult for South African businesses to distinguish between company expenses and earnings during the first year of operation due to the lack of distinction between personal and business transactions. Furthermore, Hoti & Krasniqi (2022) outline that business owners' calculations of profit in the first year of operation in South Africa are negatively impacted by the improper use of accounting information.

Fadil & St-Pierre (2021) states a number of barriers to businesses keeping financial records during the first year of operation, including the need for more accounting staff, exposure to the business's financial position, higher tax payments, difficulty maintaining the system, and the requirement for technical skills and knowledge. According to Hoti & Krasniqi (2022), the difficulties faced by businesses in the first year of operation included the relative cost of hiring professional accountants, a lack of adequate training on fundamental financial reporting principles, a false impression of accountants, a lack of knowledge and skills regarding finances and the importance to the business, and a lack of computerised accounting systems. Udoh & Okon (2021) investigated the accounting recordkeeping practices of businesses in the first year of operation. They discovered that the challenges faced by these businesses in maintaining proper accounting records were limited funds, inexperienced first-year business operators, family obligations, and a lack of professional accountants.

METHODOLOGY

This qualitative study sought to gain an in-depth understanding through exploratory research. Exploratory research was used to investigate a lack of bookkeeping practices contributing to the high failure rate of business during the first year of operation. Through exploratory research, businesses experienced inadequate business liquidity, bad cash management, and loan defaults by South African businesses in the first year of operation. Furthermore, a barrier to a business's survival is the inability to develop financial strategies that increase liquidity in the first year of operation. Ethnographic strategy found insufficient bookkeeping practices during a business's first year of existence create barriers detrimental to a business's ability to perform and compete. Furthermore, an ethnographic approach was employed to understand that the high failure rate of businesses in South Africa's first year of operation can be attributed to bookkeeping practices, leading to misuse of business resources and inefficient cash management. The population size that was targeted consisted of 311672 small businesses that were registered with the CIPC in South Africa during the first quarter of 2023 and were no more than a year old. To sample a population with a 0.1 per cent chance of selection and to remove bias, essential random sampling was employed. Excel Quantitative Management (QM) software was used for the simple random sample. Using semi-structured interviews, participants could discuss the challenges business owners face in the first year of operation in South Africa.

The study's focus areas were objectively determined by first asking broad questions. In addition, the purpose of clarification was to support participants in answering the questions. Establishing a rapport helped interviewees become more credible by removing the worries and anxiety.

The primary goal of the interviews was to extract qualitative data from the participants to identify the lack of bookkeeping practices contributing to the high failure rate of business during the first year of operation. The voice recordings and transcriptions of the interviews ensured the accuracy of the data. Themes were created by classifying the transcribed input into meaningful groups. The thematic analysis yields topics coded or categorised for further examination. Data was categorised based on the research topic and the study's purpose. The key findings were compiled from themes that surfaced and shared behaviours among participants. Themes that arise from thematic analysis are categorised or classified to facilitate analysis. Emerging themes aligned with the study's goal, and participant patterns combined to form the primary findings. Themes and sub-themes from the literature are integrated into the conversation through deductive coding. Themes from observations and insights show that a lack of bookkeeping practices is detrimental to businesses' competitiveness in South Africa's ability to compete in the first year of operation. Through conceptual analysis, issues for analysis and interpretation arose from the contributing factors that led to first-year business failures in South Africa. Several ethical approaches were adopted during this research study. Furthermore, a ' 'gatekeeper's letter was obtained from incubators.

FINDINGS

This first theme examines the inadequate bookkeeping practices businesses in the first year of operation in South Africa.. Most participants said that in South Africa, insufficient bookkeeping practices during a business's first year of existence creates barriers detrimental to a business's ability to perform and compete. Participants stated that the high failure rate of businesses in South Africa's first year of operation can be attributed to poor bookkeeping practices or the inaccessibility of financial records, which leads to misuse of business resources and inefficient cash management. The inability of business owners to manage short-term challenges like expenses, budgeting, and cash flow by providing pertinent knowledge to support control and monitoring essential for survival in the first year of operation in South Africa was another issue raised by all participants.

The second theme examines the knowledgeable of bookkeeping practices businesses in the first year of operation in South Africa. In terms of bookkeeping practices, the majority of participants said were ignorant. Less than half of the participants said kept financial records in files and on the cloud using Microsoft Spreadsheets. A minority of respondents said they hired a contractor to do bookkeeping practices. Every individual reported having a rudimentary understanding of financial structures, with five indicating they knew nothing about them. Participants also stated that they build a basic financial structure, use the Work Break-down Structure (WBS) tool, and search for ways to reduce overhead and operational costs.

DISCUSSION

According to most participants, insufficient bookkeeping practices makes more difficult for South African businesses to resolve cash flow issues and foresee potential liquidity limitations in the first year of operation. In South Africa, inadequate archiving of manual bookkeeping practices for businesses contributes to the failure in the first year of operation, as explained by Siavhundu, Nyabunze & Chinorwadza (2020). The high failure rate of businesses in South Africa during the first year of existence was partly caused by the insufficiency of human bookkeeping practices. In the first year of operation, businesses in South Africa face the challenge of hiring more skilled workers to handle the business records, which can be costly and negatively impact profitability. Amadhila (2020) argues that a lack of manual bookkeeping practices stems from a lack of business skills and resources. Participants said that in South Africa, business owners did not have access to financial records during the first year of operation, which prevented them from obtaining the information needed to assess the business's competitiveness and operational efficiency. According to the participants, the insufficiency of bookkeeping practices also hinders the ability to set fair prices for goods, explore new markets, and assess the financial stability of South African businesses during the first year of operation. The lack of bookkeeping practices on finance operations, audited accounts, sales, staff costs, owners remunerations, tax returns, marketing, accounting, and credit borrowing from lending institutions has been attributed by Mohammed, Talib & Kohar (2020) to businesses in the first year of operation in South Africa. Ojwang & Shau (2021) highlight that inadequate bookkeeping practices and administration make difficult for business owners to ascertain whether further funding or resources are needed for the business.

Every participant states that poor bookkeeping practices has a negative impact on South African enterprises' first-year financial results. Financial institutions find challenging to assess returns and potential risks when dealing with enterprises in the first year of operation in South Africa due to inadequate bookkeeping practices and accounting information. Furthermore, every participant stated that in South Africa, inadequate bookkeeping practices during a business's first year of operation lead to inadequate financial conditions, inadequate planning, bad spending control, and poor accounts receivable collection. In South Africa, there is also a dearth of record management businesses, which makes difficult to assess performance, find supplier and customer account balances, and project future business performance in the first year of operation. In addition, participants stated there is a dearth of record management businesses in South Africa that struggle in the first year of operation to assess performance, find account balances for suppliers and customers, and project future business performance. According to Nicolas (2022), a lack of bookkeeping practices leads to inadequate financial statements amongst businesses in the first year of existence.

The majority of participants had a rudimentary understanding. Those who said they knew the basics were questioned further to provide more details. A minority stated that the background is intellectual and that the knowledge is insufficient, particularly when comes to challenging to analyse statements. Every participant said that the knowledge was gained via the professional experiences. Furthermore, financial institutions make up the members' professional background or experience. According to every participant, having a rudimentary understanding of finance is necessary solely for appropriate internal bookkeeping practices. The same financial records presented to external parties are insufficient since financial institutions need detailed financial statements that include all financial data. As evidenced by the literature, financial literacy is crucial. Sooriyakumaran, Thrikawala & Pathirawasam (2022) state that because bookkeeping practices are lacking, businesses find difficult to obtain money, particularly from financial institutions, during the first year of operation. Most participants cannot receive funds from investors and financial institutions. Most businesses struggle to get funding in the first year of operation, especially from investors and financial institutions. Participants also indicated that they lacked expertise in the responses. Participants went on to clarify that is difficult to obtain capital, particularly when addressing investors and financial organisations. Due to the lack of expertise, participants reported that keeping track of most financial transactions is challenging, particularly when several occur simultaneously.

Wajebo (2022) reports that the majority of South African businesses in the first year of operation submit unsatisfactory funding proposals to investors, indicating that one of the main barriers to capital accessibility is ignorance. Participants said that balancing the business's assets and liabilities and doing financial projections are also challenging. Due to a lack of knowledge about analysing financial documents, participants reported that is difficult to manage financial resources effectively and that doing so occasionally results in liquidity issues. Otto (2023) contended that most South African enterprises do not adequately comprehend financial statements and the financial needs to raise capital during the first year. The research and comments are consistent in that most businesses in the first year of operation in South Africa lack the fundamental understanding of financial statements and the financial requirements to obtain funding from investors and financial institutions. Every participant was questioned regarding the upkeep of bookkeeping practices, regardless of the level of competence. A small percentage of participants indicated are proficient with single-entry systems despite having rudimentary financial statement analysis experience. Both the single-entry system and one entry at a time have limitations. Participants stated that is difficult to capture more transactions. Participants admitted using Microsoft Excel to keep track of the financial information. The drawback of the Microsoft spreadsheet, as mentioned by participants, is how simple mistakes can be made. According to participants who went into additional detail, bookkeeping practices are maintained and managed in the cloud. Participants who lacked expertise in financial statement analysis were questioned about bookkeeping practices maintenance. In response, everyone said that bank statements and Microsoft Word are used to keep track of business activities.

CONCLUSION

The study emphasised a lack of bookkeeping practices contributing to the high failure rate of business during the first year of operation. Bookkeeping practices assists business owners without financial skills in developing financial records and interpreting financial statements. Bookkeeping practices applies to business owners with substantial capital during start-up and business owners with acquired capital. Bookkeeping practices is a crucial for businesses starting, according to Zahrah Buyong (2020). It is imperative in South Africa to recognise, preserve, and safeguard vital business records while managing all documented business dealings. Another is gathering the necessary paperwork for the business's first year of operation in South Africa, including evidence and references. According to Bullock (2021), bookkeeping practices plays a crucial role in predicting a business's profitability during the first year of operation in South Africa and is considered a performance indicator. The results demonstrated having good internal financial records requires more than just fundamental understanding. Furthermore, is stated that the information obtained through academic background is insufficient, particularly regarding complex assertions. Participants' lack of knowledge regarding the analysis of financial statements revealed that is challenging to deploy financial resources effectively. Participants mentioned that find difficult to establish financial structures since lack this kind of expertise. Typically, inquiries from investors are concerned about the business's financial setup. Both scholarly works and in-person interviews have highlighted the inadequacies of bookkeeping practices subpar business competitiveness in the first year of operation in South Africa.

RECOMMENDATIONS

A statement of financial position, an income statement, and a cash flow statement are the three financial statements that South African business owners should create in the first year of operation to help with record keeping.

Statement of Financial position supports business owners in keeping track of the present assets, owners' equity, and obligations. Owners' equity and business liabilities are listed in the left column of a statement of financial condition. While owners' equity represents the business's capital structure, recording liabilities allows business accounts payable or expenses to be listed. The statement of financial position's right column lists the company's current assets. Business inventory, intangible assets (distinctive competency), account receivables, or money owing to the business should all be included in current business assets.

Statement of Comprehensive Income helps company owners determine the profit margin by tracking all sales, expenses, and costs throughout the first year of operation. Six months must pass between each reporting period's profit or deficit. The income statement's first row shows the sales revenue, followed by the sales costs and all other expenses, including taxes and accounts payable. Any money left over after deducting all costs from sales revenues is known as retained earnings for the company. This amount is net profit after taxes. It is intended to refinance the firm using the retained earnings.

The statement of Cash flow significantly impacts figuring out the business's liquidity. All cash inflows and outflows must be documented during the first year of business operation. Cash flow to shareholders, lenders, and assets should all be included in the cash flow statement. Liabilities must be subtracted from current assets to calculate net working capital.

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