Should SMEs invest in long term assets?

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Could you be too ambitious in your plan to invest in long term assets in your small business?

This is a question that is probably more difficult to answer and only time can tell whether the investment was worthwhile.

Mostly the decision to invest in fixed assets is based on the expectation that this long lasting investment will result in the continuous production of sustainable income and cash flow.

According to Geoffrey Injeni the financial and accounting lecturer at Strathmore Business School, long term assets are the productive assets of a company which are more expensive and complex and thus, require a lot of scrutiny before acquisition.

"When we refer to long term assets in accounting, we generally focus on the fixed assets of a business such as land, buildings, equipment, furniture and vehicles. However, the term "long term assets" also refers to investments in tangibles and any other assets that will not be turned into cash within one year," he says.

In accounting we also have the current assets of a company which are those assets that can be turned into cash within a year, Injeni says, adding the current liabilities are those obligations that are expected to be paid in one year.

"The long term assets of a company by contrast, are those assets that are not expected to be converted to cash within the next 12 months," he says.

This makes managing of these assets more different from managing the more liquid assets.

"We are concerned with how to make long term assets productive and to keep them generating revenues for the company. This relates to maintenance management and the assurance that the productive equipment is kept in good working order," he says.

Investments in fixed assets that do not generate enough revenue serve as an early warning of financial difficulty.

Injeni gives a classic example of Kenya Airways (KQ), a big local airline which is struggling with long term debt amid the challenges facing the aviation industry ranging from expensive fuel, intense competition, terrorism threat and the Ebola epidemic which have impacted global travel.

KQ took massive debt to finance the acquisition of modern planes in 2013 and 2014 and its now in a tight cash flow problem due to the challenges in its business environment.

But KQ chief executive officer Mbuvi Ngunze is quick to say "Only time will tell if we were ambitious in our plans."

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