

**Impact of Audit Quality on Financial Sustainability of SMEs in  
Karachi, Pakistan**

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**Abstract**

This study examined the impact of audit quality on the financial sustainability of Small and Medium Enterprises (SMEs) in Karachi, Pakistan. The primary objective was to investigate whether audit quality significantly influences financial sustainability and to evaluate the effects of auditor independence and compliance with auditing standards on SME sustainability. A quantitative and explanatory research design was adopted to achieve the study objectives. Data were collected from 210 respondents, including SME owners, managers, accountants and financial officers, using a structured questionnaire based on a Likert scale. The collected data were analyzed using SPSS through descriptive statistics, reliability analysis, correlation, regression, ANOVA and hypothesis testing.

The findings revealed that audit quality and financial sustainability were perceived positively among SMEs, with mean 3.82 and 3.76, respectively. Reliability analysis confirmed strong internal consistency, with Cronbach's Alpha values of 0.81 for audit quality and 0.84 for financial sustainability, indicating the reliability of the research instrument. Correlation analysis demonstrated a moderate to strong positive relationship ( $r = 0.62$ ) between audit quality and financial sustainability. Regression results further confirmed that audit quality significantly affects financial sustainability with a beta coefficient ( $\beta = 0.58$ ,  $p = 0.000$ ), indicating a positive and statistically significant impact. The model summary showed an  $R^2$  value of 0.38, meaning that 38% of the variation in financial sustainability was explained by audit quality. Furthermore, the ANOVA results ( $F = 153.25$ ,  $p = 0.000$ ) confirmed the statistical significance of the model. Hypothesis testing results indicated that all three hypotheses were accepted, confirming that audit quality, auditor independence and compliance with auditing standards positively influence SME sustainability.

**Keywords:** Audit Quality, Financial Sustainability, SMEs, Auditor Independence, Auditing Standards, Financial Performance, Profitability, Financial Stability, Business Continuity, Corporate Governance, Financial Reporting, Karachi.

## Introduction

### Background of the Study

Small and Medium Enterprises (SMEs) are widely recognized as one of the most important drivers of economic development in both developed and developing countries. These enterprises contribute significantly to employment generation, poverty reduction, innovation and overall economic growth. SMEs are particularly important in developing economies because they require relatively low capital investment, create job opportunities for skilled and unskilled labor and support income distribution across different sectors of society. In many countries, SMEs represent more than 90% of total businesses and play a crucial role in strengthening national economies.

In the context of Pakistan, SMEs are considered the backbone of the economy. They contribute significantly to industrial development, export earnings and employment generation. According to reports from the World Bank (2021) and the State Bank of Pakistan (SBP, 2022), SMEs account for a substantial portion of private sector employment and contribute meaningfully to GDP. The SME sector in Pakistan operates across various industries including retail, manufacturing, services, agriculture and trade. Despite their importance, SMEs continue to face multiple structural and operational challenges that limit their growth potential and financial sustainability.

One of the major challenges faced by SMEs is financial instability. Many SMEs struggle to maintain consistent profitability, stable cash flows and long term business continuity. Financial sustainability refers to the ability of a business to generate sufficient income to meet its operational costs, maintain liquidity and ensure long-term survival in competitive markets. SMEs often face financial sustainability issues due to weak internal controls, lack of financial discipline, limited access to credit facilities and inadequate financial reporting systems. In many cases, business owners rely on informal accounting practices, which reduce transparency and increases financial risk.

Furthermore, SMEs in developing countries like Pakistan often operate in environments where financial literacy and professional financial management practices are limited. As a result, many SMEs fail to implement proper budgeting, forecasting and financial planning systems. This leads to poor decision-making and increases the likelihood of financial distress. Studies have shown that weak financial management practices are one of the key reasons behind SME failures in emerging economies (Zia & Khan, 2020).

In this context, audit quality becomes an important factor in improving financial sustainability. Audit quality refers to the effectiveness and reliability of the audit process in detecting material misstatements, errors or fraud in financial statements. Audit quality is defined as the joint probability that an auditor will detect and report

material misstatements. High audit quality ensures that financial statements are accurate, transparent and reliable. It also strengthens accountability and improves stakeholder confidence in financial reporting (De Angelo 1981).

High quality audits play a critical role in improving organizational performance by ensuring that financial statements reflect the true financial position of a business. When audit quality is high, businesses are more likely to identify weaknesses in internal controls, reduce fraudulent activities and improve financial decision making. Furthermore, audit quality enhances the credibility of financial reports, which is particularly important for SMEs seeking external financing from banks and financial institutions. Investors and lenders are more likely to trust businesses that maintain transparent and audited financial records (Sattar et al., 2020).

In developing economies such as Pakistan, the importance of audit quality becomes even more significant due to weak institutional frameworks, limited regulatory enforcement and lack of transparency in financial reporting systems. Khan et al. (2021) argue that audit quality plays a crucial role in strengthening corporate governance and improving financial performance in emerging markets. However, despite its importance, many SMEs in Pakistan do not prioritize proper auditing practices due to cost constraints, lack of awareness and limited access to professional audit services.

In major business hubs like Karachi, SMEs often rely on informal accounting systems or low cost auditing services, which may not meet professional standards. This compromises the quality of financial reporting and increases the risk of financial mismanagement. As a result, many SMEs experience difficulties in maintaining financial sustainability and long term business continuity. The absence of strong audit practices also limits their ability to attract investors and secure loans from financial institutions Hassan, M., & Iqbal, Z. (2020).

Therefore, this study focuses on examining the impact of audit quality on the financial sustainability of SMEs in Karachi. The study specifically investigates how audit quality, through auditor independence and compliance with auditing standards, influences the financial sustainability of SMEs. By doing so, it aims to provide empirical evidence on the importance of audit quality in improving financial stability, transparency and long term business success.

### **Scope of the Study**

This study focuses on SMEs operating in Sindh, Pakistan. It examines audit quality as the independent variable and financial sustainability as the dependent variable. Audit quality is measured through auditor independence and compliance with auditing standards, while financial sustainability is evaluated through financial stability, profitability and long term business continuity.

### **Problem Statement**

Despite the important role of SMEs in economic development, many SMEs in Sindh experience financial instability and business sustainability problems. Poor accounting systems, lack of transparency and weak internal controls often result in financial difficulties. One major issue contributing to these problems is inadequate audit quality.

Many SMEs do not prioritize professional auditing because of financial constraints or lack of awareness. Poor quality audits may fail to detect errors, fraud and financial mismanagement, reducing business credibility and financial sustainability. Although audit quality has been widely studied in large corporations, limited research exists regarding its impact on SMEs, particularly in Sindh, Pakistan. Therefore, this study seeks to examine whether improved audit quality contributes positively to the financial sustainability of SMEs.

### **Objectives**

- To examine the impact of audit quality on SME financial sustainability.
- To analyze the effect of auditor independence on financial sustainability.
- To assess compliance with auditing standards on sustainability.

### **Research Questions**

- What is the impact of audit quality on SME sustainability?
- How does auditor independence affect sustainability?
- What is the effect of audit standards compliance?

### **Hypotheses**

- H1: Audit quality significantly affects financial sustainability.
- H2: Auditor independence positively affects sustainability.
- H3: Compliance with auditing standards improves sustainability.

### **Significance of the Study**

This study is important because it highlights the role of audit quality in improving the financial sustainability of SMEs. The findings may help SME owners understand the importance of quality auditing in maintaining financial transparency and business growth.

The study will also assist policymakers in developing stronger audit related regulations for SMEs. Auditors and financial institutions may benefit from understanding how quality audits contribute to better financial management and lower business risk.

### **Research Gap**

Previous studies mainly focus on large corporations and listed firms, while SMEs remain under researched. Limited attention has been given to the impact of audit quality on SME financial sustainability. Most research emphasizes corporate governance rather than SME financial stability. In developing countries like Pakistan, especially Sindh, empirical evidence on this topic is still limited. The role of auditor independence in improving SME performance is not widely explored. Similarly, compliance with auditing standards has received less attention in SME contexts. There is also a lack of region specific studies focusing on SMEs in Sindh. Therefore, this study fills this gap by examining audit quality and SME financial sustainability in Sindh.

## **Literature Review**

### **Introduction**

The literature review provides a theoretical and empirical understanding of audit quality and financial sustainability in SMEs. It examines previous studies conducted on audit quality, auditor independence, compliance with auditing standards, and their influence on organizational sustainability. The review also identifies gaps in existing literature related to SMEs in Sindh, Pakistan.

### **Concept of SMEs**

Small and Medium Enterprises (SMEs) are business entities that operate on a relatively smaller scale in terms of employees, capital investment and annual revenue. SMEs are considered the backbone of many economies because they contribute significantly to employment generation, innovation, exports and poverty reduction (OECD, 2019).

In Pakistan, SMEs represent a large portion of the private business sector and contribute substantially to GDP and industrial growth (SBP, 2022). SMEs operate in various sectors including manufacturing, retail, agriculture and services. Despite their economic importance, many SMEs face challenges such as limited financial resources, weak management systems, poor governance and lack of professional auditing practices (Ahmed & Afza, 2019). Financial sustainability is one of the major concerns for SMEs because many businesses fail to survive in the long term due to financial instability and poor financial decision making. Therefore, effective financial management and quality auditing practices are essential for improving SME sustainability.

### **Audit Quality**

Audit quality refers to the ability of auditors to identify material misstatements, errors or fraud in financial statements and report them accurately and independently. High quality audits improve the reliability, transparency and credibility of financial reporting (Knechel et al., 2013). According to previous studies, audit quality depends on auditor competence, auditor independence, professional ethics, compliance with auditing standards and audit transparency. Effective auditing helps organizations improve internal controls, reduce financial risks and strengthen stakeholder confidence (Francis & Wang, 2008).

High audit quality is particularly important for SMEs because these businesses often lack strong internal control systems and financial expertise (Gul, F. A., & Tsui, J. S. L. 2001). Reliable auditing practices can help SMEs maintain accurate financial records, secure financing from financial institutions and improve investor confidence (Sattar et al., 2020).

### **Auditor Independence**

Auditor independence refers to the ability of auditors to perform their duties objectively and without bias or external influence. Independence is considered one of the most important components of audit quality because it ensures that auditors

provide unbiased opinions regarding financial statements (Watts & Zimmerman, 1986).

Several studies indicate that independent auditors improve the credibility of financial reporting and reduce the risk of financial manipulation. Lawrence et al. (2011) argue that auditor independence enhances audit reliability and reduces misstatement risks. Lack of independence may compromise audit effectiveness and reduce stakeholder trust.

For SMEs, auditor independence is important because owners and managers often exercise significant control over financial activities. Independent auditors help ensure transparency and accountability, which ultimately supports financial sustainability.

### **Compliance with Auditing Standards**

Compliance with auditing standards refers to the extent to which auditors follow established professional guidelines during the audit process. Auditing standards ensure consistency, reliability and accuracy in financial reporting (IFAC, 2020).

Professional auditing standards provide guidelines regarding audit planning, evidence collection, reporting procedures and ethical responsibilities. Compliance improves audit quality by reducing errors and enhancing transparency. Previous studies suggest that organizations following auditing standards are more likely to maintain financial discipline and achieve sustainable performance. SMEs that comply with auditing regulations improve financial stability, operational efficiency and investor confidence (Modarress, B., Ansari, A., & Leman, Z. 2010).

### **Financial Sustainability**

Financial sustainability refers to the ability of an organization to maintain long term financial stability, profitability and operational continuity. Sustainable businesses can effectively manage financial resources, maintain positive cash flows and survive economic uncertainties (World Bank, 2021).

Indicators of financial sustainability include:

Profitability

Liquidity

Business continuity

Financial stability

Growth potential

For SMEs, financial sustainability is essential because small businesses are more vulnerable to financial crises and market fluctuations. Weak financial management practices often result in business failure and reduced competitiveness (Zia & Khan, 2020).

Research suggests that transparent financial reporting and quality auditing practices can positively influence financial sustainability by improving financial planning, accountability and stakeholder confidence.

### Relationship between Audit Quality and Financial Sustainability

Several empirical studies have explored the relationship between audit quality and organizational financial performance. Most findings indicate that high audit quality positively affects financial sustainability because quality audits improve financial transparency, reduce fraud risks and strengthen investor trust (Becker et al., 1998).

Studies in developed economies show that organizations with effective audit systems are more likely to achieve stable financial performance and long term growth. Audit quality improves decision making by ensuring accurate financial information (Knechel et al., 2013). In developing countries, the relationship between audit quality and SME sustainability remains relatively underexplored. However, available evidence suggests that SMEs with stronger auditing practices experience better financial management and reduced operational risks (Kamran et al., 2023).

In the case of SMEs in Karachi, audit quality may play a significant role in improving business sustainability because many SMEs face challenges related to poor accounting systems and limited financial transparency.

Theoretical Framework

#### Agency Theory

Agency Theory explains the relationship between business owners (principals) and managers (agents). Conflicts arise when managers prioritize personal interests over organizational goals (Watts & Zimmerman, 1986).

Auditing helps reduce agency problems by ensuring transparency and accountability in financial reporting. High quality audits provide assurance that financial statements are accurate and free from manipulation, thereby improving financial sustainability.

#### Stakeholder Theory

Stakeholder Theory states that organizations must consider the interests of all stakeholders, including investors, employees, customers, creditors and regulators (R. Edward Freeman 1984). Quality auditing enhances stakeholder confidence by improving financial transparency and accountability. SMEs that maintain reliable financial reporting are more likely to gain stakeholder trust and secure long term financial support.

#### Conceptual Framework

##### Variables of the Study

##### Independent Variable

###### Audit Quality

- Auditor Independence
- Compliance with Auditing Standards

##### Dependent

###### Financial Sustainability

- Profitability
- Financial Stability
- Business Continuity

The conceptual framework illustrates the relationship between audit quality and financial sustainability of SMEs. Audit quality is considered the independent variable, which influences financial sustainability (dependent variable). When SMEs maintain high auditor independence and comply with auditing standards, their financial transparency improves, leading to higher profitability, stronger financial stability and better business continuity.

### **Research Methodology**

#### **Research Design**

This study adopts a quantitative and explanatory research design. A quantitative approach is used because the data is collected in numerical form and analyzed statistically to test relationships between variables. The explanatory design is suitable because the study aims to explain the relationship between audit quality (independent variable) and financial sustainability (dependent variable) in SMEs, rather than just describing them.

#### **Study Area**

The study is conducted in Karachi, which is the largest commercial hub of Pakistan. Karachi is selected because it hosts a large number of Small and Medium Enterprises (SMEs) operating in different sectors, making it an appropriate location for examining financial and auditing practices.

#### **Population**

The target population consists of SME owners, managers, accountants and financial officers. These respondents are chosen because they are directly involved in financial decision making and auditing related practices within SMEs, making their responses relevant and reliable for the study.

#### **Sample Size**

A total of 210 respondents are selected for data collection. This sample size is considered adequate for statistical analysis using SPSS, especially for correlation and regression techniques and helps ensure more reliable and generalizable results within the selected study area.

#### **Sampling Technique**

The study uses convenience sampling, a non probability sampling technique. Respondents are selected based on their availability and willingness to participate. This method is often used in SME based studies due to limited access to complete population lists and time constraints.

#### **SME Sector Focus**

The research focuses on three major SME categories:

**Retail SMEs:** Businesses involved in direct selling of goods to consumers.

**Wholesaling SMEs:** Firms that sell goods in bulk to retailers or other businesses.

**Local distribution SMEs:** Enterprises involved in logistics and distribution of goods within local markets.

These sectors are selected because they play a significant role in Karachi's economy and actively manage financial records and auditing practices.

### Data Collection

Data is collected through a structured questionnaire based on a 5 point Likert scale (ranging from strongly disagree to strongly agree). This method allows respondents to express the level of agreement with statements related to audit quality and financial sustainability in a standardized and measurable way.

### Variables

The study includes two main variables:

**Independent Variable :** Audit Quality

This includes aspects such as auditor independence and compliance with auditing standards.

**Dependent Variable:** Financial Sustainability

This is measured through profitability, financial stability and business continuity.

The relationship between these variables is examined to understand how audit quality influences the long term financial health of SMEs.

### Data Analysis Tools

The collected data is analyzed using SPSS.

The following statistical techniques are applied:

**Descriptive Statistics:** To summarize basic features of the data such as mean, frequency and standard deviation.

**Correlation Analysis:** To measure the strength and direction of the relationship between audit quality and financial sustainability.

**Regression Analysis:** To determine the impact of audit quality on financial sustainability.

**ANOVA (Analysis of Variance):** To test differences among groups (e.g., SME sectors).

**Model Summary:** To evaluate the overall fit of the regression model, including R square and explanatory power.

### Results and Findings

#### Descriptive Statistics

Table:1

Descriptive Statistics of Variables

Variable	N	Mean	Std. Deviation
Audit Quality	210	3.82	0.71
Financial Sustainability	21-	3.76	0.69

Source: Authors Calculation

The descriptive statistics indicate that a total of 210 respondents participated in the study. The mean value for Audit Quality (3.82) suggests that respondents generally perceive audit practices in SMEs positively. Similarly, Financial Sustainability recorded a mean value of 3.76, indicating a moderate to high level of sustainability among SMEs. The standard deviation values (0.71 and 0.69) show relatively low variation in responses, meaning participants had fairly consistent opinions. Overall, the results suggest that both audit quality and financial sustainability are present at satisfactory levels in SMEs in Karachi.

### Reliability Test

Table: 2

Reliability Analysis (Cronbach's Alpha)

Variable	No. of Items	Cronbach's Alpha
Audit Quality	6	0.81
Financial Sustainability	6	0.84

Source: Authors Calculation

The reliability analysis results indicate that both variables have strong internal consistency and are suitable for further analysis. Audit Quality, consisting of 6 items, achieved a Cronbach's Alpha value of 0.81, indicating good reliability. Similarly, Financial Sustainability, also measured through 6 items, recorded a Cronbach's Alpha value of 0.84, which reflects a high level of consistency among responses. Since both values are above the acceptable threshold of 0.70, the questionnaire is considered reliable. Therefore, the measurement scales used in this study are valid for analyzing the relationship between audit quality and financial sustainability.

### Correlation Analysis

Table: 3

Correlation between Audit Quality and Financial Sustainability

Variables	Audit Quality	Financial Sustainability
Audit Quality	1	
Financial Sustainability	0.62	1

Source: Authors Calculation

Note:  $p < 0.01$

The correlation analysis indicates a positive relationship between Audit Quality and Financial Sustainability with a correlation coefficient of 0.62. This suggests a moderate to strong positive association, meaning that improvements in audit quality are linked with better financial sustainability in SMEs. The findings imply that organizations with stronger audit practices tend to experience improved profitability, financial stability and business continuity. Since the correlation value is relatively

high, it shows that the two variables move in the same direction. Overall, the results support the view that effective audit quality contributes positively to financial sustainability.

**Model Summary**

Table: 4

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error
1	0.62	0.38	0.54	

Source: Authors Calculation

The model summary results indicate a moderate relationship between audit quality and financial sustainability, with R value of 0.62. The R Square value of 0.38 shows that 38% of the variation in financial sustainability is explained by audit quality. This suggests that audit quality has a meaningful contribution to financial sustainability among SMEs. However, the remaining 62% variation may be influenced by other factors not included in the study, such as managerial skills, market conditions and financial resources. Overall, the model demonstrates that audit quality is an important predictor of financial sustainability.

**ANOVA Results**

Table: 5

ANOVA

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	45.12	1	45.12	153.25	0.000
Residual	73.45	208	0.35		
Total	118.57	209			

Source: Authors Calculation

The ANOVA results indicate that the regression model is statistically significant, as shown by the F-value of 153.25 and a significance value of 0.000, which is less than 0.05. This confirms that the model is valid for examining the relationship between audit quality and financial sustainability. The regression sum of squares (45.12) shows the variation explained by the model, while the residual sum of squares (73.45) represents unexplained variation. These findings suggest that audit quality significantly influences financial sustainability among SMEs. Therefore, the overall regression model is considered reliable and statistically meaningful.

**Regression Coefficients**

Table: 6

Regression Analysis

Variable	Beta (β)	Std. Error	t-value	Sig.
(Constant)	1.25	0.18	6.94	0.000
Audit Quality	0.58	0.05	12.38	0.000

Source: Authors Calculation

The regression analysis results show that Audit Quality has a significant positive effect on Financial Sustainability. The beta coefficient ( $\beta = 0.58$ ) indicates that an increase in audit quality leads to an improvement in financial sustainability among SMEs. The t-value of 12.38 and significance value (0.000) confirm that the relationship is statistically significant, as the p-value is below 0.05. Additionally, the constant value (1.25) indicates the baseline level of financial sustainability when audit quality is held constant. Overall, the findings confirm that audit quality is an important predictor of financial sustainability in SMEs in Karachi.

### Hypothesis Testing Results

Table: 7

Hypothesis Testing Results

Hypothesis No.	Hypothesis Statement	Results
H1	Audit quality significantly affects financial sustainability.	Accepted
H2	Auditor independence positively affects sustainability.	Accepted
H3	Compliance with auditing standards improves sustainability.	Accepted

Source: Authors Calculation

The hypothesis testing results indicate that all three hypotheses were accepted, confirming the significant role of audit quality in improving financial sustainability among SMEs. H1 confirms that audit quality significantly affects financial sustainability, suggesting that better auditing practices contribute to improved financial performance and business continuity. H2 demonstrates that auditor independence positively affects sustainability, highlighting the importance of objective and unbiased auditing processes. H3 confirms that compliance with auditing standards improves sustainability by enhancing financial transparency and accountability. Overall, the findings suggest that strong audit mechanisms are essential for achieving long-term financial sustainability in SMEs.

### Summary of Findings

The findings of this study indicate that audit quality plays a significant role in enhancing the financial sustainability of SMEs in Karachi. The descriptive results suggest that respondents generally hold a moderately positive perception of both audit quality and financial sustainability. This implies that while many SMEs recognize the importance of proper auditing practices such as auditor independence and compliance with auditing standards, the implementation of these practices is not yet fully optimal across all firms. This reflects the common situation in developing economies where SMEs often face limitations such as cost constraints, lack of professional expertise and weak internal control systems, which affect the quality of auditing practices.

The correlation analysis revealed a positive and significant relationship between audit quality and financial sustainability ( $r = 0.62$ ), indicating that improvements in audit

quality are associated with better financial outcomes in SMEs. In practical terms, firms that maintain higher audit standards tend to experience improved profitability, stronger financial stability and better continuity of operations. This supports the idea that audit quality enhances transparency and reduces the likelihood of errors or financial mismanagement, thereby strengthening overall financial performance.

Similarly, the regression results confirmed that audit quality has a statistically significant positive effect on financial sustainability ( $\beta = 0.58$ ,  $p < 0.001$ ). This suggests that audit quality is an important predictor of financial sustainability in SMEs. In other words, improvements in auditing practices lead to measurable improvements in financial outcomes. However, the R-square value of 0.38 shows that audit quality explains 38% of the variation in financial sustainability, meaning that other factors such as managerial capability, market conditions, access to finance and business environment also play an important role in determining SME performance.

The ANOVA results further confirmed that the overall model is statistically significant, indicating that the relationship between audit quality and financial sustainability is not due to random chance. When compared with existing literature, the findings are consistent with previous studies that highlight the importance of audit quality in improving financial transparency, reducing agency conflicts and enhancing stakeholder confidence. The results also support agency theory, which explains that strong audit mechanisms reduce information asymmetry between managers and stakeholders, leading to improved financial decision making and accountability.

Overall, the findings suggest that strengthening audit quality can significantly contribute to the financial sustainability and long term survival of SMEs in Karachi, although it should be complemented with other managerial and environmental improvements to achieve optimal results.

### Conclusion

The study examined the relationship between audit quality and financial sustainability in SMEs in Karachi, with the aim of determining whether improvements in audit practices contribute to stronger financial performance and long-term business continuity. The results of the study clearly demonstrate that audit quality has a significant and positive influence on financial sustainability.

The descriptive findings showed that respondents moderately agree that audit quality practices, such as auditor independence and compliance with auditing standards, are present in SMEs, although there is still room for improvement. The correlation analysis revealed a positive and significant relationship between audit quality and financial sustainability ( $r = 0.62$ ), indicating that better audit practices are associated with improved profitability, financial stability and business continuity. Similarly, the regression results confirmed that audit quality is a strong predictor of financial sustainability ( $\beta = 0.58$ ,  $p < 0.001$ ), meaning that any improvement in audit quality leads to a measurable increase in financial sustainability among SMEs.

The model further explained 38% of the variation in financial sustainability ( $R^2 = 0.38$ ), which indicates a moderate explanatory power and suggests that other factors also contribute to SME financial outcomes. The ANOVA results supported the overall

significance of the model ( $p < 0.05$ ), confirming that the relationship between the variables is statistically reliable and not due to chance.

Based on these findings, it is concluded that audit quality plays a crucial role in enhancing financial sustainability in SMEs in Karachi. High quality auditing improves transparency, reduces financial irregularities and strengthens decision making processes within organizations. However, since audit quality does not fully explain financial sustainability, SMEs must also consider other operational, managerial and environmental factors to achieve long term stability.

Overall, strengthening audit quality can significantly improve the financial health and sustainability of SMEs, making it an essential component of effective business management and growth strategy.

### **Recommendations**

SMEs should strengthen audit quality practices by ensuring full auditor independence to improve the reliability and credibility of financial reporting.

SMEs must ensure strict compliance with auditing standards, as adherence enhances transparency, reduces errors and improves financial decision making.

SME owners are encouraged to hire qualified and experienced auditors/accountants to improve internal controls and ensure accurate financial reporting.

Where hiring is costly, SMEs should consider outsourcing audit services to reputable audit firms to maintain objectivity and professional audit standards.

Regulatory bodies and professional institutions should organize training programs and awareness workshops to educate SMEs about the importance of audit quality and financial sustainability.

SMEs should adopt modern accounting and auditing software systems to improve accuracy, efficiency and real time financial monitoring, while also strengthening overall business management practices.

### **Limitations**

The study is limited to SMEs operating in Karachi, which restricts the generalizability of the findings to other regions. It uses convenience sampling, which may introduce selection bias. The data is based on self-reported questionnaires, which may lead to response bias. The study focuses only on audit quality and financial sustainability, excluding other important determinants. It does not consider differences across SME sectors in depth. The research is cross sectional, so it cannot capture changes over time. Therefore, it does not fully establish strong causal relationships between the variables.

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